

## RUSSIAN INVESTMENT LEGISLATION FROM THE POINT OF VIEW OF CAPITAL FLIGHT AND ITS REINVESTMENT PROBLEM

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**Key words:** capital flight, reinvestment, investment legislation, investment, economic security, foreign investment, investment climate, ethnic capital, investor, investment risk.

The author gives the classification of all Russian legislation in connection with a problem of flight of the capital and its reinvestment. The special attention is given the block "the investment legislation": the main laws in a context of a lifted problem are analyzed. The author does a conclusion about imperfection of the investment legislation of Russia that stimulates flight of the capital and blocks its reinvestment. At the analysis of separate acts the author offers ways of improvement of the investment legislation.

Russia always suffered from the lack of capital. An extremely severe this influence was witnessed in the course of the various social and economic reforms which, as a rule, were followed by the increasing economic and political misbalance. In the 1990-s the investment climate in Russia fell down considerably, the economic growth was reduced to nothing, there was apparently an economic and political regress. The state faced then new problems as well as new ones: lack of capital in the country was aggravated by a rapid capital flight abroad, while deficit of internal investments was not fully recompensed by foreign investments.

An increasing capital flight out of Russia jeopardizes the economic stability of the country, sharpens the lack of internal investments etc. By reduction of the volumes of the flight capital one can succeed to increase the consumption of investments inside Russia and people's savings. The return of the Russian capital might solve the aforementioned problems, in the first place, that of the economic stability. Nowadays in Russia there is a great role of factors which stimulate the flight of capital and bar the process of its reinvestment.

The whole set of problems which stimulate the flight of capital and bar the process of its reinvestment could be surely solved with the help of the most important state regulation levers - legal acts.

The whole legislation, due the problem capital flight, can be divided into the following branches:

### 1. Investment legislation.

#### 1.1. General clauses.

1.2. Normative acts which regulate the investment activity which is performed in a form of capital investments.

1.3. Agreement on the sharing of production.

1.4. Normative acts which regulate the investment activity in the form of leasing.

1.5. Normative acts which regulate the investment activity on the equity market.

1.6. Normative acts which regulate the activity of investment funds.

1.7. Normative acts which regulate the process of investment of pension accumulation acts.

1.8. Normative acts which regulate the status of foreign investments.

1.9. Normative acts in the sphere of the investment activity of foreign nature.

#### 2. Exchange and customs control.

#### 3. Criminal legislation.

4. Some other legal acts which influence the investment climate in the country.

The investment legislation holds the prime position among the factors which influence the capital flight and makes it possible to solve both the problem of capital flight reduction out of Russia and the problem of reinvestment the financial assets fled out of the country.

While studying the investment legislation of Russia one should pay attention to the fact that quite a number of norms are devoted to the foreign investments formation; though, there are no norms which could be directly focused on the formation of the ethnic capital which had been removed from the country.

The federal legal act № 1488-1 of "The investment Activity in Russia" pays special at-

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tion to the fact that “all the investors have got equal rights to perform and carry out investments activities” (cl.5, pt.1). Consequently, an immediate accent is done upon the equality in rights between all the investors without any protection of domestic investors or coming back to Russia ethnic capital.

By the same legal act the state guarantees the stability of rights of subjects in process of the investment activity underlining that “in case when the legal acts, the principals of which restrict the rights of subjects of the investment activity, are approved the aforementioned clauses can not come into force until a one-year period since their publication” (cl.14, pt.1). Nevertheless, as it is clear from a practical viewpoint, the presence of the norm itself, which allows altering “the rules of the game” in this or that market, do lead anyway to ambiguity and risks which in turn affect badly the investment climate in the country. Moreover, an opportunity and possibility to play another game under the existing rules do not result in solving the problem because a year is quite a short-term period for reorganization of the already established system of interrelations in this or that sector of economics. So, the capital reacting the instability and high risks simply leads its way to where there is stability and confidence.

Clause 15 of the considered legal act provides guaranties the protection of investments from the gratuitous nationalization. At the same time point 2 of the above-mentioned clause underlines that nationalization is possible with recompense of all losses of the investor. One can not but notice that, however, that with real and true-to-life Russian compensation paid to the investor is frequently not equal to the real scale of damage: assets are withdrawn by the state for the scanty payment. The example of such a situation can be withdrawal by the state the land which is situated on the place of the would-be incircling highway in Saint-Petersburg. The latter again give rise to the risks of ambiguity, lack of confidence to the state and worsening of the investment climate.

According to point 1 clause 284 part 2 of The Internal Revenue Code of the RF tax rate for the income tax is set on the level of 24% of which 6,5% are transfer to the federal budget while 17,5% - to the regional budgets of the RF. Still, it is noticed that “tax rate of the tax which is to be transferred to the regional budgets of the RF can not be reduced for the sake of certain categories of tax-payers in Russia. At the same

time the established tax rate is not to be lower than 13,5%”. This means that the income tax (to be more precise, its part to be transferred to the regional budgets of the RF) could be easily used as a massive tool to stimulate the development of various domestic enterprises.

