



Food and Agriculture Organization of the United Nations (FAO)

Forest Sector Study in the Russian Far East
Roadmap for Value-added Investment in Forest Industry

Annex Report I

**Assessment of Forest Policy
and Forest Industry Policy
in the Russian Far East**

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Terminology and abbreviations

Forest policy – a complex of decisions and actions taken by certain institutions as well as instruments to achieve them, based on public priorities at any given stage of social, environmental and economic objectives in the field of forest-use benefits. The RF Forest Code lacks an official definition of the forest policy. Therefore, the above definition, formulated by the author is further used in this document.

Forest users – a generic term for entrepreneurs engaged in the timber business, including timber harvesting, all types of processing and product export.

RF – Russian Federation

RFE – Russian Far East

RF Forest Code, 2007 – the Forest Code of the Russian Federation, adopted December 4, 2006, № 200-FL, enacted from 2007.

Rosleskhoz – the Federal Forestry Agency (FFA).

Rosprirodnadzor (RPN) – the Federal Service for Supervision of Natural Resources

Rosselkhozadzor – the Federal Service for Veterinary and Phytosanitary Surveillance

Entity (Subject) of the Russian Federation – an administrative-legal entity of the Russian Federation. There are the following types of RF entities: republics, krais, oblasts, autonomous oblasts, autonomous okrugs.

Territory investment potential – a complex of factors determining the attractiveness of a certain area for an investor, sufficient conditions for business start up and development. This potential can be realized, or remain unrealized, depending on future management actions at all government levels. The following types of potentials, which are subject to the government regulation of economic activities in the forest sector, are described: normative and regulatory, institutional (economic regulations and mechanisms for their implementation), financing-economic, information, resource, and infrastructure.

Investment risk – probability (threat) of financial losses (decrease or loss of capital or profits) due to the uncertainty of investment conditions. Such threat can be mitigated if timely taken into account by the investor. Here the focus is on the risks associated with the state regulation of economic activities in the forest sector namely investments into high-tech timber processing industries. The following types of risks are identified: normative-regulatory, institutional, financial-economic, information, resource, infrastructure, and market.

Recommendations – a list of possible actions aimed at mitigation of identified risks (threats) to facilitate investment projects in high-tech timber processing.

Leskhoz – an administrative forestry enterprise

TIC – a timber industry complex

PPP – a pulp and paper plant

MDF – medium density fiber board

FEFO – the Far Eastern Federal Okrug

RFE – the Russian Far East

Definitions for specific Russian forestry terminology

Forest Fund- a generic term used in Russian as applied to: all forest lands, covered or not covered by forests, the within the limits defined by forest and land laws that are under Federal ownership and intended for forest and forestry purposes.

Deep processing – value added processing

Forest relations – a generic term used in Russian as applied to “legal, normative/regulatory or economic relations between Federal government institutions and/or entities (subjects) of the Russian Federation, local self-governing bodies (local authorities, citizens, juridical persons etc in connection of (“on the subject of”) forest use, conservation, protection, regeneration etc.

Forest management – (management of forest use) – the State system of management (control) of use, conservation, protection and regeneration of forest resources. It consists in the definition of general rules for forest use and control over their implementation. Forest management is implemented via the following functions: administration of forest resources; control over forests’ condition and use; forest monitoring, inventory, cadastre and engineering; forest protection from fires, pests and diseases and illegal use.

Executive summary

Russian forest policy

Over the past twenty years the Russian forest policy has undergone intensive changes with substitution of old market institutions/relations in the forestry sector by the new ones. Based on the results of the State Council Presidium meeting on “*Improved efficiency of the RF forest complex*”, in May 2013 President signed a **list of priority measures** (N-1037, 07.05.2013¹).

Those measures include:

1. Update of the RF state programmes “**Forestry development for 2013-2020**” and “**Development of industry and increase of its competitive ability till 2020**” with consideration of the “Foundations of the state policy in the field of forest use, conservation, protection and regeneration”.
2. Introduce amendments in the RF legislation relative to:
 - (i) Tenders for forest plots lease by processing enterprises, with clear selection criteria;
 - (ii) The definition of criteria and norms for defining categories for protective forests and specially protected plots in the forests, as well as definition of legal regimes in those forests²;
 - (iii) Possibility for a full, partial or postponed reimbursement of VAT for the export of unprocessed timber;
 - (iv) Possibility to use means from the forest construction funds of RF entities and municipalities for construction and maintenance of common use roads which are also used for forest exploitation.
 - (v) The provision of long term subsidies to forestry complex enterprises for a partial re-imburement of interests on credits for technical (re-)equipment and preparation of projects on value added processing.
 - (vi) Elaboration and introduction of a common information system (data base) on timber harvesting and roundwood trade.

As of 2013 interest rate subsidies on loans are to be granted to the organizations implementing priority investment projects aimed at development of high-tech manufacturing facilities³.

In September 2013 the new policy document called the **Foundations of the State Policy in the Field of Forests Use, Conservation, Protection and Regeneration till 2030** has been adopted.⁴ This document defines principles, goals, and tasks related to forests use, conservation, protection and regeneration. It serves as a basis for further formulation of regulations, plans and other policies for forest sector. According to *the ‘Foundations’*, key tasks of the state policy related to forests focus on:

¹ <http://www.lesprom.com/news/56334>

² This will solve contradictions between forest users and ecological organizations

³ RF Government Resolution N2 (16.01.2013) on the “Rules on Subsidy Provision from the Federal Budget to Organizations of the Timber Industry Complex for a Partial Compensation of the Interest on Credits Obtained in 2012-2013 for Implementation of Investment Projects to Create New High-Tech Manufacturing Facilities”
<http://www.minpromtorg.gov.ru/docs/government/76>

⁴ <http://government.ru/media/files/41d4926bf69a218ee79f.pdf>

- *improvement of forest governance*
- *intensification of forest use and regeneration*
- *development of the domestic market of timber products and improved competitiveness of the Russian forest industry, including an increase in the production and exports of wood and paper and value-added products*
- *efficiency of forest fire protection, protection of forests from pests , diseases and other adverse factors, as well as from illegal logging*
- *improvement of forests productivity*
- *preservation of the ecological potential of forests*
- *improvement of scientific, technical, technological, and human resources potential of the forest sector*
- *development of international cooperation in forestry and forest industry*
- *involvement of citizens in decision-making process*

Russia's accession to the WTO

Russia's accession to the WTO (22.08.2012) brought about changes of regulations on unprocessed timber exports (see Annex 1.1). Experts of the Russian Economic School [14] consider that the reduction of import duties on timber products as a consequence of Russia's accession to the WTO will cause the increase in volume of timber products imports and the decrease in domestic timber industry (by 6.7%). The most serious outcomes are projected for the Russian Far East, where a 25.9% decrease of domestic processing is forecasted.

Possible investment risks related to forest policy and institutional framework at the national level

- Continuous changes in the Russian forest related legal framework which is due to the lack of a comprehensive national forest policy and a clear-cut long-term national strategy for the forest sector development, undermines institutional potential capacities for a steady business in the forestry sector.
- Dual nature of responsibilities and control over the use of land resources (federal and regional levels) imposes bureaucratic protraction in the approval of investment projects. There are cases when the ownership is not clearly defined between the federal government, RF entities and municipalities.
- The data on forest resource potential are outdated and inaccurate, same is the information about volumes and quality of forest resources.
- The lack of a complete cadaster of forest plots makes it impossible to use them as collateral for loans, subleasing, etc.
- The inconsistency of the Russian government in implementing timber export policy leads to instability in relations between Russian and foreign partners in trading timber products.
- Strong competition and new types of products pose challenges for Russian manufacturers.
- Financial exemptions for investors are very few, and all of them are applied only at the level of RF entities.
- The existing system of tax revenue distribution between the federal and regional budgets does not encourage regional authorities to attract investment because a part of this revenue is returned to the federal government through taxes on the activities of investors.

- The rights and conditions of forest road exploitation for the lease holders who built this road, are not clearly defined neither for the actual leasing period, nor for the post-contract period [17].

