

An Analysis of the Fixabilities and Restrictions of Foreign Investments Policies and their Impact on the Investment Climate: The Case of The Russian Federation*

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Abstract

The investment climate of a state or its region plays a key role in the investment decision in the eyes of a foreign investor. The investment climate of the Russian Federation is considered favorable and very promising by foreign investors, despite all the difficulties that have befallen it.

Stimulating investment activity of the regions and improving the investment climate is a priority task at the political level. Over the past 30 years, the Russian government has implemented the process of attracting foreign investment into the domestic economic sector through the implementation and elaboration of legislative mechanisms. The other side of the coin is the mandatory consideration of private and public, foreign and domestic interests. In most cases, the interests of government and business do not coincide.

Thus, in the Russian Federation we can observe two opposite, opposing tendencies. On the one hand, Russia longs for a large inflow of foreign investment and, in this context, is developing a legal regulatory mechanism that directs policy toward supporting the interests of investors. On the other hand, Russia wants to protect its national state interests by restricting, shackling and prohibiting the activities of foreign investors. All this requires a more comprehensive scientific study, both from a legal, juridical and economic point of view. The optimal combination of these two elements, the interests of the parties, will be the key to achieving a balance that will certainly lead to an improvement of the investment climate in Russia.

Keywords: Investment Attractiveness, Investment Climate, Legal Regulation, Foreign Investor.

Introduction

According to the World Bank report, the Russian Federation was among the 30 countries that were attractive to foreign investors in terms of Doing Business until 2020. Since the World Bank stopped publishing the rating from 2021 due to a number of established violations, there are no updates on this part. Nevertheless, structural disadvantages in economic governance continue to hinder foreign investment inflows to Russia. This refers to the inequality of the state vis-à-vis foreign investors when it comes to legal disputes. As a result, foreign investors are deprived of the Russian government's support in legal disputes. An additional problem is the high level of corruption in the country. This situation is also exacerbated by the effects of sanctions imposed by the European

Union and the United States, which severely restrict economic activity and force greater import substitution within the country (U.S. Department of the Treasury. Office of Foreign Assets Control, 2022).

Literature Review

Special Investment Contracts (SPIC)

Since 2015, a program to encourage foreign investors has been launched in the Russian Federation. The incentive mechanism was called "Special Investment Contracts" (SPIC). These contracts allow a foreign investor to participate in the Russian import substitution program and provide access to many areas of activity, subsidies, and the development of local production. In 2019, the incentive mechanism SPIC was updated to "SPIC-2.0". SPIC-2.0 provides the opportunity to encourage long-term foreign investment in high-tech projects and the introduction of new technologies into production. The term of SPIC has been extended to 20 years, depending on the amount of investment. The most important elements in evaluating the proposals were the modernization of technologies, the level of these technologies in the production process and, of course, the volume of production.

The Russian government is very interested in attracting foreign investors to the high-tech development of key regions of Russia. As an incentive, the government can provide a guarantee plus 12% on profits for 15 years for power plants (turbines) with turbines with local content. Currently, Russia is very concerned about public procurement for the pharmaceutical and medical equipment sectors. Due to sanctions, public procurement restrictions are the primary means for the Russian Federation to meet localization requirements without international violations.

Russian Direct Investment Fund (RDIF)

Do not forget the enormous contribution of the Russian Direct Investment Fund (RDIF) to attracting foreign investment. The purpose of this fund is to cooperate with long-term and strategic investors, co-finance foreign investments and improve production technologies. The Russian Direct Investment Fund has been able to attract more than 26 billion dollars over all these years, and in addition, the Fund itself has invested more than 2.7 billion dollars in the Russian economy at its own expense. The Russian Direct Investment Fund was able to attract another 40 billion dollars through long-term strategic partnerships. However, this is only one indicator of direct investment. In total, more than 185 billion dollars has flowed into Russia over the past 30 years (Reshetnikov M., 2022). This fact is confirmed by the Ministry of Economic Development of the Russian Federation. The Russian Direct Investment Fund, in cooperation with the National Center for Microbiology and Epidemiology named after Gamalei, was able to finance the development and distribution of the Russian vaccines Sputnik V and Sputnik Lite.

Main Legal Framework

In 2013, the Russian Agency for Strategic Initiatives launched the Invest in Russian Regions project to attract more foreign investment to the country. And starting from this period, the Russian Agency for Strategic Initiatives (ASI) annually publishes its rating of regions that will be attractive to future foreign investors in terms of investment climate and competitiveness. In 2021, almost 40 regions of Russia have improved their performance in investment climate rating (Agency for Strategic Initiatives, 2022).

To date, the main legal framework in Russia regulating investment:

- Law No. 160-FL dated July 9, 1999 "On Foreign Investments in the Russian Federation" (version dated July 14, 2022) (Federal Law No.160-FL, 1999);
- Law No. 39-FL dated February 25, 1999 "On investment activity in the Russian Federation in the form of capital investments" (Law No.39-FL, 1999);
- Law No. 57-FL dated April 29, 2008 "On Foreign Investment in Enterprises of Strategic Importance for State Security and Defence" (Law on Strategic Industries) (Law No.57-FL, 2008);
- RSFSR Law No. 1488-1 of June 26, 1991 "On Investment Activity in the Russian Soviet Federative Socialist Republic (RSFSR)" (Law No.1488-1, 1991);
- Federal Law No. 69-FL dated April 1, 2020 "On Protection and Promotion of Capital Investments in the Russian Federation" (with amendments dated 21. 11.2022) (Federal Law No. 69-FL, 2020).

