

Legal analysis of Federal law dated 13.07.2015 N 212-Φ3 “On the free port of Vladivostok”: Important points, problems, general assessment (hereinafter referred to as the Law)

I. Target setting

Study of basic provisions of the Law, their analysis and brief idea within this Memorandum. Getting an idea of the availability of correlation (interrelation) between provisions of the Law and tasks previously set (attraction of additional investments in the region, improvement of an investment climate etc.). Reveal of problematic issues. Conclusions and recommendations.

II. Statistic data and definition of the free port of Vladivostok

Commencement of the document - 12.10.2015 (except particular provisions which will be specified additionally).

The *free port of Vladivostok* (hereinafter referred to as the FP) is understood as the part of the territory of Primorsky region in which according to the Law and other federal laws measures of the state support of business activity are established.

The free port of Vladivostok includes territories of 15 municipal entities in Primorsky region (article 4 of the Law)¹.

The free port of Vladivostok is created for 70 in view of a possible prolongation of the said term.

III. Management bodies

1) *Supervisory Board - collective management body of the FP in view of wide powers:*

- a) Defines types of business activity
 - prohibited for the FP resident;
 - not supported by the state.
- b) Coordination functions with government officials;
- c) Monitoring of economic processes;
- d) Other.

Composition formation is a rather complex process with an allowance for its approval by the Government of the Russian Federation.

2) *The authorized federal body (AFB) – a body coordinating activities on implementation of state programs and federal target programs in the territory of the Far-Eastern Federal District:*

- a) Keeps the register of the FP residents and proves a procedure of keeping the register;
- b) Controls a managing company;

¹ The free port of Vladivostok includes the territories of municipal entities of Primorsky region: Artem City Area, Vladivostok City Area, Bolshoy Kamen City Area, Nakhodka City Area, Partizansk City Area, Spassk-Dalny City Area, Ussuriisk City Area, Nadezhdinsky Municipal District, Shkotovo Municipal District, Oktyabrsky Municipal District, Olga Municipal District, Partizansk Municipal District, Pogranichny Municipal District, Khasansky Municipal District, Khankaisky Municipal District, including territories and water areas of seaports located in the territories of these municipal entities

- c) Provides the work of the Supervisory Board;
- d) Provides, as agreed upon with the Supervisory Board of the free port of Vladivostok, plots of land federally owned;
- e) Other.

Among other issues, it is entitled to delegate its powers to the managing company.

3) *The managing company* – a company (joint-stock company) with a 100% authorized capital of the Russian Federation determined within 473-ΦЗ² by the Government of the Russian Federation in order to ensure the operation of territories of priority social and economic development in the territory of the Far-Eastern Federal District, or its subsidiary company:

- a) assesses the applications and accompanying documents with due regard for the right to conclude an *agreement on activity* with a FP resident;
- b) exercises control over the *compliance with agreements on activity* by residents of the free port of Vladivostok;
- c) Other.

4) *The public council of the free port of Vladivostok* – an elective entity formed among the representatives of public organizations, all-Russian associations of trade unions, all-Russian employers' associations, public consumers' associations, scientific organizations, expert organizations and natural persons (refer to Section VI. Problematic issues).

IV. FP resident

A resident of the free port of Vladivostok is understood to be (1) an individual entrepreneur or a legal entity being a commercial organization, (2) which are officially registered in the territory of the free port of Vladivostok in accordance with the Russian legislation (except state and municipal unitary enterprises), which (3) hereunder concluded an *agreement on activity* and (4) are incorporated in the *register of residents of the free port* of Vladivostok.

The said agreement is concluded with the Managing Company in view of a need for a compliance of the resident himself and his documentation with numerous criteria (refer to Section VI. Problematic issues). An entry to the register is made by the AFB.

As one of the main criteria, the Law points to the implementation of agreed investment by the resident.

The resident of the free port of Vladivostok is not entitled to delegate his rights and obligations to another person under the *agreement on activity*, which fully complies with chapter 24 of the Russian Civil Code.

V. Measures of state support

1) Special options for **minimization of control of business** of the resident within the FP by public officials, in particular, concerning the dates of audits and a necessity of additional

² **Note.** Federal law dated December 29, 2014 N 473-ΦЗ “On territories of priority social and economic development in the Russian Federation”, hereinafter referred the FL on TPD

coordination of audits with the AFB³.

2) Preferences are established in the **area of migration issues**, in particular:

- a) Employer residents should not obtain a permit for attraction and use of foreign employees;
- b) Work permit for a foreign citizen attracted for engaging in work activities by the resident of the free port of Vladivostok is issued without regard to quotas for issue of invitations to foreign citizens for entry to the Russian Federation and quotas for issue of work permits to foreign citizens, but with due regard to *a maximum share of such foreign employees determined by the Supervisory Board*.

A simplified visa procedure of entry to the Russian Federation, stay in the Russian Federation within eight days and exit from the Russian Federation is established for foreign citizens arriving in the FP territory.