Russian Far East institutional environment

In 2012 the **RF Ministry on the Development of the Far East** [26] was established to coordinate the implementation of government programs, as well as to control the execution of powers delegated to local authorities. A special **Council on Encouragement of Foreign Investment** was formed under the RF President Plenipotentiary Representative in the Far Eastern Federal Okrug to improve the investment climate. **Fund for the Development of the Far East and the Baikal Region** [27] was established in 2011 under the auspices of the Vnesheconombank to provide investment consulting for regional authorities and investors, as well as to partially finance investment projects carried out in the Far East.

In order to stimulate investment processes in the most competitive sectors of the RFE economy, including the timber industry complex, a federal target program on “**Economic and Social Development of the Far East and Zabaikalje till 2013**” was adopted and implemented during 17 years (1996–2013) [24]. A complementary *Strategy of Social and Economic Development of the Far East and the Baikal Region for the period up to 2025* was adopted in 2009.

For details on regional policies, refer to Annex 2.1.

Transport

Underdeveloped logistics and infrastructure are the biggest obstacles for the timber business development in Russia, although possibilities of the Baikal-Amur Mainline (BAM) development are being discussed nowadays. BAM is connected with Vanino Port and its improvement will increase its transportation capacity and reduce the time of delivery. The following three major challenges related to transport policy can be indicated:

- (i) underdeveloped forest roads network and their low quality;
- (ii) weight restrictions for timber transportation by road (restrictions on large goods vehicles driving on the existing roads were enacted in 2009) [16];
- (iii) a sharp increase in tariffs for railroad transportation; lack of railway cars and poor quality of services;

Energy infrastructure

According to the World Bank, Russia is the last one among 183 countries in the ranking of the availability of connection to the power supply network [18]. Power supplying companies quite often violate legal requirements and regulations, their denials for services are rather common and frequently unsubstantiated and connection procedures are very time-consuming for customers [19]. In 2012 an action plan was approved in Russia to ease the conditions for the connection of customers to the energy infrastructure in Russia. It is proposed to make the network connecting procedure easier, faster, more transparent and less costly.

Human resources and demographic policy

Four important human resources issues are to be stressed in relation to the encouragement of investments into the forest sector:

- (i) protection of the rights of hired workers,
- (ii) general labor force deficit in the Russian Far East,
- (iii) shortage of qualified workers, and
- (iv) foreign labor intake.

The Concept of the *State Migration Policy of Russia* until 2025 [22] was adopted in 2012. It sets the task to stop migration of people from the Far Eastern regions by 2020. The Concept also sets the task to develop differentiated mechanisms of attraction, selection and employment of foreign labor according to the needs of Russian economy.

Environmental initiatives

The RF Forest Code divides forests by the purpose of use into protection forests, commercial forests and unexploited (reserved) forests. Forest harvesting and construction of timber processing infrastructure are prohibited in protection forests and special protected areas. Some of these areas are created to fulfill Russia's international obligations as a signatory of international conventions and agreements⁵. There is a gap between international commitments, signed by the federal government, and their local implementation. In some areas of the Far East the establishment of protected plots in forests (as required by the Forest Code) has not been completed. The boundaries of such protected plots in the leased forest lands are not clearly defined, which causes disputes between forest users and environmental organizations

Recommendations on creating favorable policies and institutional environment into encourage investments in value added timber processing in RFE

1. A full-fledged **financing of forest inventory** from the federal budget should be guaranteed (alternative sources may be searched for) in order to provide accurate information about the quality and quantity of forest resources available for investors.
2. The **state cadastre of forest plots** should be completed to enable the introduction of leased forest plots into the economy utilization in accordance with civil and land legislation.
3. It is recommended to **authorize the lease holders to fight fires** on the leased plots without license in order to reduce risks of timber loss, thus encouraging further processing.
4. Federal authorities should **compensate the costs of forest and fire management** works carried out by the lease-holders through re-investment of forest fees into the fire-management (*re-investment mechanism of forest charges should be defined and introduced*).
5. A new mechanism allowing the **reinvestment of resource fees** into forest management should be defined. The increase of timber fees (standing timber fee) will make it an effective incentive, encouraging investments into timber processing.

⁵Russia has signed 18 international conventions and agreements of legal status, 8 of which are directly or indirectly related to forest conservation and use.

6. The **procedure** for obtaining the status of a priority investment project should be **simplified** through abolishing the requirement to provide excessive amounts of additional explanatory documents.
7. Transport and energy infrastructure should be developed for creating new industrial sites (greenfields)

Recommendations on creating enabling conditions and incentives for investments into value-added timber processing in RFE

1. Government measures should be undertaken to define and fix **clear and simple procedures** for the attribution of public lands to the federal government, RF entities and municipalities as well as land allotments for mill construction purposes.
2. To enhance **effective development of value added timber processing** in the Russian Far East the Federal government should provide financial support to investors through facilitating their access to more diverse guarantees for loans in new high-tech manufacturing facilities.
3. **More tax incentives** for investors are needed to reduce capital costs of investment projects.
4. The government as the owner of forests should invest into the **construction of major roads** and include these costs in the increased forest charges. This would be one of the mechanisms to stimulate investments into timber processing. Businesses can build local roads to connect with the major ones, built by the state.
5. **Regulations, norms and standards of forest roads use** should be revised.
6. The efforts **to improve the system of quotas for foreign labor** should be intensified and effects monitored.

Assessment of forest policy and forest industry policy in RFE

Introduction

Over the past twenty years Russian forest policy has undergone intensive changes with substitution of old market institutions/relations in the forestry sector by the new ones. Since 2007 Russia started a new phase of significant institutional changes in the field of forest management and use: the most important are forest sector reform and the changes in the timber industry and export policies. The past 2 years (2012-2013) witnessed developments that may have a significant impact on investments in the Russian forest sector: Russia joined the WTO, the Federal Forestry Agency has passed under the authority of the Ministry of Natural Resources and Environment Protection with an appointment of a new head and a new forest policy is being elaborated through an active participatory process; following V.V. Putin's recommendation the new policy document will be called **Foundations of the State Policy in the Field of Forests Use, Conservation, Protection and Regeneration till 2030**; at the Federal level there is a noticeable intensification of measures aimed at the efficiency improvement in the RF⁶ forestry complex⁷.

According to the RF administrative division the Far East belongs to the Far Eastern Federal Okrug (FEFO) and consists of nine regions: the Republic of Sakha (Yakutia), Primorsky, Khabarovskiy and Kamchatskiy Krai, Amurskaya, Magadanskaya, Sakhalinskaya and Jewish Autonomous Oblasts and Chukotskiy Autonomous Okrug. The timber industry is most developed in the Khabarovskiy and Primorsky kraia, and the prospects for further industry development are associated with these regions. However, we cannot exclude investment possibilities in Amurskaya and Sakhalinskaya oblasts.

Khabarovskiy and Primorsky Kraia, Amurskaya and Sakhalinskaya Oblasts were selected for the present analysis, as they are rich in forest resources and have a relatively well-developed timber industry; they are located in the most economically developed southern part of the Russian Far East with a less severe climate permitting year-round forestry activities. They are most densely populated: 73.6% of the total 6.3 million population of the Far East live in these 4 RF entities.

An important characteristic feature of modern timber processing in the Far East is the fact that almost all major timber processing companies are former logging companies, previously engaged in logs export. New institutional context forced timber logging / exporting companies to develop timber processing facilities. Therefore, all institutional changes in forestry and timber industry affect the interests of practically all the concerned stakeholders.

The way of functioning of the State administration makes it difficult to separate institutional decisions initiated at the federal or regional levels. Therefore, the report discusses policy decisions initiated at the federal level and their impact on the regional level.

