

# Legal Aspects of Production Localization In View Of Import Substitution Policy

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  - ✓ Import of equipment
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6. Our firm, contacts



# Localization – Advantages, Disadvantages and Current Problems

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## **Advantages:**

- +Lower personnel and production costs due to decrease of ruble exchange rate
- +Possibility to participate at state procurement
- +Support measures with regard to production localization
- +Necessity to increase the localization by automobile producers
- +Possibility to export to Customs Union member countries and other countries

## **Disadvantages:**

- Market instability and decrease of domestic demand
- Volatility of local currency

## **Specifics for automotive suppliers:**

- ?Minimizing the investment volume, use of imported components & creation of Russian-made product
- ?Control of competent authorities and car producer

## Recent developments:

### 1. Restricting access of foreign-made goods to public tendering

(affects a number of sectors including, the automotive, heavy equipment, light industry and medical device sectors, and the list may continue to expand)

### 2. Action plans for import substitution providing for a gradual reduction in the level of foreign goods being consumed in Russia by 2020 in more than 20 sectors of the economy

(machine manufacturing, light industry, oil refining and petrochemical industries, medical and pharmaceutical industries).

### 3. Measures to encourage production localization in Russia - Federal Law “On industrial policy” No. 488-FZ of 31 December 2014, in force since 1 July, 2015.

- ✓ Incentives mechanism to support industrial production & priority for Russian-based manufacturers
- ✓ Criteria for recognition the product as Russian (established by Government Decree No. 719 dated July 17, 2015)

## Applicable methods:

1. Decree No. 719 dated 17 July 2015 - determines the criteria for designation of industrial products as goods of Russian origin with respect to products of six branches of industry:

- machine tool industry
- automobile manufacturing
- special machine building
- photonics and lighting engineering
- power and electrical engineering
- heavy machinery

2. The agreement “On the Rules for Determining the Country of Origin of the Goods in the CIS” dated November 20, 2009 - applicable to the countries participating in the Customs Union and the CIS, in particular, in order to determine whether goods have been produced in Russia.



## 1. Criteria according to Decree No. 719 / depending on the type of product

1. Requirements for products manufactured (as a percentage share of the cost of foreign raw materials and components in the price of the final products, etc.)
2. Requirements for activities of the manufacturer in Russia, including:
  - performance of certain production and technical operations in the territory of Russia,
  - rights of the manufacturer to the product's design and technical documentation;
  - a service center in one of the member states of the Eurasian Economic Union.
3. Combination thereof.

### **Example** - motor cars

Localization criterion - performance of certain technical operations in Russia, e.g.:

- installation of the powertrain, front and rear suspension, exhaust system, steering gear, electric equipment, interior and exterior parts;
- welding;
- car body painting and assembly;
- checkout tests of finished vehicles.

The number of operations performed must increase gradually – currently it is at least 7, from 1 January 2016 – at least 9, from 1 January 2017 – at least 11.

