

# RUSSIAN DESK

## New Regulations for Special Investment Contracts in Russia. SPIC 2.0.

On 2 August 2019 three Federal Laws were signed by the President of Russia, which set a new legal framework for an important support tool for investment projects – special investment contracts (hereinafter referred to as “SPIC”).

Below we comment on the most important legislative amendments that are relevant to the practical implementation of the special investment contracts.

### 1. LONG-TERM SUBSIDIES FOR INVESTMENT PROJECTS

The new version of Article 78 of the Budget Code of the Russian Federation now allows for obtaining subsidies from federal, regional or local budgets for a longer term than just one budgetary period (one year) for projects implemented under SPIC. Thus, the budgetary subsidies can be made available to investors on a long-term basis, which is particularly important for large investment projects. The application of long-term subsidies should help to reduce the cost of products manufactured under SPIC, which in its turn shall make the prices of SPIC products more competitive.

### 2. SPIC CONTENT AND CONCLUSION PROCEDURE

The Federal Law “On Industrial Policy in the Russian Federation” (hereinafter “**Industrial Policy Law**”) has been supplemented with a chapter dedicated to special investment contracts, whereas some of the earlier basic principles have been changed.

In the previous version of the Industrial Policy Law, the subject matter of the special investment contract was the creation, modernization and commencement of the production of industrial goods. The new version introduces the term “technologies”. Thus, the focus is not just on industrial investments but on high-tech industrial projects. Technologies include both legally protected and unprotected results of intellectual activity. SPIC shall be concluded for the purpose of development (acquisition) and use of “modern technologies”, i.e. technologies that enable the production of globally competitive goods. The list of such technologies has yet to be determined by the Government of the Russian Federation.

SPICs may be concluded under the new rules until the end of 2030. Below we present an overview of the main new provisions.

### 2.1. ABOLITION OF THE MINIMUM INVESTMENT THRESHOLD

The minimum investment threshold was previously 750 million rubles. When the draft law was being considered, it was proposed to increase it to 1 billion rubles. However, finally it was decided to abolish this requirement and to focus on technologies.

### 2.2. EXTENSION OF THE SPIC TERM

Previously, the maximum SPIC duration was limited to 10 years. The new rules have considerably extended the contract term: now special investment contracts may be concluded for a period of up to 15 years where the amount of investments volume is less than 50 billion rubles excluding VAT (approximately EUR 680 m.), or for a period of up to 20 years where the amount of investments exceeds 50 billion rubles excluding VAT.

### 2.3. STABILITY OF ECONOMIC CONDITIONS

Special attention should be paid to the new article 18.4 of the Law which introduces a provision concerning the protection of investors from the legislative changes.

According to the general rule, legislative changes that have been passed after the conclusion of a SPIC and that may affect the project implementation shall not apply. However, there is a number of restrictions:

- the safeguard clause shall only be applicable if a special procedure applied to SPIC parties on the date of the conclusion of the contract in accordance with the effective Russian legislation;
- the clause shall not apply to any laws that (1) have been adopted in pursuance of international treaties of the Russian Federation;

ration and (or) Eurasian Economic Union legal acts, and/or (2) relate to fundamental constitutional values and ensure state security.

The Law also contains direct references to provisions of regional, local and fiscal legislation with regard to the application of the clause on the legal provisions stability. At the regional level, the same rules on the stability of the legal provisions for investors generally apply. However, the situation with local laws is more complicated. If local legislation does not protect investors in the event of changes of rules set therein, the above rules on protection against changes at the local level will not be effective in this case. This fact worsens the transparency of legislation and makes it difficult to protect investors' rights, especially when a local authority acts as a party to a SPIC.

Fortunately, the provisions of the Tax Code of the Russian Federation (hereinafter referred to as the RF Tax Code) which set out the principles of non-increasing the tax burden for investors who implement projects under SPIC, remain effective with minor amendments.

#### 2.4. TENDER PROCEDURE FOR SPIC CONCLUSION

Under the new rules, the investor shall be determined based on the results of a tender. Tenders shall be conducted at the initiative of federal authorities, including in cooperation with regional and local authorities, as well as at the initiative of investors. Basically, tenders shall be open, with the exception of projects for the mass production of industrial goods required for the state security.

SPIC can be concluded without the tender procedure in only two cases:

- i. on the basis of a presidential decree on conclusion of a contract for the purpose of implementation of a project having strategic importance for the economic development or national security, and
- ii. if only one application that meets the legal requirements has been submitted for tender selection.

#### 2.5. ECONOMIC CHARACTERISTICS OF AN INVESTMENT PROJECT

For all investors, a uniform list of compulsory economic conditions which must be fulfilled under a SPIC project (other than those set forth by Government Decree No. 708 of 16.07.2015) now applies. Such conditions include, in accordance with the Industrial Policy Law, the following:

- the amount of manufactured and sold industrial products (in quantitative and monetary terms);
- minimum amount of taxes, duties and social insurance fees which shall be paid by the investor taking into consideration SPIC incentive measures applied;
- number of jobs created in the course of the project implementation.

All the above characteristics must be determined in the contract. In addition, the investor must maintain separate accounting of income and expenses as well as of assets and property rights related to the project implementation if the investor also performs other activities along with the activities under the SPIC.

The SPIC may also contain other conditions that the parties deem essential. This can relate to both economic characteristics of the project and the investor's financial situation.