1. Forest and timber industry related policies of Russia: general overview

1.1 National forest related policies and legal framework

Institutional set-up and responsibilities

⁶ See Annex 1 for terms and abbreviations

⁷ <http://xn--d1abbgf6aiiy.xn--p1ai/%D0%BD%D0%BE%D0%B2%D0%BE%D1%81%D1%82%D0%B8/17876>

The process of definition and adoption of a formal Russian forest policy document is ongoing since 2011. Current document is titled: *Foundations of the State Policy in the Field of Forests Use, Conservation, Protection and Regeneration till 2030* has been adopted in September 2013. Since the present forest related legislative practice does not consider timber industry as a subject of forest policy, the forest and timber industry policies have to be discussed separately.

In 2012, the Rosleshoz was re-introduced into the structure of the RF Ministry of Natural Resources and Environment Protection with a parallel transfer of normative functions, including definition of forest policy.

Basic forest laws regulate the forest-related activities in Russia. Three basic forest laws provide for the definition of responsibilities and powers between federal and regional authorities: the federal level basically preserves all control over the management of state forest lands (Table 1.1).

Table 1.1 Division of forest related responsibilities between federal and regional authorities in Russia in 1993-2011

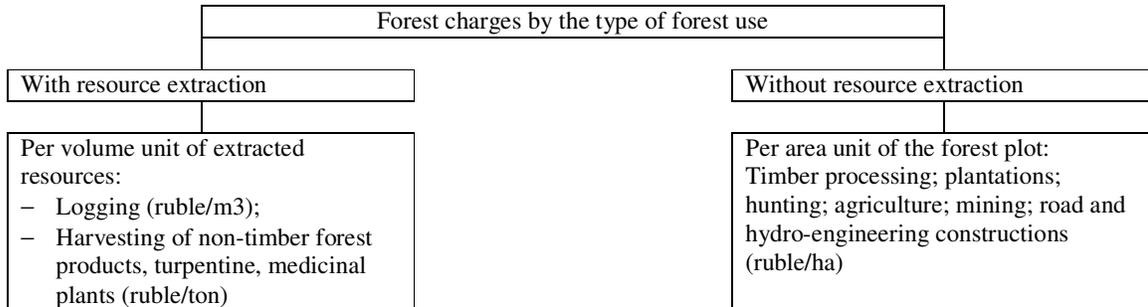
Year of enactment	Regulatory document	Federal level	Regional level
1993	Fundamentals of the RF Forest Legislation		The right to manage forest resources is given to the local (municipal) and regional authorities
1997	RF Forest Code		RF entities strengthened their authority over forest resources
2005	Amendments to RF Forest Code	The rights to manage forest land are given to federal authorities	
2007	RF Forest Code		The Federal government passed the responsibility over forest lands management to the RF entities, but retained a strict control over it.

Since RF forest Code adoption, 2007, forest management **at the territorial level** has undergone the following changes (Fig. 1.1).

- *Leskhoz*es, later transformed into forest districts (*lesnichestvo*), were transferred under the jurisdiction of regional forestry authorities and were entrusted with forest management functions. Forest management activities have to be carried out by specialized forestry enterprises, as well as by forest tenants (lease-holders).
- Forest planning in RF entities was introduced, including: a forestry plan (forest description based on inventory data), detailed forest management plans for forest districts, “*reglament*”(detailed forest description of the forest district based on forest inventory), as well as forest logging plans with stand description for leased forest plots.

Based on the auction results, a forest plot lease agreement is signed for a stipulated period from 1 to 49 years depending on the type of forest use [2]: eg. for 10-49 years for timber harvesting and from 1-49 years for processing. Depending on the type of forest use the charges are calculated based on two types of chargeable rates, defined by the federal authorities (Fig. 2).

Figure 1.2 Forest charges by the type of forest use



Charges may be adjusted by coefficients depending on a number of factors, eg. regional premiums (regional charges defined by RF entities) based on auction results. Charges for forest resources do not exceed 1% of the cost of logging.

The RF entities are authorized to collect and monitor payments for forest land use, whereas the federal authorities are responsible for the overall control of the process. There is no direct correlation between the forest charges and profitability of the leased forest plot because there is no mechanism that would provide for the revenue reinvestment into silvicultural activities or to finance forest related business development.

The conditions of a lease agreement oblige a lease-holder to establish a forest management plan (project) for the designated plot, with a specification of types and volumes of forest use and intended silvicultural measures, including forest regeneration, thinning and fire control (this can be considered a reason for the low rental fee).

In the non-leased forests, the Regional forestry authorities carry out silvicultural activities under subventions from the federal government. Since 2012 licensing of forest fire fighting has been introduced, including for those to be done by lease-holders. This increases bureaucratic obstacles and costs of lease.

1.2 National timber industry policy and legal framework

Normative framework related to investments

The normative framework for investments and strategic development of timber industry consists of the following documents: (Figure 1.2).

Table 1.2 Legal framework for investments in the Russian timber industry

Regulatory document	Content
Forest Code, 2007	Investment in forest resource use and priority investment projects in timber processing are mentioned for the first time
Strategy for the Development of the Forest Complex of Russia, adopted by the Decree of the RF Ministry of Industry and Trade № 248 and the Decree of the RF Ministry of Agriculture № 482, dated October 31, 2008	It contains a list of investment projects in timber processing, which the government intends to support as a priority
Subprogram “Timber Industry Complex” in the Russian State Program “Development of the Industry and the Increase of its Competitiveness”, approved by the RF Government decree № 2539-p dated December 27, 2012	Its target is to improve investment climate and further implement priority and other investment project
Priority Investment Projects on Forest Development: RF Government Resolution №419 dated June 30, 2007	Provides a number of privileges to companies that develop timber processing. Projects with investments of 300 million rubles and above are considered as priority projects. Privileges: - leasing without auction is possible; - forest land leasing charges are 50% reduced for the project payback period
Investment activity in the Russian Federation in the Form of Capital Investments: Federal Law, February 25, 1999, № 39-FL	It defines the normative framework for investment in RF economy; introduces guarantees for the protection of investors’ rights, interests and property.
Foreign Investments in the Russian Federation: Federal Law, June 9, 1999, № 160-FL	It defines basic guarantees of the foreign investors’ rights to investments and their generated revenues and profits; it also defines conditions of entrepreneurs’ activities for foreign investors in Russia

Based on the results of the State Council Presidium meeting on “*Improved efficiency of the RF forest complex*”, President signed a **list of priority measures** (N-1037, 07.05.2013⁸). Those measures include:

- Update of the RF state programmes “**Forestry development for 2013-2020**” and “**Development of industry and increase of its competitive ability till 2020**” with consideration of the “Basics of the state policy in the field of forest use, conservation, protection and regeneration.”
- Introduce amendments in the RF legislation relative to:
 - (i) Tenders for forest plots lease by processing enterprises, with clear selection criteria;
 - (ii) The definition of criteria and norms for defining categories of protective forests and specially protected plots in the forests, as well as definition of legal regimes in those forests⁹;
 - (iii) Possibility for a full, partial or postponed reimbursement of VAT for the export of unprocessed timber;

⁸ <http://www.lesprom.com/news/56334>

⁹ This will solve contradictions between forest users and ecological organizations

- (iv) Possibility to use means from the forest construction funds of RF entities and municipalities for construction and maintenance of common use roads which are also used for forest exploitation.
- (v) The provision of long term subsidies to forestry complex enterprises for a partial re-imburement of interests on credits for technical (re-)equipment and preparation of projects on value added processing.
- (vi) Elaboration and introduction of a common information system (data base) on timber harvesting and round wood turnover.

As of 2013 interest rate subsidies on loans are to be granted to the organizations implementing priority investment projects aimed at development of high-tech manufacturing facilities¹⁰.

Institutional setup relevant for timber industry

The privatization of timber companies in the 1990 caused the destruction of the existing management structures of timber industry in the country, disruption of production, technological and economic relations in the forest complex, as well as the loss of the strategic goals of its development at the federal level. This was partially the reason why regional administrations took control over the regional forest industry in those RF entities where the forest complex was an essential part of the local economy.

At the national level two public administrations share responsibility for timber industry: the Department of Forestry and Light Industry in the RF Ministry of Industry and Trade (Minpromtorg) and the Council for the Development of the Forest Complex of the RF Government (Table 1.2).