## 2. Criteria according to the CIS Agreement dated November 20, 2009

### 1. Change in the customs commodity code

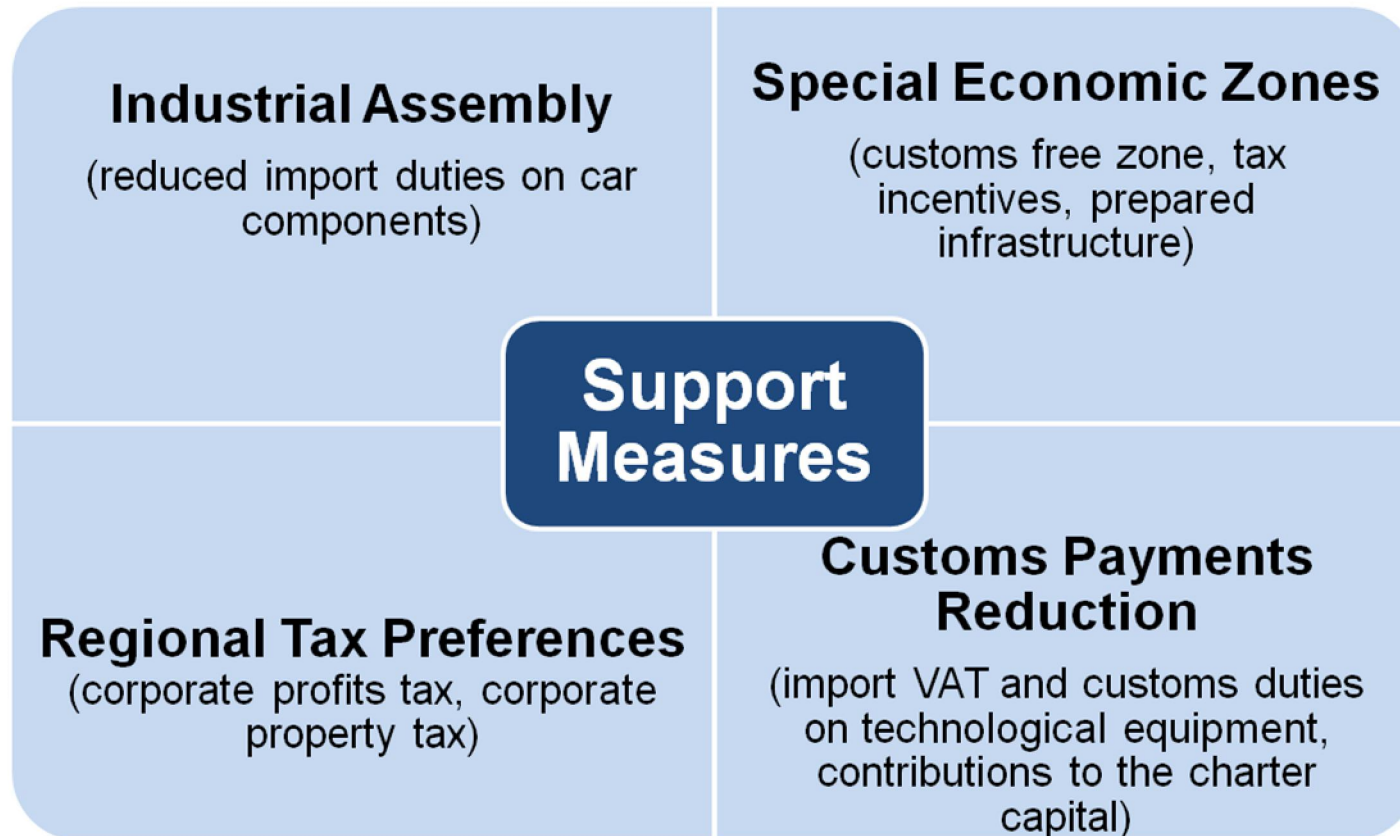
- ✓ at least within the range of the initial four symbols
- ✓ import of set of components to be assembled can be classified as a ready disassembled product → impossible to classify it as a Russian product.

### 2. Performance of certain production and process operations

- ✓ *Practical examples of operations not meeting the criterion of sufficient processing:* cleaning, coating with oxide, oil or other substances; painting or polishing; simple assembly operations (NB: no legal definition for that).

### 3. Ad valorem share rule - the maximum value of imported materials in the finished product

- ✓ materials are evaluated based on their custom value at the moment of their import or on the price of the initial sale in the territory of the manufacturer country;
- ✓ the cost of the final product is evaluated based on the price on the ex works conditions.
- ✓ **Example:** parts of vehicles included in group 87 - the ad valorem share shall be not less than 50%, plastics (group 39) – 80%





## Industrial development funds

- ✓ loans, grants
- ✓ equity participation in project companies, leasing, etc.

## Special investment contracts

- ✓ incentive package
- ✓ stable tax burden
- ✓ Russia is recognised the country of origin of goods



## Financial and tax incentives

- ✓ Subsidies to be granted on the basis of tenders
- ✓ Tax incentives (in particular, for projects approved by the Russian Government, which shall be implemented before 2025)

## Support of industrial parks and industrial clusters

- ✓ Special tax regimes

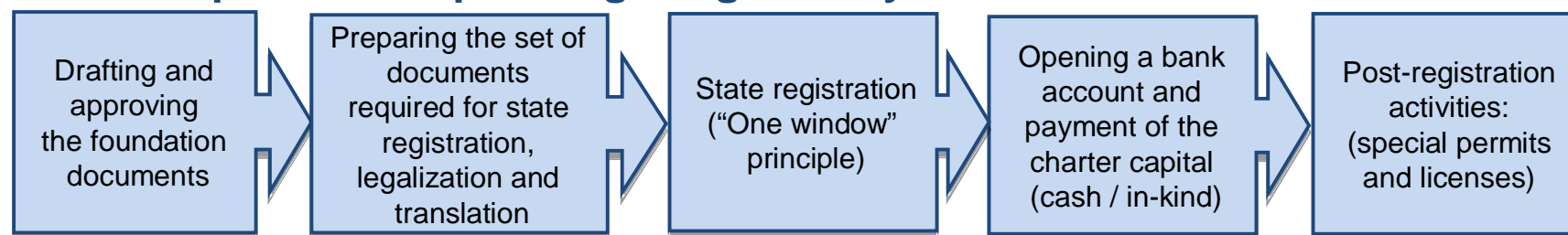
\* Introduced by Federal Law "On industrial policy" No. 488-FZ of 31 December 2014