3) As part of exchange of experience and increase of service quality, amendments are referred in the **area of medical and educational activities**. Tell the truth, these new laws are not adopted by the Government of the Russian Federation.

4) **Exemptions in taxation⁴**

A resident taxpayer of the free port of Vladivostok is considered to be an organization acquired a status of the resident of the free port of Vladivostok in accordance with law № 212-ФЗ. At that, continuously within five grace periods for profit tax, the following requirements should be carried out:

- State registration of a legal entity is carried out in the territory of the free port of Vladivostok;
- Organization does not include separate divisions located outside the territory of the free port of Vladivostok;
- Organization does not apply special tax treatments stipulated by the Russian Tax Code;
- Organization is not a member of consolidated group of taxpayers;
- Organization is not a nonprofit organization, bank, insurance organization (insurer), non-state pension fund, professional securities market participant, clearing organization;
- Organization is not a resident of a special economic zone of any type;
- Organization is not a participant of regional investment projects.

a) reduced profit tax rates

Residents of the free port of Vladivostok from 01.01.2016 (along with resident organizations of the territory of priority social and economic development) gained the right to use preferential profit tax rates. This is possible within 5 tax periods beginning from that period when the first profit from operation in the territory of the free port of Vladivostok has been gained in the

³ Relevant amendments were introduced to Federal law dated 26.12.2008 N 294-ФЗ (as amended on 06.04.2015) "On protection of rights of legal entities and individual entrepreneurs when exercising state control (supervision) and municipal control" // Reference legal System "ConsultantPlus"

⁴ Refer to Federal law dated 13.07.2015 N 214-ФЗ "On making amendments to part two of the Russian Tax Code in connection with adoption of Federal law "On free port of Vladivostok". Commencement of document - 01.01.2016. Provisions of sub-clause 4, clause 2, article 176.1 of part two of the Russian Tax Code are not apply in respect to a declarative procedure of refund of a value added tax for tax period beginning from October 01, 2015

resident's tax accounting.

In respect to a profit tax paid to:

- the federal budget the tax rate is **0 percent** ([clause 1.8, article 284 of the Russian Tax Code, clause 3, article 284.4 of the Russian Tax Code](#));
- the budget of an entity of the Russian Federation, the tax rate **cannot exceed 5 percent**. In so doing, within the **following 5 tax periods**, the tax rate cannot be **less than 10 percent** ([clause 4, article 284.4 of the Russian Tax Code](#)). Residents are entitled to apply the said tax rates subject to **two conditions** as a whole ([clause 2, article 284.4 of the Russian Tax Code](#)):
- Incomes from of activity in the territory of the free port of Vladivostok are not less than 90 percent of all the taxpayer's proceeds;
- Organization maintains separate records of incomes and expenses.

b) residents are entitled to VAT refund by way of declarative procedure

The law-maker has decided to grant benefits not only for a profit tax but for VAT. Therefore, the residents now may apply a declarative procedure of VAT refund. In this regard, it is necessary to submit a tax return and surety agreement (copy) to the managing company. Relevant amendments are included in sub-clause 4, clause 2, article 176.1 of the Russian Tax Code.

These provisions are applied for the tax periods beginning from 01 October 2015 (clause 2, article 2 of Federal law dated 13.07.2015 № 214-ФЗ).

5) Benefits in the area of insurance contributions to off-budget funds (from 01.01.2016)

Reduced rates of insurance contributions⁵ are established for the resident of the free port of Vladivostok (Federal law dated 13.07.2015 № 213-ФЗ, hereinafter referred to as Law № 213-ФЗ):

to Pension Fund of Russia - 6% in accordance with an option of pension security - 0 or 6 % for financing of a pension saving (articles 9, 17 of Law № 213-ФЗ);

to Social Insurance Fund - 1, 5% (article 17 of Law № 213-ФЗ);

to Federal Compulsory Medical Insurance Fund - 0,1% (article 17 of Law № 213-ФЗ).

6) Peculiarities of fishery regulation (now, it is of declarative nature)

7) Peculiarities of control in checkpoints of the FP (from 01.10.2016)

Thus, actions of officials of state control bodies concerning the violation of dates of exercise of state control resulted in unreasonable delays in exercise of state control are considered by the Supervisory Board of the free port of Vladivostok.

8) Customs privileges

A customs procedure of free economic zone is applied in the territory of the free port of

⁵ Refer to Federal law dated 13.07.2015 № 213-ФЗ, hereinafter referred to as **Law № 213-ФЗ**.

Vladivostok which is established by the *Agreement in free (special, particular) economic zones in the Customs Union customs territory and customs procedure of a free customs zone dated 18 June 2010* (hereinafter referred to as the **Agreement on free economic zones**), with particular aspects 212-Φ3.

The said customs procedure enable to place and use goods in the territory of the free port without payment of customs dues, taxes, without application of prohibitions and limitations and without placement under customs procedure of releases for domestic consumption, in view of *compliance with certain conditions and procedure.*

Thus, decisions to apply a customs procedure of free customs zone established for *a port and logistics special economic zone* with an allowance for establishing a special legal treatment can be taken in specific areas and territories by decision of the FP Supervisory Board.