The Council for the Development of the Forest Complex is chaired by the Deputy Prime Minister of Russia. This strengthens the institutional framework for encouraging investments in the value added timber processing and brings the decisions at a higher governmental level, although the Council has the status of an advisory body.

Table 1.3 Timber industry regulating authorities

Regulating authority	RF Minpromtorg Department of Forestry and Light Industry	Council for the Development of the Forest Complex of the RF Government
Status	A structural division of the federal executive authority	A permanent advisory body
Objectives in the Timber Industry Complex (TIC)	1) Development of state policy; normative and regulatory function in forestry, pulp and paper and timber processing industries; 2) Drafting of forest-related industries' development strategies and programs; 3) Impact analysis of various state policy implementation mechanisms and instruments on the development of these industries	1) preliminary review of legal drafts related to the organization of forestry, TIC development, timber market and illegal timber harvesting and trade; 2) preparation of proposals for encouraging investment into the forest complex development, increase of competitiveness of value added timber products, a qualitative change in the structure of exports of timber and paper products; 3) review of draft strategies for the forest complex development and investment attraction plans; 4) preparation of proposals for the improvement

¹⁰ RF Government Resolution N2 (16.01.2013) on the "Rules on Subsidy Provision from the Federal Budget to Organizations of the Timber Industry Complex for a Partial Compensation of the Interest on Credits Obtained in 2012-2013 for Implementation of Investment Projects to Create New High-Tech Manufacturing Facilities"
<http://www.minpromtorg.gov.ru/docs/government/76>

Regulating authority	RF Minpromtorg Department of Forestry and Light Industry	Council for the Development of the Forest Complex of the RF Government
		of public-private partnership in the forest complex

The lack of a specialized high ranking federal executive body, responsible for the TIC management and regulation does not permit to respond adequately and effectively to timber industry problems and hampers the execution of the adopted systemic solutions.

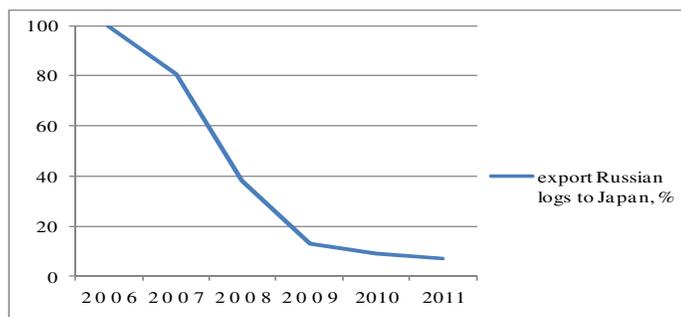
Customs Regulations on Timber Export

A resolution on gradual increase of customs duties on the export of unprocessed timber was adopted in 2007 [11]. It was foreseen to introduce the increase during the period of 2.5 years in three stages: with 15% increase at the first stage; 25% at the second stage, and up to 80% of the contract export price at the third stage. No noticeable changes in the product structure of the Russian timber industry have happened. The decision on raising tax to a punitive 80% across-the-board was postponed twice: first to 2010, then to 2011, and now it has been applied only to above-quota log exports of spruce and pine under the current scheme.

Changes in the Russia export policy provoked changes in the demand-supply structure of the East Asian timber market: buyers from Japan, China, and South Korea began to focus on the round wood supplies from the U.S., Canada, and New Zealand.

This caused the reduction of Russia's share and timber supply to Japanese and Chinese markets. This tendency was particularly evident in Japan (Fig. 1.3).

Figure 1.3 Roundwood exports to Japan



Russia's Accession to the WTO

Russia's accession to the WTO (22.08.2012) brought about changes of regulations on unprocessed timber exports. Thus, in 2012, the Russian government renounced its decision to increase export duties to prohibitive levels, retaining them at 25% [12]. In addition, there was a reduction of customs duty rates on the export of spruce logs (to 13%) and pine logs (to 15%), but only within the limits of tariff quotas [13] (see Annex 1.1). Quotas will be revised every year and are allocated through licenses. The over-quota tariff for these species will be 80%. Quotas on larch wood are not assigned and export duty remained at the same level of 25%. The export duty rate for birch wood was reduced from 25 to 7%, and that for aspen pulpwood was reduced from 10 to 5%. The quota amount exceeds the total volume of Russian timber exports in 2011 (21

million m³). It was done as a compromise with the EU, but China also enjoys some benefits from this decision being a major importer of Russian timber (71.2% of Russia's timber exports in 2011) and the importer of the quota timber (logs).

The reduction of export duties mainly affects the interests of the Russian North-West and Siberia. Its impact on the Far East is less significant, because larch dominates in timber export. It may be expected that a selective duty reduction as related to tree species that are likely to cause dissatisfaction of the Chinese and Japanese importers. As a consequence, the Russian government may make further concessions in the customs duties (for more information on the neighboring countries' policies see Annex 1.2).

The reduction of customs duties on exports of timber, coniferous species in particular, within the newly established tariff quotas allows investors to use the revenue from the round wood export to the completion of timber processing projects. At the same time, due to the reduction of export duties, the round wood export in the North-West of Russia and Eastern Siberia will significantly and almost inevitably increase. This in its turn a roundwood deficit on the domestic market could be expected. As a consequence, this may lead to the rejection of investment projects for value added timber processing [6]. Thus, Russia's tendency for unprocessed wood export will be confirmed as a consequence further limiting this timber market segment.

According the experts of the Russian Economic School and Ernst & Young [15], the reduction of import duties on timber products as a result of Russia's accession to the WTO will cause the increase in volume of imported timber products and, consequently, the decrease in domestic timber industry (by 6.7%). The most disastrous outcomes are projected for the Russian Far East, where the 25.9% decrease of domestic processing is forecasted.

Tax Policy

Timber companies pay a number of general taxes and duties, as well as industry-specific charges. According to the RF Tax Code general taxes are divided into federal, regional and local ones (Table 1.4). Lease-holders, at least large ones, admit that the tax burden is not very heavy for doing business in this sphere.

Table 1.4 Taxes relevant for the forest industry

General taxes and duties			
Federal	Regional	Local	Special charges
- tax on profits - value added tax (VAT) - tax on personal income and insurance premium	- transport tax - corporate property tax	- land use tax	- forest charges - penalties for environmental disruption

In Russian economy value added tax and duties on foreign trade make the major part in the structure of tax revenue. They are also factors that scale down the demand and business activity [15]. At the same time some positive aspects should be noted:

- abolition of export duties on all products of timber processing (plywood, lumber, pulp, paper);

- exemption from import duties and value added tax on manufacturing equipment which is not produced in Russia.

Top priority investment projects

The implementation of top priority investment projects is declared high in the state agenda. In 2012, the Priority Investment Projects list in the forestry sector, approved by the RF Ministry of Industry included 114 projects with total funding of RUR 418.7 billion with annual timber processing volumes expected up to 80 million m³. The actual investment reached only RUR177.9 billion. 24 projects with a total investment of RUR70 billion (USD 2.3 billion) were put into operation [6]. Geographically the projects are primarily located in the European part of Russia (over 70 projects), other 43 projects are located in the Urals, Siberia and the Far East. Such low investment rate can be accounted for the increase of export charges on round wood up to a prohibitive level.

In Khabarovskiy and Primorsky Krai and Amurskaya Oblast there are 10 priority investment projects in timber processing. Most of the projects started before 2007, and were included into the priority list for obtaining privileges. There is no large pulp and paper plant construction projects listed for priority investment due to the need of high investments, lack of well-developed transport and energy infrastructure, and a shortage of skilled labor. Russian and foreign investors consider the investment climate for pulp and paper manufacturing to be still unfavorable.