# Localization – Main Legal Steps

## Step 1 – Creation of a Legal Entity

- Mostly - a limited liability company under Russian law (OOO)
- Minimum registered capital 10.000 RUB
- May have one or several founders
- Liability only to the extent of the investment amount (with some exceptions)
- Registration within 1 week after filing an application
- Representation powers – General Director(s) (CEO)
- Tax registration and tax obligations in Russia
- Bank accounts in Russia, Russian accounting reporting
- Subsidiary vs. joint venture

### Main steps for incorporating a legal entity:



## Acquisition of a Land Plot

- Due Diligence:
  - ✓ Functional designation? (category of land, permitted use)
  - ✓ city planning restrictions, easements, other encumbrances on the land plot
  - ✓ Technical Due Diligence is also recommendable
- Possible legal options for acquisition - private ownership and lease (including long-term lease) to land plot and production facilities (if brownfield)
- State registration of rights

## Preparation for construction

- Connection to power supply network
- Obtaining a construction permit and filing the required documents:
  - ✓ title documents to the land plot;
  - ✓ city development plan of the land plot;
  - ✓ design documents (in the scope provided for by legislation), and
  - ✓ positive opinion of the state expert examination.

## Contract preparation

- Delivery basis? Payment conditions? Securities?
- New or used equipment (customs value appraisal might be required)
- Mixed contracts (e.g. supply + installation):
  - ✓ Separation of contract subjects and prices – important for customs and tax reasons
  - ✓ Check of permanent establishment risks when foreign personnel renders services in Russia



## Customs payments optimization

- Importing goods as a property contribution to the share capital of a subsidiary company
- Exemption from VAT for technological equipment that has no analogues manufactured in the Russian Federation
- Obtaining a (preliminary) classification decision

# Production Permits and Certification

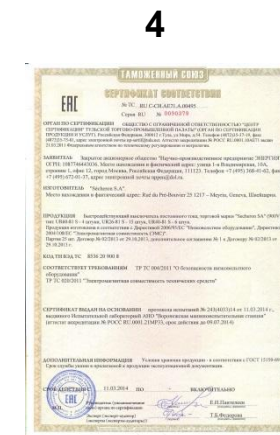
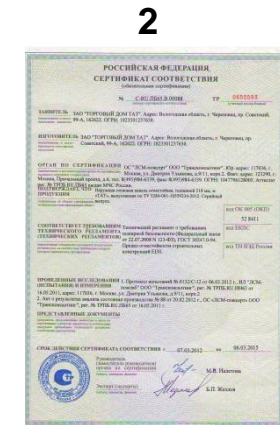
1. Compliance with industrial safety requirements the :

- Certificate of compliance with requirements of technical regulations
- Industrial safety certificate (voluntary)
- Registration of production facility in the register maintained by Rostekhnadzor (Federal Service for Environmental, Technical and Nuclear Supervision) – if an enterprise is considered as hazardous facilities.

2. Fire safety certificate – for certain types of products (in particular, construction materials and electrical products)

3. CT-1 certificate confirming the country of origin

4. Obligatory conformity confirmation in cases stipulated by the respective technical regulation (e.g. *Technical Regulation of the Customs Union "On the safety of wheeled vehicles" TP TC 018/2011*)



Speaker

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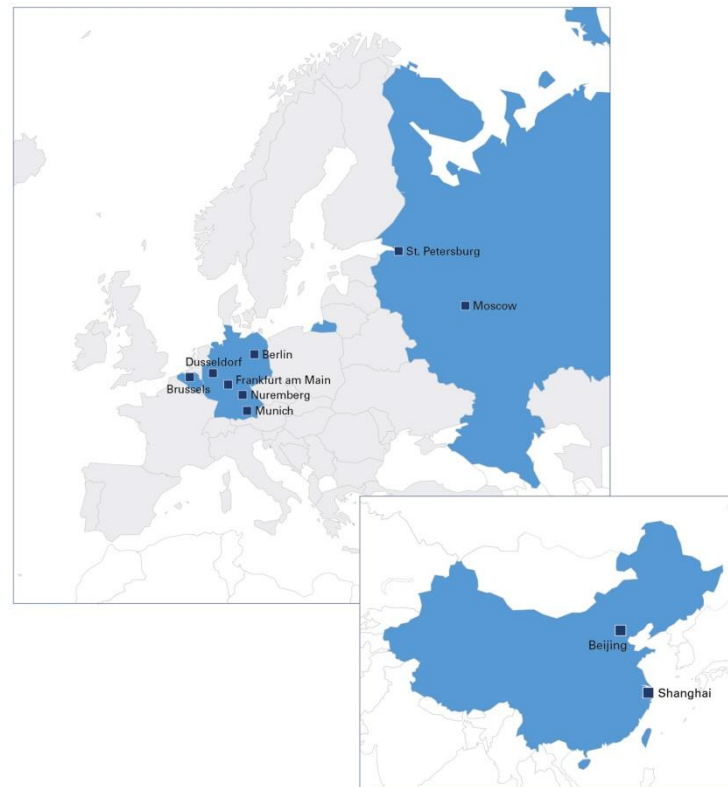