The goods established in accordance with the Agreement on free economic zones cannot be placed under the customs procedure of free customs zones.

In addition, the goods cannot be placed by the resident of the free port of Vladivostok under the customs procedure of free customs zone in case of:

- 1) Initiation of *insolvency (bankruptcy) proceeding* in respect to the resident of the free port of Vladivostok;
- 2) Introduction of reorganization procedure (except for reorganization of a legal entity as transformation) or taking a decision on liquidation of a legal entity;
- 3) Taking a decision by the court or authorized body on suspension of activity of a legal entity;
- 4) Suspension, in accordance with the Russian legislation, of validity of a permit for carrying out a certain activity if the resident of the free port of Vladivostok carries out only such activity.

The provision is worthy of notice whereunder if a way of identification of foreign goods suggested by a declarant is not considered as acceptable by the customs body, the **customs body is entitled to independently determine a way of identification**. It bears noting, how often this provision being of absolutely positive interest will be applicable practically.

9) Peculiarities of carrying out of town-planning activities

Simplified and reduced procedures for obtaining permits in the area under consideration are established, for example, obtaining an urban development plan for a plot of land located in the FP territory, issuing building permits, permits for putting objects into operation in performing construction, reconstruction, overhaul repair of capital construction facilities located in the territory of the free port of Vladivostok.

Dates for public hearings on one or another issues which are next smaller in comparison with general rules are limited.

10) Protection of interests of residents of the free port of Vladivostok

The managing company is entitled to represent and protect interests of the residents of the free port of Vladivostok who seek assistance in the court, bring actions on the cases appearing from administrative and other public law on protection of rights and legal interests of public legal entities

and individual entrepreneurs having residency status in the free port of Vladivostok.

This norm contradicts the Russian Code of Arbitration Procedure with regard to a possibility of applying by the managing organization in favor of the public, since public interests are affected which can be protected by government authorities only (part 1, article 53 of the Russian Code of Arbitration Procedure).

11) Other measures

Thus, Law 212-Φ3 and Law 213-Φ3 review the provisions in respect to peculiarities of state registration of the right of ownership to an *artificially created plot of land* and a plot of land (plots of land) formed therefrom.

VI. Problematic issues

1) Abundance of issues are referred to subordinate statutory acts which are not adopted now and the dates of their adoption are unclear (for instance, establishing criteria for selection of residents).

2) Optionality of the formation of the Public Council.

3) Lack of a clear understanding related to criteria and procedure of gaining a resident status of the FP. Thus, an application with a set of documents is handled by the Managing Company. An entry into the register is made by the AFB. Criteria for business plan assessment are established by the FP Supervisory Board and AFB. While criteria for selection of FP residents are determined by the Government of the Russian Federation. In so doing, the said criteria remain to be established. On the other hand, supposedly such branching and division of functions and powers will enable to avoid a practice of double standards and corruption.

4) We think that there may be procedural difficulties with contesting the awarded judgment by the Managing Company concerning the refusal of concluding an agreement, including in view of the fact that at present there is no procedure of contesting such decision stated in the Law.

5) There are questions about control over the FP resident with an allowance for a possibility of using a residency of the beneficiary's controlled business unit by the beneficiary in order to gain benefits of other economic agents of the Group of companies. This situation is aggravated with consideration for the fixed **24-month period** of failure to carry out activity by the resident under the agreement as a ground for cancellation of the latter.

On the other hand, for example, with regard to using tax benefits, thresholds as a compliance of the FP resident with special conditions (see above) are specially provided.

6) A person ceased to be the resident of the free port of Vladivostok is entitled to carry out business in the territory of the free port of Vladivostok **unless otherwise provided by** this Federal law or agreement on activity. The reasonable examples are difficult-to-understand, which would require to close down an enterprise, except for a gross violation of the agreement. On the other hand, this provision can be a tool for illegal seizure of the resident enterprise and (or) its assets.

7) The above considered conflict of the Law and the Russian Code of Arbitration Procedure with regard to appealing of the Managing Organization in favor of the general public.

VII. General conclusion

It should be stressed that strong majority of provisions of the Law, including preferences and benefits, are embodied in the Law on territories of priority development. As a whole the Law on the free port of Vladivostok should be considered as a potentially positive tool aimed at achieving the goals set by the law-maker (refer to Section I), but to what extent it will be effective its practical application will show.

A positive fact for the system development and application of provisions of the Law at hand is adoption of Law on public-private partnership dated 13.07.2015 №224-ФЗ expected a while by all business community⁶.

⁶ Refer to Federal law dated 13.07.2015 N 224-ФЗ “On public-private partnership, municipal-private partnership in the Russian Federation and introduction of amendments to specific Russian legislative acts”. Effective from 01.01.2016, except article 46 hereof