This system of laws guarantees equality between foreign and domestic investors operating in Russia. However, exceptions are possible when necessary to protect the Constitution, national security, and human rights. Foreign

investors are free to use the profits from investments in Russia for their own purposes if they do not violate the laws of the Russian Federation (Saydasheva M.V., 2022).

The new Federal Law of April 1, 2020 No. 69-FL "On Protection and Promotion of Investments in the Russian Federation" (as amended on November 21, 2022) provides for the possibility of implementing new investment projects, with the support measure consisting of compensation (Federal Law No. 69-FL, 2020):

- costs for the creation or reconstruction of infrastructure;
- interest on loans taken out for the creation of the project.

The maximum amount of eligible costs shall not exceed 50% of the actual costs of providing infrastructure facilities and 100% of the actual costs of related infrastructure facilities. The cost recovery period shall be five years for ancillary infrastructure and ten years for related infrastructure.

Under Russian law, there are two main restrictions on land ownership by foreign investors. The first restriction concerns full ownership of land in border areas or other "key areas". The second restriction concerns ownership of agricultural land. The restriction is that this land can only be acquired on a lease basis. In this context, foreign investors often lease land for a period of 49 years, which is the maximum period allowed by law. The same restrictions on property rights also exist in the media sector of the Russian Federation. Thanks to the Law of the Russian Federation of 27 December 1991 N 2124-1 (as amended on 14 July 2022) "On Mass Media" (as amended on 1 December 2022), foreign capital in a Russian media company, as well as the share in the ownership of these Russian companies, may not exceed 20% (Federal Law of the Russian Federation No. 2124-1, 1991).

Federal Antimonopoly Service (FAS)

The Government Commission for the Control of Foreign Investments in the Russian Federation was established in 2008 to control foreign investments in strategic sectors in the interest of the country's security (Official website of the Government of Russia, 2022). According to the Federal Antimonopoly Service (FAS), in the period from 2008 to 2020, this government commission received more than 645 applications for foreign investment, 90% of which were approved and the remaining 10% rejected (Official website of the Federal Antimonopoly Service of the Russian Federation, 2022). This is a good sign of the government's loyalty to the investors involved.

Methodology

We also note that the leadership of the Russian Federation does not interfere in the affairs of Russian investors abroad and does not seek to restrict them in any way. Since 2015, the adopted "Law on Deoffshorization" (376-FL) obliges residents of the Russian Federation to report their foreign assets to the Russian government in order to be taxed (Federal Law No. 376-FL, 2014). From 2020, residents of the Russian Federation will be able to safely use declared personal foreign accounts to save money and invest in various financial products.

The Russian Federation provides transparent policies for foreign investors at all levels of activity. The main regulations of the ministries are constantly published and deposited on the official websites. Accounting is fully transparent and consistent. However, accounting records can only be provided to companies that operate in foreign markets or have borrowed money from foreign creditors. Reports under the rules and regulations of the International Financial Reporting Standards (IFRS) are required for the consolidated accounts of all companies that share common characteristics, such as: Listed securities, various banks, insurance companies, pension funds. Basically, in all sectors, classical accounting is applied according to the rules applicable worldwide. Nevertheless, many foreign companies state that the testing and certification of foreign goods is a problem when exporting. Russia requires product testing and certification as a key element for the approval of various products by a legal entity registered and established in Russia. This is the legal entity that can apply for product approval. This means that testing and certification by competent authorities outside Russia will be a very difficult task. Such problems also exist for manufacturers of oil and gas equipment, construction machinery and other construction materials, pharmaceuticals and medical devices. They report serious difficulties in obtaining product approvals in Russia. Problems with technical barriers to trade also exist for spirits, medicines and medical equipment. In April 2021, an amendment to Article 1360 of the Civil Code was adopted, which significantly simplified the mechanism for issuing licences for the pharmaceutical industry. The amendments concerned the granting of a licence "in the interest of protecting life and health" (U.S. Department of State. Bureau of Economic and Business Affairs, 2022).

Conclusions

It is necessary to consider the issue of settlement of disputes between foreign investors and the state. In most cases, lawyers of foreign companies having investment or trade disputes in Russia forward their complaints to international arbitration centers in Paris, London, Stockholm or The Hague. Due to the 2015 changes in the legislation of the Russian Federation, the Constitutional Court of Russia has the right to ignore the decisions of international courts if their decisions contradict the Constitution of the Russian Federation. In addition to the court system, Russian law recognizes mechanisms for alternative dispute resolution, i.e. domestic arbitration courts, international arbitration courts, and mediation. The decisions of such domestic arbitration courts are also enforced in accordance with international treaties and conventions to which Russia is a party. Thus, the possibility of an ideal combination of legal regulation and consideration of the interests of all economic operators in attracting investment will help to increase the investment potential and investment climate of the country.

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