The federal legal act № 39-FLA “The investment activity in the Russian Federation carried out in the form of the capital investment” and its point 1, clause 15 as well enumerates the guaranties provided by the state to investors, namely:

- ◆ Guaranties of the equal rights during the investment activity;
- ◆ Guaranties of publicity during discussions of investment projects and the like;
- ◆ Guaranties of the right to make an appeal against the decision and actions (inaction) of the federal authority bodies, the institutions of local government and their officials;
- ◆ Guaranties of the protection of the capital investments.

It goes without saying that the availability of the guaranties of such kind raises the authority the state, while the non-fulfillment of them injures the state itself and the investment climate, in general. There is no special need to say that in Russia such guaranties are not provided in most cases: the judicial system of the country works rather badly, some acknowledges investors enjoy some groundless privileges right from the state, decision on some investment project are discussed and made behind closed doors or with the help of the ostensible public hearings, capital investments in Russia are quite often unprotected.

The federal legal act № 39 - FLA clause 19 indicates that the investment activity in Russia could also be carried out by the institutions of local governments. At the same time, municipalities are not parts of the state power of the RF, which leads to much of ambiguity and misunderstanding.

The central position in the investment legislation due to the flight capital and its reinvestment problem is held by the legislation which referred to the regulation of the status of foreign investment in Russia. This section is remarkable for, firstly, the fact that the legislation which referred to the regulation of the status of foreign investment in Russia influence the investment climate in the country on the whole and, secondly, it is directly focused on how to solve the problem of reinvestment of the removed capitals. It happens really often that the

removed ethnic capital turns into an internal one and comes back to Russia as foreign. This can not be omitted but taken into consideration while solving the problem of capital reinvestment in Russia.

In general, the federal legal acts of the RF provide for the foreign investors a legal status on the territory of the country which is not worse than that for the domestic investors (in other words, it sustains the national internal legal regime and status). Consequently, one can surely define the Russian legislation concerning the regulation of the status of the foreign capital as a liberal and democratic one.

The centre of the legislation concerning the abovementioned matter is generally considered to be the legal act № 160-FLA "Foreign Investments in the Russian Federation". According to this normative act, the state provides the following guaranties for foreign investors (FI):

- ◆ Guaranties of the legal protection of the foreign investors activities on the territory of Russia

- ◆ Guaranties of using by foreign investors various forms of making investments on the country's territory;

- ◆ Guaranties of the possibility of transfer of rights and responsibilities to someone else;

- ◆ Guaranties of the compensation in case of nationalization and requisition of the property of foreign investors or commercial organization with foreign investments;

- ◆ Guaranties of the protection of investments in case there is a negative change for FI or commercial organization with foreign investments in the Russian legislation;

- ◆ Guaranties to provide the proper dispute settlement which aroused out of the FI's making investments and business on the territory of Russia;

- ◆ Guaranties to be able to operate with revenue, profit and other legally gained sums of money on the country's territory and to remit them abroad;

- ◆ Guaranties of foreign investors' rights to perform a free export abroad of the property and information arranged either in a form of document or in a form of an electronic version which had been imported to Russia's territory as foreign investments;

- ◆ Guaranties of foreign investors' right to buy equities;

- ◆ Guaranties to provide FI a right to own a land, other natural resources, buildings, constructions and other immovable property.

It is extremely important to mention and notice that the Russian legislation has got a vast number of tools and leverages in the way of regulation of foreign investments, which indicates a high interest coming from the state to attract foreign investments in Russia. Among all the rest the RF Governmental Regulation № 883 dated June 23<sup>rd</sup> 1996 "Privileges on payment of entrance custom tax and value-added tax in respect of the good imported by foreign investors to be considered as contribution to the authorized capital of the enterprises with foreign investments" is rather interesting and its point 1 says that "the good imported to the custom territory of the Russian Federation as contribution of the foreign founder to the authorized capital is released from custom taxation provided that the goods are not excise and belong on the basis of production funds, imported in due time set by the constituent instruments for formation of authorized capital". The aforementioned norm is primarily directed to stimulate reinvestment of capital in Russia. For justice' sake, it is necessary to mention that a considerable number of enterprises use the aforementioned privilege making investments through offshore subsidiary companies. Nonetheless, even in this case all does not appear to be so ideal as desired. Particularly, while making a contribution to the authorized capital it is recommended to carry out an independent estimation of the market price of the imported goods. Such estimation, however, is quite often of a sponsoring nature and aimed at decreasing the real value of the imported goods in order to decrease the tax base, for instance, of the property tax.

On the whole, one should say that the modern Russian investment legislation leaves much to be desired being not as perfect as desired again. The elimination of the abovementioned drawbacks could certainly promote a significant rise of its effectiveness as a key tool to reduce the rate of the flight capital and to stimulate its reinvestment.

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<sup>1</sup> Investment legislation: Collected normative acts: Official text. / Compiled by Y.V. Lazarev. M., 2005. P. 3-9.

<sup>2</sup> Ibidem. pp. 14-31

<sup>3</sup> Ibidem. pp. 78-90.

<sup>4</sup> Ibidem. pp. 370-381.

<sup>5</sup> Ibidem. pp. 395-396.