



Doing Business in Russia

Trade Controls Conference 2017

Vladimir Efremov, Partner, Moscow

8 November 2017



1

Developments in the Eurasian
Economic Union (EAEU) and
Customs Regulations

Russia and Eurasian Economic Union (“EAEU”)

- Russia is a member of the Eurasian Economic Union (Russia, Belarus, Kazakhstan, Armenia and Kyrgyzstan, “EAEU”) since 2015
 - unified customs territory, customs regulations (tariff regulations, non-tariff, sanitary, technical regulations)
 - safeguard (antidumping) measures, regulations on special economic zones
 - indirect tax regulations (VAT and excise duties) on trade in goods, works and services
 - partially unified: IP regulations and turnover of medicinal preparations
- EAEU issued a number of regulations which are officially stated to be compliant with the WTO Agreements and Russia's obligations and commitments within the WTO
- Penalties and law enforcement are established and performed at the local (national) level
- **Main bodies of the EAEU:**
 - EAEU Highest Counsel (heads of states) – legislative role
 - EAEU Commission – implementing regulations, executive role
- By 2020 the EAEU plans to increase integration on the following spheres: export controls, energy policy, trade in services, currency control regulations, IP, antitrust regulations, public procurement, natural monopolies, etc.

New Customs Code of Eurasian Economic Union (“EAEU”)

- **New Customs Code** of the EAEU is expected to come into force starting from January 1, 2018 to codify over 17 supranational acts of the EAEU and simplify customs regulations
- Why the new Customs Code is needed:
 - since 2010, the Customs Union and the EAEU issued a large number of supplementing and implementing regulations in the customs sphere which are difficult to apply
 - the current Customs Code has been actively criticized and needs to be replaced
- **What's new:**
 - electronic (on-line) customs declaration (paperwork in exceptional cases) – Russia already applies electronic declaration in 98% of cases, but not the other EAEU countries
 - mandatory preliminary notification of the customs authorities about the planned importation, A “single window” – an online service for any interactions with the customs
 - the extended status of Authorized Economic Operators (AEO) (more simplifications in the sphere of customs operations for AEO)
 - branch offices as IORs
 - more detailed regulations on the application of certain customs procedures:
 - e.g., it is expected that foreign companies would be able to place their goods at customs warehouse in Russia without a local IOR (now this rule is dormant)

Enforcement Issues (1)

- The Russian customs authorities traditionally apply a formalistic and pro-budget (fiscal-oriented) approach to the customs clearance of goods:
 - a list of major Russian importers that could pay additional amounts of import customs duties and import VAT and increase collections to the state budget
 - Federal Customs Service Order No. 280 of 16.02.2016 = increase of customs control
- Performance of the Russian customs authorities for the 1st 3 Quarters of Y 2017:
 - imposed RUB 121 bln (or USD 2 bln) in fines for illegal imports
 - imposed RUB 19,3 bln (or USD 340 mln) of fines for currency control issues
 - opened 84,311 administrative investigations (increase by 42,3%)

Enforcement Issues (2)

- **During the importation and customs clearance any uncertainties / discrepancies in the provided documentation are viewed as formal grounds for:**
 - initiation of administrative/criminal cases against the IORs, and
 - customs value adjustment increasing customs payments
- special focus on:
 - **interrelation between** the exporters and Russian IORs
 - higher prices have been declared to the customs for the same/similar goods within the 3 months prior (or after the supply)

Customs Law Enforcement Issues (3)

- **After the importation**
- more frequent “post clearance” customs audits
- initiation of administrative / criminal investigations
- customs value adjustment and increase of customs payments
 - change in HS classification of goods (reclassification)
 - customs valuation issues and inclusion of royalties into customs value
 - deny application of reduced 10% rate of import VAT or VAT exemption
- deny return of customs deposits after the importation
- **Other problematic areas (non-tariff measures and export controls)**
 - import/export **encryption clearance** - much more difficult to register notifications for encryption-based products with the Federal Security Service (“FSS”)
 - increased focus on **export controls** – more frequent on-site audits performed by the Russian Federal Service for Technical and Export Control (“FSTEC”)



Technical Regulations – Labeling Issues

- The majority of B2C products require mandatory confirmation of conformity (“certification”) in accordance with EAEU/Russian technical standards
 - e.g.: vehicles, machinery, IT/telecom equipment, certain food products, etc.
- Certificates/declarations of conformity:
 - “one shot” certificate/declaration - for 1 shipment (holder = Russian importers of record)
 - “serial/unlimited” (holder = authorized representative of foreign vendor)
 - Protocol on Technical Regulations of the EAEU Treaty (2015) introduced a definition of “**putting into circulation**” = local manufacturing and/or **importation**
- Possible compliance issues related to the certification:
 - the “EAC” sign (unified sign of conformity) and other mandatory labeling must be placed on the product/consumer package **before** the importation to Russia
 - some Russian importers use “fake” test reports, which triggers substantial legal risks (criminal and administrative cases, reputational risks, etc.)