1.3 Possible investment risks related to forest policy and institutional framework

- Continuous changes in the Russian forest related legal framework which is due to the lack of a comprehensive national forest policy and a clear-cut long-term national strategy for the forest sector development, undermines institutional potential capacities for a steady business in the forestry sector.
- Dual nature of responsibilities and control over the use of land resources (federal and regional levels) imposes bureaucratic protraction in the approval of investment projects. Procedures for administration of land lease intended for construction are complex and lengthy (up to 2 years in some cases). The RF Land Code (Article 30) describes procedures for land plots allotment for construction purposes. Construction plots in municipal and state property are leased through auctions. There are also cases when the land plot has the status of an undivided ownership, i.e. when the ownership is not clearly distributed between the federal government, RF entities and municipalities. The data on forest resource potential are outdated and inaccurate as well as the information about volumes and quality of leasable forest resource; with the actual budget allotment for forest inventory, quality and large scale works to improve the situation are not possible.
- The lack of a cadastre makes impossible the use of leased plots as collateral for loans, subleasing, etc. This limits investment capacities in timber processing¹¹.

¹¹ The Forest Code (2007) provisions on economic use of forest are complaint with the provisions of civil and land legislation. However, the Federal Law on “Enforcement of the Forest Code of the Russian Federation” imposes a time limit for these actions until the state cadastre inventory of forest lands is completed.

- The inconsistency of the Russian government in implementing timber export policy lead to instability in relations between Russian and foreign partners in trading timber products. The decreased demand on foreign markets caused the decrease of round wood export from the Russian Far East, which in its turn resulted in the decrease of employment in timber industry, and a consecutive reduction of tax payments to the budget.
- Lack of established niches on the timber market; strong competition and new types of products pose challenges for Russian manufacturers
- Financial exemptions for investors are very few, and all of them are applied only at the level of RF entities. The exemptions provided in timber industry (obtaining forest plots without an auction and privileges on forest charges) help only to save operating costs.
- The existing system of tax revenue distribution between the federal and regional budgets does not encourage regional authorities to attract investment because a part of this revenue is returned to the federal government through taxes on the activities of investors.
- RF Forest Code and related regulatory documents do not give clear provisions for the construction and maintenance of forest roads. The rights and conditions of forest road exploitation for the lease holders who built this road, are not clearly defined neither for the in-lease contract period, nor for the post-contract period [17].
- The privileges for investments in timber processing in the Russian Far East cannot be considered as strong incentives: timber charges in Russia are less than 1% of the cost of timber harvesting, whereas large forest lands with high-quality timber, located in the areas with developed road infrastructure, are almost unavailable.

1.4 Recommendations for creating favorable policies and institutional environment to encourage investments into value added timber processing

1. Once a national forest policy is adopted defining of a long-term strategy for forest sector development with clear-cut objectives and priorities; once a relevant package of regulations ensuring their implementation is elaborated, **a 5-10 year "moratorium" on amending major basic norms and regulations** as well as reorganizations of public institutions controlling timber industry should be imposed in order to provide a stable environment for timber business development.
2. A specialized **high level federal executive body** responsible for the forest complex management through the integration of forestry and timber industry should be established.
3. A full-fledged **financing of forest inventory** from the federal budget should be guaranteed (alternative sources may be searched for) in order to provide accurate information about the quality and quantity of forest resources available for investors.
4. The **state cadastre of forest plots** should be completed to enable the introduction of leased forest plots into the economy utilization in accordance with civil and land legislation.
5. It is recommended to **authorize the lease holders to fight fires** on the leased plots without license in order to reduce risks of timber loss thus encouraging further processing.
6. Federal authorities should **compensate the costs of forest and fire management** works carried out by the lease-holders through re-investment of forest fees into the fire-management (*mechanism of forest charges should be defined and introduced*).

7. It is necessary to change the calculation principles for the **resource fees** while leveling them to the costs of performed forest management activities. A new mechanism allowing the **reinvestment of resource fees** into forest management should be defined. The increase of timber fees (standing timber fee) will make it an effective incentive, encouraging investments into timber processing.
8. The **procedure** for obtaining the status of a priority investment project should be **simplified** through abolishing the requirement to provide additional explanatory documents.
9. Transport and energy infrastructure should be developed for creating new industrial sites (greenfields) in order to encourage investor to develop large timber-processing and pulp and paper plants.

2. RFE institutional environment for the timber industry complex

2.1 Specific policies and institutional framework to encourage investment in the RFE

According to the RF administrative division the Far East belongs to the Far Eastern Federal Okrug (FEFO) and consists of nine regions: the Republic of Sakha (Yakutia), Primorsky, Khabarovskiy and Kamchatskiy Krai, Amurskaya, Magadanskaya, Sakhalinskaya and Jewish Autonomous Oblasts and Chukotskiy Autonomous Okrug. Timber industry is most developed in the Khabarovskiy and Primorskiy kraia, and the prospects for further industry development are associated with these regions.

In the past recent 3-4 years Russian federal and regional authorities have been giving increased attention to the creation of favorable business climate in national economy in general, and to investments promotion in particular. The main impetus from the federal level sets the institutional framework for implementation at the regional level. In 2012 the **RF Ministry on the Development of the Far East** [26] was established to coordinate the implementation of government programs, as well as to control the execution of powers delegated to local authorities. A special **Council on Encouragement of Foreign Investment** was formed under the RF President Plenipotentiary Representative in the Far Eastern Federal Okrug to improve the investment climate in the FEFO.

Fund for the Development of the Far East and the Baikal Region [27] was established in 2011 under the auspices of the Vnesheconombank (State Corporation “Bank for Development of Foreign Economic Activity”) to provide investment consulting for regional authorities and investors, as well as to partially finance investment projects carried out in the Far East.

In order to stimulate investment processes in the most competitive sectors of the RFE economy, including the timber industry complex, and to overcome the risks of the region a federal target program on “**Economic and Social Development of the Far East and Zabaikalje till 2013**” was adopted and implemented during 17 years (1996-2013) [24]. The program proposed to use the funds of the RF Investment Fund (IF established at the Federal level to finance large projects of minimum RUR5 billion value, and used exclusively for infrastructure) to assist the creation of value added timber processing in the region, but this proposal has not yet been realized. The intended risks were only partially mitigated. Infrastructure constraints were eased and primary timber processing began to develop, but without high added value. A complementary *Strategy of Social and Economic Development of the Far East and the Baikal Region for the period up to 2025* was adopted in 2009.

Far Eastern kraia and oblasts have their own regional peculiarities. Keeping in mind that the federal government sets the 'general tone' in creating the legal framework, including the investment environment, regional policy instruments to attract investment to local economies are rather similar. However, as the RF entities have to compete for investments among themselves, each region tries to find its own approach to encourage investment (Annex 2.1) and to soften administrative barriers (Annex 2.2). In the staff of regional authorities there is a serious lack of specialists with specialized training capable to effectively support elaboration of projects, manage project approvals, and coordinate such activities.

2.2 Transport

Underdeveloped logistics and infrastructure are the biggest obstacles for the timber business development in Russia, although possibilities of the Baikal-Amur Mainline (BAM) development are being discussed nowadays. BAM is connected with Vanino Port and its improvement will increase its transportation capacity and reduce the time of delivery. The following three major challenges related to transport policy can be indicated:

- (i) underdeveloped forest roads network and their low quality;
- (ii) weight restrictions for timber transportation by road (restrictions on large goods vehicles driving on the existing roads were enacted in 2009) [16];
- (iii) a sharp increase in tariffs for railroad transportation; low capacity and poor quality of services

Directly or indirectly these problems lead to the increased costs and price of the final product. Road users are obliged to compensate the damage caused to the road, if the weight of the loaded vehicle exceeds the norm set. This creates an additional financial burden on road users, as the monetary compensation of damages is too high and unaffordable even for big companies. According to experts of the RF Chamber of Commerce and Industry, these payments per one cubic meter of timber in Russia amount to 600-700 rubles (15-18 euros), while in Germany it is only 65 rubles (1.6 euro) [7]; The analysis of the cost of timber in stock at the processing plant showed that transport costs in the price of timber reaches at least 65% of the cost of raw materials in downstream products (which is up to 35% of the final product price). This reduces the competitiveness of domestic products [7]. Additional expenses for timber transportation by railway should be included in investment plans at the project design stage.