#### 2.6. CONTROL OVER THE FULFILLMENT OF OBLIGATIONS BY THE INVESTOR

Under the new Article 18.5 of the Law, general control over fulfillment of SPIC by investors shall be exercised both at federal and regional levels under the procedure to be determined by the RF Government and shall involve two types of audits:

- review of documents submitted by the investor to the competent authorities;
- on-site inspections carried out at the industrial production site.

The Government of the Russian Federation shall be provided with an annual summary report on the results of the audits of the projects being implemented in accordance with SPIC.

#### 2.7. LIABILITY UNDER SPIC

The new version of the Law on Industrial Policy contains specific provisions on the liability of the contracting parties in terms of the fulfillment of their obligations under the special investment contracts.

According to the general rule, the parties shall be liable for non-performance or improper performance of their contractual obligations in the form of compensation for the actual damages and payment of contractual penalties in accordance with the provisions of the Law and SPIC. Any lost profits in connection with non-performance or improper performance of the SPIC obligations shall not be reimbursed to the parties.

The liability of the investor is limited to the total value of the incentives granted thereto. The mandatory tax amounts not paid as a result of an application of the tax incentives under SPIC and (or) any subsidies received shall be paid and shall be deducted from the amount of actual damages to be compensated by the investor in the event of non-performance or improper performance of contractual obligations.

If state support measures cannot be applied, the investor shall be entitled to terminate the special investment contract. The procedure for compensation of actual damages to the investor in this case shall be determined in the contract.

When concluding a SPIC, the investor should agree on the consequences in case the investor incurs losses if the other party fails to ensure the stability of economic conditions. One has to take into account that any income not received by the investor for this reason (lost profits) shall not be compensated.

Claims by the tax and/or customs authorities regarding the payment of taxes, duties, contributions, customs duties, fines, interest and penalties shall not be deemed a violation of the SPIC conditions. In case a state body claims compensation for actual damages in connection with the breach of the SPIC obligations by the investor, such amounts shall not be included in the actual damages.

Special attention is to be paid to the sanctions for non-performance by the investor of the essential SPIC obligations. The sanctions depend on the extent of achievement of the project indicators as well as on the fulfillment of other essential obligations by the investor, namely:

- If the investor has breached less than 50 percent of their obligations regarding investment amount or timelines, or if the production output or other economic indicators have not been achieved or the obligation to maintain separate accounting is violated, whereas these violations were not caused by non-fulfillment by the other contracting party of the obligation to grant support measures, the investor shall pay the penalty in the amount and according to the procedure determined in the SPIC upon request of the other party.
- If the investor has failed to meet the target investment amount or timelines by more than 50 percent, or failed to fulfill their obligations to develop and/or acquire exclusive rights to the technology, technology implementation and use of these rights for the mass production of industrial goods, the other contracting party shall be entitled to withdraw from the SPIC without judicial proceedings and demand compensation for the actual damages by the investor.

In addition, the public party to SPIC shall be entitled to withdraw from the SPIC without judicial proceedings and without reimbursement of actual damages if the investor was declared insolvent (bankrupt).

### 3. TAX INCENTIVES FOR INVESTORS

Federal Law No. 269-FG dated 2 August 2019 amended tax legislation to optimize the application of profit tax incentives by investors. On 2 September 2019 a new chapter in the Tax Code RF entered into force which sets out specific regulations for SPIC parties.

From 1 January 2020, the provisions of Art. 25.9 part 1 of the RF Tax Code, according to which the parties in SPIC were treated equally to parties to regional investment projects, will expire. Instead of them, the RF Tax Code introduces new rules regarding the application of tax rates by SPIC parties. Thus, SPIC parties may apply reduced rates of profit tax as follows:

- with respect to all profits, if the income from the sale of products manufactured under SPIC constitutes at least 90 percent of all income taken into account for determination of the tax base (excluding exchange rate gains); or
- with respect to profits from the activity under SPIC, provided that the respective profits (expenditures) and profits (expen-

ditures) generated by other activities have been accounted separately.

The method for determining a tax base shall be stated in the company's accounting policy and must not be changed during the entire period for which the SPIC was concluded. Therefore, it is important for investors to plan their future activities as early as when they prepare to conclude SPIC.

Starting from 2020, Art. 284 of the Tax Code RF will be supplemented with point 1.14, according to which the zero tax rate will be set explicitly for SPIC parties in relation to the profits tax payable to the federal budget. Until then, a reduced tax rate shall apply to the parties to regional investment projects, to which SPIC parties were treated equally. The reduced rate will be applied according to the following rules:

- The exemption from the payment of the federal tax part shall apply for the same period for which the incentive for the respective regional tax part is granted.
- The tax rate for the profits tax payable to the regional budget may be reduced to 0 percent for SPIC parties on the basis of regional laws.
- The reduced federal and regional tax rates shall apply until the SPIC termination, but in any case no longer than when the total amount of budget expenses and income not received by the state as a result of provision of incentives under SPIC exceeds 50 percent of the investment amount specified in the SPIC.

The transitional provisions stipulate that the reduced corporate income tax rates set by regional laws for companies that have concluded a SPIC without the participation of the Russian Federation before 1 January 2019 will apply until the relevant agreements are terminated.

The experts of BEITEN BURKHARDT will be pleased to advise you on all matters relating to special investment contracts and setting up production in Russia, as well as on all other legal and tax issues.



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