2

Impact of Ukraine-Related Sanctions on Foreign Business in Russia – Market Access

Russia's Direct Response to Ukraine-Related Sanctions

- Travel ban for certain western politicians (list is not fully disclosed)
- Food import ban (Decree of the Russian President No. 560) introduced in August of 2014 was extended to be effective until December 31, 2018 (this term may be further extended)
 - covers specifically listed by HS codes meat, poultry, fish and sea products, milk and dairy products, certain types of vegetables, fruits, nuts (subject to certain exceptions) and, starting from November 1, 2016, salt
 - originating from the EU, US, Canada, Australia, Norway (from August 7, 2014), Albania, Montenegro, Iceland, Liechtenstein (from August 6, 2015) and Ukraine (from January 1, 2016)
- Starting from August 6, 2015 the illegally imported products found in Russia must be destroyed
- In July 2017 Russia ordered US to reduce the number of diplomatic and technical personnel across US diplomatic missions in Russia to 455 people, matching the number of Russian diplomats left in the US after Washington expelled 35 Russians in December 2016. Russia also suspended the use of a storage facility in Moscow and a country house outside Moscow (the US diplomatic properties in Russia)

Public Procurement in Russia

- Public procurement is one of the biggest markets in Russia:
 - in Y 2016 = approx., RUB 5.3 trillion (approx., USD 90 bln)
 - total amount of public procurement, including state-owned corporations, was estimated, approx., to be RUB 30 trillion (approx., USD 540 bln)
- Russia is a member of the WTO, but it has not joined the WTO GPA
- Russian Federal Law on public procurement No. 44-FZ (“**Law No. 44-FZ**”)
 - establishes national treatment for foreign products on the mutual basis, but
 - preserves the right to restrict access of foreign companies and foreign goods
- “Made in Russia” equally applies to goods originating from the EAEU
- On the following slides we summarize all types of restrictions for foreign products/vendors in the sphere of public procurement

Limitations for Foreign Goods in Public Procurement in Russia



- Since 2014 Russia imposed a number of limitations and prohibitions on the access to public procurement for the following types of foreign goods:
 - I. **Ban** on imported goods: light industry products, goods/works/services in the sphere of defense and national security, industrial machines and motor vehicles, software products
 - II. “**3 is a crowd**” rule: radio-electronic devices, food products, medical devices, vital and essential medicinal preparations
 - foreign goods cannot participate in a public tender if there are at least 2 suppliers offering “Made in Russia” products or included into special lists of local manufacturers (depending on the particular types of goods)
 - III. “**2 is a crowd**” rule = established for disposable medical goods made of p.v.c. plastic
 - IV. **15% preference** for locally produced products in public tenders and any goods / services procured by state-owned corporations (i.e., 50% or more owned by the state)
- **Key aspects:**
 - Special lists of goods (listed by “All-Russia” classification codes, “OKPD2”) and special localization criteria (depend on the type of goods)
 - General exemption: absence of locally produced analogues
 - “Made in Russia/EAEU” = Certificate of Origin (“ST-1” form) issued in accordance with the CIS Rules of Origin 2009 by the Chamber of Commerce and Industry

Import Substitution of Software in Public Tenders

- Prohibition for public tenders with respect to foreign software products
 - Governmental Decree No. 1236 dated November 16, 2015 (effective January 1, 2016)
- Special eligibility criteria and market access restrictions to public procurement for almost all types of software products (listed by "OKPD2" codes), e.g.:
 - List of Russian software includes almost all types of software
 - State Register of Domestic Software ("State Register") – includes over 3,900 products
- Eligibility criteria:
 - The exclusive (IP) rights must be 50% or more owned by Russian persons (state or citizens)
 - 30% limit on royalties payable to foreign persons (directly/indirectly)
 - Special eligibility criteria for different types of software (Governmental Decree No.325 dated March 23, 2017)
 - Special requirements for software with data security functions (e.g., anti-viruses, etc.)
 - must be developed under a local license (the FSTEC/FSS)
 - must be certified by the FSTEC/FSS

Alternative Options of Localization

- Special Investment Contracts ("**SPICs**") (Governmental Decree No. 708 dated July 16, 2015) **industrial manufacturing = import substitution**
- SPICs provide the following tax incentives:
 - decreased corporate profits tax rate (0% rate of "federal" portion, right to decrease the "regional" portion down to 0%)
 - accelerated depreciation coefficient
 - property tax incentives
 - other regional and local tax incentives
- Under SPICs investors could get simplified access to public procurement
 - the status of "single supplier"
 - subject to special criteria
- Simplified and accelerated procedure for receipt of the status of "Russian manufacturer"
 - Guarantee of non-increase of the total tax burden



3

Screen your Russian Business Partner

Screening Your Russian Counterparty

- I. Screen the Russian customers/distributors/end-users in advance (and periodically) in order to avoid prohibited transactions with SDN/DP/SSIL
 - Public Joint Stock Companies (PJSC) are transparent: disclose information on their beneficiary owners and board of directors:
 - Quarter reports (published 45 calendar days after the end of each quarter)
 - Lists of Affiliated Persons (published 2 business days after the end of each quarter)
 - Limited Liability Companies (LLC) are relatively transparent (current owners and general managers are listed in the State Register and Spark database)
 - Joint Stock Companies (JSC) are not transparent, only initial founders are available in the official databases
 - Check the company and its management in the tax records, court records (e.g., <https://www.nalog.ru/rn77/>, <http://www.arbitr.ru/>, <http://www.spark-interfax.ru/>, etc.)
 - Media publications, information published on official web-sites of the screened companies



Vladimir Efremov
Partner
Moscow, Russia

Baker McKenzie
Tel: + 7 495 787 27 00
vladimir.efremov@bakermckenzie.com

www.bakermckenzie.com

"Бейкер и Макензи - Си-Ай-Эс, Лимитед" входит в состав Baker & McKenzie International, организации, созданной в форме швейцарского объединения (Swiss Verein), состоящего из юридических фирм - участников объединения в разных странах мира. В соответствии с общепринятой терминологией, используемой компаниями в сфере профессиональных услуг, термин "партнер" означает лицо, имеющее статус партнера в такой юридической фирме или занимающее аналогичную должность. Термин "офис" или "представительство" означает, соответственно, офис такой юридической фирмы.

© 2017 Бейкер и Макензи – Си-Ай-Эс, Лимитед