2.3 Energy infrastructure

According to the World Bank, Russia is the last one among 183 countries in the ranking of the availability of connection to the power supply network [18]. Power supplying companies quite often violate legal requirements and regulations. Their denials for services are rather numerous and frequently unsubstantiated and connection procedures are very time-consuming for customers [19]. The creation of supplementary power-generating facilities is highly expensive for the investor. For example, the MDF manufacturing company (built by a Malaysian company) in Khabarovsk spent 10 million U.S. \$ on such a facility. At the same time the foreign investor must transfer the power-generating facility to the power supply network operator.

The above mentioned is a serious constraint for the Russian business, hence in 2012 an action plan ("the road map") was approved to ease the conditions for the connection of customers to the

energy infrastructure in Russia. It is proposed to make the network connecting procedure easier, faster, more transparent and less costly.

2.4 Human resources and demographic policy

Four important human resources issues are to be stressed in relation to the encouragement of investments into the forest sector:

- (i) the protection of the rights of hired workers,
- (ii) the general labor force deficit in the Russian Far East,
- (iii) the shortage of qualified workers, and
- (iv) the foreign labor intake.

The rights of forest industry workers are nowadays protected by the Agreement for 2012-2014 [20] between the RF Forest Industries Workers Union and the employers of pulp and paper, wood and furniture industries. The Agreement states payments of bonuses and wage coefficients for workers in the Far North and in the southern parts of the Far East.

Since 2012 the employers are obliged to compensate their employees working in the Far North and similar areas (most of the Far East) expenses for regular travelling to the place of vacation and back. The deficit of labor force is a common problem in the Russian Far East. The region occupies 36.1% of Russia's territory but its population is only 6.3 million people or 4.4% of the Russian total. For the recent two decades the demographic potential of the Far East has been decreasing due to the natural population loss and migration, the latter factor being dominant. In 2001-2011 the decline of population was 841,000 people. Out of that the natural population decline was 18%, and the outflow migration made 82%.

The average population density is one person per a square kilometer. Three quarters of the population live in the southern part of the Far East, mainly in the regional centers. Living standards in the region are lower than Russia's average and effective incomes of Far Eastern population make up only 40% of the national average [21]. When developing investment projects the investor should consider the local labor deficit and additional funds to attract labor from outside the Far East.

The local labor deficit forces entrepreneurs to attract both engineering personnel and workers from outside the region. The existing system of quotas for foreign labor is inadequate and requires unnecessarily long procedures for processing employers' demands. Often the expressed demands are not satisfied. The Concept of the *State Migration Policy of Russia* until 2025 [22] was adopted in 2012. It sets the task to stop migration of people from the Far Eastern regions by 2020. The Concept also sets the task to develop differentiated mechanisms of attraction, selection and employment of foreign labor according to the needs of Russian economy.

2.5 Environmental initiatives

The RF Forest Code divides forests by the purpose of use into protection forests, exploited forests and unexploited (reserved) forests. Some areas in any forest type may be allocated under a "special protection". Forest harvesting and construction of timber processing infrastructure are prohibited in protection forests and special protected areas. Some of these areas are created to

fulfill Russia's international obligations as a participant of international conventions and agreements¹². There is a gap between international commitments, taken by the federal government, and their local implementation. In some forest-rich areas of the Far East the establishment of protected plots in exploited forests (as required by the Forest Code) has not been completed. The boundaries of such protected plots in the leased forest lands are not clearly marked, which causes disputes between forest users and environmental organizations.

Along with other programs, the *Global Tiger Recovery program* (Russia joined it in 2010) is very important for the Russian Far East [23]. Its implementation will help review, strengthen and expand the network of special protected areas in the Far East, but before it is properly regulated, it gives some grounds for disputes between the ecological organizations and forest users. The above uncertainties add to the general complexity of the institutional framework to be taken into consideration while preparing investment projects.

2.6 Recommendations for creating favorable institutional conditions for investment into value-added timber processing

1. Government measures should be undertaken to define and fix **clear and simple procedures** for the attribution of public lands to the federal government, RF entities and municipalities as well as land allotments for mill construction purposes.
2. To enhance **effective development of value added timber processing** in the Russian Far East the Federal government should provide financial support through increasing the number of investors possessing the right to state guarantees for loans (according to the RF Government resolution on the "Adoption of the Rules on Subsidy Provision to Organizations of the Timber Industry Complex to Compensate a Part of the Interest on Loans Obtained in 2012-2013 for the Implementation of Investment Projects to Create New High-Tech Manufacturing Facilities").
3. **More tax incentives** for investors are needed to reduce capital costs of investment projects.
4. The government as the owner of forests should invest into the **construction of major roads** and include these costs in the increased forest charges. This would be one of the mechanisms to stimulate investments into timber processing. Businesses can build local roads to connect with the major ones, built by the state.
5. **Regulations, norms and standards of forest roads use** should be revised.
6. The efforts **to improve the system of quotas for foreign labor** should be intensified.

¹²Russia has signed 18 international conventions and agreements of legal status, 8 of which are directly or indirectly related to forest conservation and use.

2.7 Investment risks in the Russian Far East timber industry and their recommended mitigation

Risks of investing into the RFE forest industry are caused by a number of existing problems, which in Table 2.1 are grouped by types of risks.

Table 2.1 Types of risks for investments in the RFE forest industry

Risk type	Risk
Legal	<ul style="list-style-type: none"> - Lack of a national forest policy and a consistent long-term government strategy for the forest sector development; - Frequent changes in forest legislation; - Incomplete cadastral inventory of forest lands limits their involvement in economy
Institutional	<ul style="list-style-type: none"> - Numerous reorganizations of forestry sector management authorities; - Lack of a specialized high level federal executive body responsible for managing the timber industry complex; - Licenses are needed to be able to fight forest fires; - Lack of clear regulations on the construction and maintenance of forest roads; - Boundaries of special protected areas in exploited forests are not yet defined; - Privileges on resource charges and obtaining forest lands without auctions are not sufficient incentives for investments in timber processing; - Inconsistency of the timber export policy; - Lack of qualified specialists in government bodies in charge of investment promotion
Information	<ul style="list-style-type: none"> - Inadequate information on the quantity and quality of forest resources to be leased due to reduced government financing of forestry management and inventory activities; - A large package of documents of supporting and informative character is needed to put an investment project on the priority list
Resource	<ul style="list-style-type: none"> - Shortage of timber due to the depletion of available high quality and accessible resources
Infrastructure	<ul style="list-style-type: none"> - Low supply of industrial sites, for which the issues of transport, engineering, and energy infrastructure have been settled; - Long and complex procedures of connections to energy supplies; - Growing railway tariffs, lack of wagons, increasing time of cargo delivery
Market	<ul style="list-style-type: none"> - Shortage of niches for new products and strong competition in the existing ones; - Lack of demand on the domestic market
Labor	<ul style="list-style-type: none"> - General labor shortage in the Russian Far East; - Shortage of qualified engineers and skilled workers; - Unbalanced supply of trained workers not matching wood industry demands; - Imperfect system of quotas for foreign workers with lengthy application procedures
Financial and economic	<ul style="list-style-type: none"> - Rise in costs due to the additional cost of forestry management and forest fire fighting, which tenants have to bear the increase of costs on raw materials; - Tenants have to bear the costs of road construction and maintenance to develop leased forests; - Lack of affordable long-term credit offering in the Russian banks; - Reduction in the interest rate subsidy for logging companies to create intra-seasonal reserves;

Risk type	Risk
	<ul style="list-style-type: none"> - High ratio of capital to output in deep timber processing; - Lack of privileges on capital expenditure for investors implementing investment projects in forest exploitation; - Additional costs of fines due to numerous scheduled and unscheduled inspections

Most risks are related to the institutional, financial and economic risks. In many ways, the financial and economic risks are caused by the institutional risks, which are partly the result of legislative and organizational activities of the federal government. Therefore, to remove the risks several actions should be taken mainly at the federal government level, but also at regional and local levels. In addition, some activity is also required from the business (Table 2.2).