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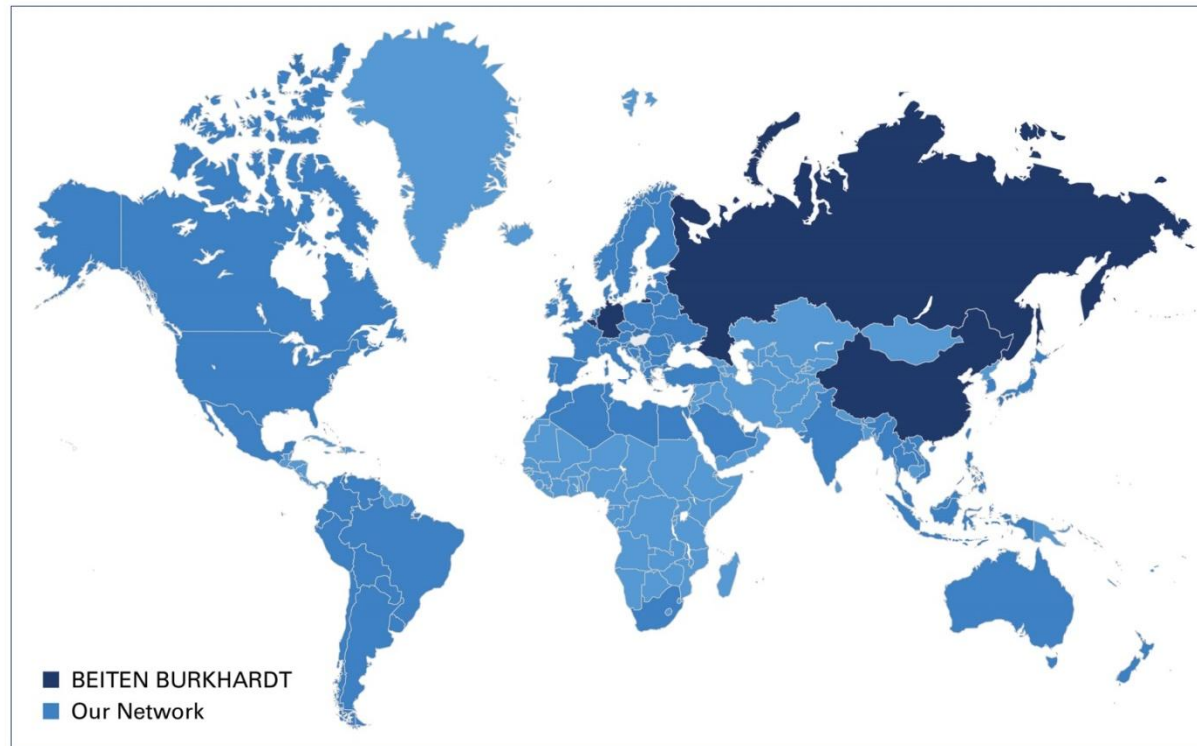
# BEITEN BURKHARDT at a Glance

## BEITEN BURKHARDT is an international corporate law firm.

Founded	1990 in Munich
Lawyers worldwide	273
in Germany	235
Lawyers international	38
Offices	Beijing, Berlin, Brussels, Dusseldorf, Frankfurt am Main, Moscow, Munich, Nuremberg, Shanghai, St. Petersburg



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- Corporate law, M&A** → establishing representative offices and branches of foreign companies, subsidiaries and joint ventures, legal due diligence on target Russian companies in Russia, corporate housekeeping
  - Commercial and contract law** → drafting and negotiating contracts, structuring transactions from the legal and tax perspective
  - Real estate and construction** → due diligence on real estate, legal support for greenfield and brownfield projects, drafting contractual documentation, advice on construction issues
  - Taxation** → advising on issues related to tax planning and structuring of investment projects, tax analysis of contractual documentation, representing clients in tax disputes
  - Employment and migration** → advice on employment issues, obtaining permit documents and visas to perform labor activities
  - Customs law** → optimizing the customs registration process, support on the issues of reducing customs duties and import VAT relief, support in disputed with customs bodies
  - Intellectual property** → protection of trademarks and patents in Russia, advice on concluding license and franchise agreements, know-how protection
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