Table 2.2 Recommendations on investment climate improvements to create value-added timber processing

Type of risks	Recommendations to mitigate risks	Implementing level: federal, regional, local, business
Legal	A well-grounded national forest policy and long-term national strategy for forest sector development with clear objectives and priorities should be adopted together with a package of regulations to ensure their implementation. They should be followed by a ‘moratorium’ on amendments of regulatory documents for a period of 5-10 years.	federal
	The state cadastre of forest lands should be completed to make possible the involvement of leased forest lands in the economy compliant with civil and land legislation.	federal
	The legal division of lands between the federal government, federal entities and municipalities will help reducing the time of obtaining land for the construction of processing facilities.	federal, regional, local
Institutional	A ‘moratorium’ on reorganizations of TIC managing bodies should be announced in order to provide a stable business environment in the forest sector.	federal
	A specialized high level federal executive body should be established to manage activities in the forest complex composed of the forestry and timber industry complex.	federal
	To reduce the risk of loss of raw materials and reduction of the base for timber processing, tenants should be able to fight forest fires without having a license for that activity.	federal
	The principles of payment for resources should be changed and associated with the degree of forestry management costs. A relevant mechanism should be developed to make possible the use of forest charges to finance forestry management.	federal
	The procedure of obtaining the status of a priority investment project should be simplified discharging investors from the obligation to provide excessive documents of supporting and informative function.	federal
	Measures should be taken to shorten the time of obtaining land for	regional

Type of risks	Recommendations to mitigate risks	Implementing level: federal, regional, local, business
	the construction of processing facilities.	
Information	Forest management activities should be entirely financed by the government in order to provide investors with reliable information on the number and quality of the forest resource to be leased.	federal
Infrastructure	Industrial sites with developed transport and energy infrastructure should be created to encourage investors to establish efficient timber processing companies.	regional
	The government should participate in investing the construction of major timber transport roads in the undeveloped forest massifs.	federal, regional,
Labor	While designing investment projects, the investor should consider the local labor shortage and should plan for additional costs and incentives on labor brought from outside the Far East.	business
	Efforts to improve the system of quotas for foreign labor should be more efficient, supported by practical measures	federal
Financial and economic	Forestry and forest fire fighting activities of the tenant should be compensated through a return mechanism in forest charges.	federal
	There is a need to accelerate the adoption of the draft RF Government Resolution on “Adoption of the Rules on Subsidy Provision to Organizations of the Timber Industry Complex to Compensate a Part of the Interest on Loans Obtained in 2012-2013 for the Implementation of Investment Projects to Create New High-Tech Manufacturing Facilities”.	federal
	To finance the establishment of investment projects the mechanism of state guarantees for bank loans should be improved.	federal, regional,
	The authorized bank for priority investment projects in the forest sector should be selected and provide 8-10 year loans for timber industry.	federal
	More tax incentives for investors to reduce their capital costs should be initiated.	federal, regional,
	It is necessary to abolish payments for road damage, caused by excess-weight timber haulers and to keep only traffic restrictions in time of the spring thawing.	federal, regional,
	While designing investment projects, the investor should consider additional expenses for timber transportation by railroads.	business

It seems important to amend the existing legislation, to ensure law enforcement by the state authorities as well as to increase the responsibility of the authorities for action against violations. The government has to clarify its **position for business in terms of resource use**, following national priorities, and to **provide a stable environment for investors**.

Annex 1.1 Russia's tariff rate quotas (TRQ) for the export of unprocessed timber, thousand m3

Tree species	Tariff		Quota	
	within quota	outside quota	2012	2013
Common spruce (<i>Picea abies</i> Karst.) and common silver fir (<i>Abies alba</i> Mill.) (CN FEA CU* codes 4403 20 110 and 4403 20 190), total	13%	80%	2082.2	6246.5
including:				
to the European Union			1986.9	5960.6
to other countries			95.3	285.9
Common pine (<i>Pinus sylvestris</i> L.), (CN FEA CU* codes 4403 20 310 and 4403 20 390), total	15%	80%	5346.1	16038.2
including:				
to the European Union			1215.3	3645.9
to other countries			4130.8	12392.3
Larch	25%		n/a	n/a
Birch	7%		n/a	n/a
Birch (diameter under 15 cm)	0%			
Aspen	5%		n/a	n/a

* Note: CN FEA CU – Commodity Nomenclature for Foreign Economic Activity of the Customs Union

Source: State Russia Duma, 2012, p.871

Federal Russian Duma. (2012). Official website of the Duma for Bill No. 89689-6 "On ratification of the Protocol on the Accession of the Russian Federation to the Marrakesh Agreement about World Trade Organization Accession beginning April 15, 1994. Automated System for Ensuring Legislative Activity."

Annex 1.2 Review of forest policies in the North-East Asian countries

Japan

The general tendency of the Japan's forest policy is the shift in forest management goals from forest commercial use to biodiversity conservation and recreation.

The main problems of the Japanese forest sector are as follows:

- The timber demand is reducing due to increasing use of alternative materials, changes in the methods of construction and its reduction.
- Labor force aging and attrition as well as reduction of young labor sources happen due to low attractiveness of work.
- Forests degrade and domestic timber loses its competitiveness against cheap and good-quality imported timber [28].

Since 2012 the Forest Agency of Japan has launched several model projects under the new policy. They are supposed to reduce costs in the woodworking industry. Approximately 40% of the timber demand in Japan goes into wooden house building. Nowadays house-building companies are using local timber more actively, also owing to the incentives of special programs. Japan's revision of its energy policy after the *tsunami* in 2011 favorably effected the development of bio-energy production from wood biomass [29]. The incentives for the use of local timber will further reduce the roundwood import from the Russian Far East.

Republic of Korea

At present Korea is implementing the Fifth National Forest Plan (2008-2017) focused on the multi-use development of forest resources; the restoration of the timber industry and increase of its competitiveness; the conservation of forests as a national resource of the country; the creation of a 'green space' to improve the quality of life; strengthening of international cooperation in the use of resources and the global forest cover preservation [30].

The country has established a full-scale system of creating and maintaining recreational forests. Korea's self-sufficiency in timber is very low. Thus, in 2010 only 10% of the timber demand was satisfied with own resources, the rest being imports. Korea plans to increase the national timber share to 22% by 2020 and to 36% by 2040 and is actively expanding forest plantations abroad. The RK Government has designed a program for large-scale wooden housing by the Japanese model to be implemented in the next 15 years.

Peoples' Republic of China

In 2011 China reached a record level of timber imports (\$ 8 billion), and became the world's largest importer of round and sawn timber [31]. Russia is the major exporter of timber products to China, and in 2011 it exported 2.8 million m³ of sawn timber and 20.7 million m³ of round wood [32].

As a result of over-exploitation of forests by the end of 1990 China introduced a new forest policy aimed at increasing forest regeneration and limiting timber harvesting in the north-eastern part of the country. Particular emphasis is given to the importance of enhancing cooperation in the deep timber processing with Russia, creating mechanism for joint fighting of forest fires [33].

The following main tendencies of China's forest policy can be identified [34]:

- the integration of forestry, timber harvesting and processing industries;
- increasing use of timber, especially in construction;
- state incentives to diverse forms of ownership in forestry and timber processing;
- The Chinese government uses market instruments for resource mobilization.

The following main problems in the Chinese forest sector may be listed:

- low productivity of forest plantations and a high level of investments with low investment returns;
- a high ratio of labor to output;
- low rates of economic development in rural areas;
- shortage of forest resource.

The inter-governmental program of cooperation between the regions of the Far East and Eastern Siberia of the Russian Federation and the North-East of China (2009-2018) may be considered an instrument of cross-country regional cooperation in forest management [35]. 23 joint timber processing projects are proposed to be implemented under these programs. One of the projects is to build a center of deep timber processing (RFP Group) in Amursk (Khabarovsky Krai). Russia-China Investment Fund (RCIF) allocated \$ 200 million for this project.

Annex 2.1 Policies to attract investments in the RFE

Indicator	Khabarovsk Krai	Primorsky Krai	Amurskaya Oblast	Sakhalinskaya Oblast
Regional specifics	<ul style="list-style-type: none"> - population density is 1.7 persons / km²; historical practices of timber harvesting and processing; - forested area makes 66.7 % of the region total area; - total timber reserve is 5.2 billion m³; - the biggest TIC in the RFE with timber harvesting share of 50 % of total Far East harvesting; - timber export of 68 % of total Far East export; - timber processed goods make 20% of harvested timber volume; - oriented to the markets of China, Japan and the Republic of Korea 	<ul style="list-style-type: none"> - population density is 11.84 persons / km²; - historical practices of timber harvesting and processing; - forested area makes 77.9 % of the region total area; - total timber reserve is 1.9 billion m³; - 32 % of the RFE timber harvest and 24 % of the RFE total export; - oriented to the markets of China, Japan and Republic of Korea 	<ul style="list-style-type: none"> - population density is 2.27 persons / km²; - forested area makes 65 % of the region total area; - total timber reserve is 2.0 billion m³; - 90 % of total timber harvest is unprocessed; - 50% TIC share in the oblast export; - oriented to the markets of China 	<ul style="list-style-type: none"> - population density is 5.69 persons / km²; - historically, it was the most developed region in pulp and paper industry; - forested area makes 67.7 % of the region total area; - total timber reserve is about 0.6 billion m³; - forest resources are depleted, there little stock of high quality timber; - unprocessed timber is not exported because of high customs tariffs
Responsible authorities	<ul style="list-style-type: none"> - Forest management department, Khabarovsk Krai Government; - Timber industry committee, Khabarovsk Krai Ministry of natural resources; - Inter-industry commission on promoting priority investment projects for timber processing, implemented in Khabarovsk Krai 	<ul style="list-style-type: none"> Primorsky Krai forestry department Council on foreign investment attraction to Primorsky Krai 	<ul style="list-style-type: none"> Amurskaya Oblast forestry department 	<ul style="list-style-type: none"> Sakhalinskaya Oblast Ministry of forestry and hunting management
Major regulatory	<ul style="list-style-type: none"> - Forest Plant of Khabarovsk Krai for 2009 – 2018; 	<ul style="list-style-type: none"> - Forest Plant of Primorsky Krai for 2009 – 2018; 	<ul style="list-style-type: none"> - Forest Plant of Amurskaya Oblast for 2009 – 2018; 	<ul style="list-style-type: none"> - program “Support for the timber industry complex development of Sakhalinskaya

Indicator	Khabarovsky Krai	Primorsky Krai	Amurskaya Oblast	Sakhalinskaya Oblast
documents	<ul style="list-style-type: none"> - The main directions for the development of the forestry sector of the Khabarovsky Krai in 2013-2015 and up to 2020; - Law “On the state investment policy in the Khabarovsky Krai”; - Law “On the regional taxes and tax reductions in Khabarovsky Krai”; - Law “On the procedure for selection of applications for the implementation of priority investment projects in the area of forest development in Khabarovsky Krai”; - Target Program “Increasing the investment attractiveness and investment climate of Khabarovsky Krai for the period 2012 - 2015 years”; - Target program “Promoting economic development, competition, investment and foreign trade in Khabarovsky Krai”; - Regulation on support for major investment projects implemented or planned for implementation in Khabarovsky Krai 	<ul style="list-style-type: none"> - Strategy for social and economic development of Primorsky Krai for the period up to 2025; - State Program of Primorsky Krai “Economic Development and innovative economy Primorsky Krai” for 2013 - 2017 years; - The procedure for selection of applications for the implementation of priority investment projects in the area of forest development in Primorsky Krai 	<ul style="list-style-type: none"> - Key tendencies of the development of oblast timber industry complex for 2007 - 2010 and for the period up to 2020; - Law “On Investment Activity in Amurskaya Oblast”; - Law “On the Procedure of state guarantees of Amurskaya Oblast”; - The procedure for selection and approval of applications from commercial organizations for the implementation of priority investment projects in the area of forest development in Amurskaya Oblast 	<ul style="list-style-type: none"> Oblast until 2017”; - Law “On state support of investment activity in Sakhalinskaya Oblast”
Adopted measures /privileges to stimulate investment	<ul style="list-style-type: none"> - Reduced rates of income tax and property tax; - Privileges for land rent; - Krai Government guarantees; - Assistance in obtaining bank loans; - The introduction of the institution of investment authorized persons; - The introduction of curatorship for investment 	<ul style="list-style-type: none"> - The introduction of the institution of investment authorized persons; - The creation of the infrastructure necessary for the operation of krai priority investment projects; - Development and implementation of the road maps for reducing 	<ul style="list-style-type: none"> - Assistance to enterprises to purchase of timber harvesting and processing equipment using leasing schemes; - Creation of a center of training for TIC; - Assistance to enterprises to raise funds to create timber 	<ul style="list-style-type: none"> - The development of a network of timber roads due to the reimbursement of expenses to tenants for their construction; - Subsidizing the cost of connection of sawmills to the power supply system; - Subsidizing part of the cost for

Indicator	Khabarovsky Krai	Primorsky Krai	Amurskaya Oblast	Sakhalinskaya Oblast
	<p>projects;</p> <ul style="list-style-type: none"> - Additional exemptions for forest payments to the krai budget; - Development of contract based vocation training based on orders/demands from the forest industry; - Providing advice to forest enterprises on foreign trade; - Assistance in addressing issues of transport infrastructure of the krai timber industry facilities included in the list of priority projects 	<p>administrative barriers to business;</p> <ul style="list-style-type: none"> - Development of the catalogue of Primorsky Krai investment projects 	<p>processing facilities;</p> <ul style="list-style-type: none"> - Tax credits and deferrals for regional taxes; - Investment tax credits; - State guarantees area; - Leasing of concessional lands 	<p>loans for big investment projects;</p> <ul style="list-style-type: none"> - Subsidizing part of the cost of the interest on loans for the purchase of new equipment; - Training specialists in forestry and technology; - Exemptions on taxes, subject to the oblast budget; - State guarantees Sakhalinskaya Oblast; - Assistance in obtaining approvals and permits from government, selection of production facilities for investment projects; - Investment tax credit
Projects (federal and regional)	Federal: JSC “Amur-Forest”, JV “Arkaim”, “Rimbunan Hijau MDF”, “RFP Group”, LLC “Asia Les”, LLC “Berezovy”, Krai: LLC “Ros-DV”	Federal: JSC “Terneiles”, CISC “Iseexport”; JSC “Primorskie timber users”	Federal: LLC “Mostpootryad-T» and CJSC “Turanles”; Regional: LLC “SK Vostokinvesksroy”; LLC “Amur – Forest”	JSC “BM Sakhalin” going to implement joint activities for the investment project on the complex timber processing

Annex 2.2 Areas where administrative barriers are to be removed

Area	Actions
Business registration	<ul style="list-style-type: none"> • restrict the list of documents required for the registration to the most essential ones, i.e. authorities have no right to demand extra documents beyond the specified list; • business registration should not exceed 5 days; • introduce "one window" procedure, i.e. business registration at multi-service centers, which provide state and municipal services; • replace the practice of demanding special permissions for business initiation by pure information notice ("notification regime") for 3/4 types of business activities
Inspections of businesses by controlling bodies	<ul style="list-style-type: none"> • ban non-judicial suppression of activities and licenses; • limit the frequency of scheduled inspections and fix them to 1 inspection every 3 years, unscheduled inspections may be permitted only with the sanction of the prosecutor; • introduce inspectors' responsibility for violations of norms and regulation while carrying out state inspections
Mandatory certification of goods (works, services)	<ul style="list-style-type: none"> • decrease the share of obligatory state quality certification of products from 78% to 46% as a sign of trust to business quality • increase the share of the goods to be declared from 22% to 54%

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