

# ***New trend in import substitution - establishment of the Russian origin criteria***

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## ***In brief***

On June 30, 2015 the Federal Law #488-FZ “On industrial policy” of 31.12.2014 came into force (hereinafter – **the Federal Law**). This document envisages different trends towards supporting Russian industry, in particular, through provision of the preference for the Russian-made goods in the area of state procurement. However, as of today, Russian legislation does not lay down either legal definition of the “Russian-made goods” nor criteria for determining Russian origin for the above-mentioned purposes.

The Russian Ministry on Industry and Trade (hereinafter – **Minpromtorg**) was instructed to develop the criteria of the Russian origin (hereinafter – **the Criteria**). The Draft Russian Government Decree establishing such Criteria (hereinafter – **the Draft Decree**) was recently published. This draft was developed by Minpromtorg in cooperation with working committees within different business associations. The document is expected to be finalized upon negotiations with the federal authorities, however, it is already obvious what approaches to determination of the Russian origin and what Criteria will be put in place. To the best of knowledge, the Draft Decree is likely to come into force on September 1, 2015.

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## ***In detail***

### ***For what purposes the Criteria will be used?***

In accordance with the Federal Law the Criteria are developed primarily for the following purposes:

- ❖ *Provision of the preference* to the Russian-made goods in state procurement tenders and tenders arranged by the state-owned companies;
- ❖ *Introduction of bans/restrictions* for goods of foreign origin being purchased via state procurements tenders;

The current practice suggests that companies, which produce certain types of goods, should

follow the CIS Rules of Origin<sup>1</sup> in order to participate in state-procurement tenders.

The idea to develop specific criteria of the “Russian origin” for each industry sector is explained by the fact that the CIS Rules of Origin do not allow to fully and adequately take account of specifics of technical and technological processes in different industries.

### ***To what products the Criteria will be applied?***

According to the publically available version of the Draft Decree, the Criteria are to be established for the following industry sectors:

- 1) Machine tool industry;
  - 2) Automotive industry;
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<sup>1</sup> The CIS rules of Origin adopted by the Agreement on the Rules for Determination of the Country of Origin of Goods in the Commonwealth of Independent States of 20 November 2009

- 3) Special machine industry;
- 4) Photonics and lighting industry;
- 5) Electrical engineering and electric power industry;
- 6) Heavy machines industry.

We do not exclude that the above list may be further expanded.

It should be also noted that measures of state support could be applied not only to the products from the above list but also to other products, independently on if the Criteria is established for them or not.

### ***What the Criteria say?***

The Criteria set out various requirements for:

- ❖ *product* (e.g. the “ad valorem share” rule, where the value of foreign raw materials/ components used for production should not exceed the established threshold, etc.); or
- ❖ *manufacturer* (e.g. execution on the Russian territory of certain production and technological operations).

For example, to allow combine harvester to be treated as originating in Russia, starting from 2016 it is required to execute at least 7 production operations on the territory of Russia, including assembly and welding of the base frame.

If the product is not covered by the Draft Decree, but measures of the state support apply to it, its origin should be determined in accordance with the CIS Rules of Origin.

For those manufacturers, which have the special investment contracts with the Russian government, special criteria could be introduced. In this case, goods will be treated as “made in Russia” based on the individual criteria set forth in such contract.

The Draft Decree envisage that documents confirming Russian origin may vary depending on the applicable Criteria.

### ***What does it mean for your company?***

We understand that primarily the Criteria are to be used for establishment of the restriction for goods of foreign origin subject to state procurements. The state-owned companies may also establish own internal procedures and

specific requirements towards arrangement of the procurement tenders including the preference of Russian-made goods.

Moreover, currently, certain companies (not state-owned companies), tend to establish their internal procedures and specific requirements towards arrangement of the commercial procurement tenders including the priority of Russian-made goods. Therefore, we cannot exclude that they may apply the Criteria for procurement tenders in future.

It means that access to the state procurement tenders will be closed for those importers of foreign goods and manufacturers who failed to meet the Criteria. Such companies may even lose their access to commercial tenders, when preference is given to the producers who were able to organize production in Russia in compliance with the established rules.

### ***Recommended steps***

For the companies, which only consider setting up production in Russia, it is worth arranging preliminary analysis of the Criteria to be established under the Draft Decree. Such analysis will enable to better understand what technological operations should be performed in Russia, what level of localization is required, whether there are any possibilities to use foreign materials and components for production purposes, how to adjust existing production plans in order to keep presence on the state procurement market.

Adjustment of the production process (e.g. increase of local content, introduction of new technological operations, etc.) may result in tax and customs implications as compared to the current business model.

It is worth mentioning, that the Criteria are new ones both for the manufacturers and for the bodies in charge for issuance of the documents confirming observation of the Criteria.

Therefore, difficulties with interpretation of the Criteria may occur not only when determining applicability of the Criteria but also when confirming observation of the Criteria.

PwC experts will be pleased to advise on the Criteria, steps needed to be take in order to meet the Criteria, to comment on the already prepared production plans in view of the Criteria, assist with obtainment of the required documents for confirmation of the Criteria’ observation.

## Let's talk

We would be happy to answer your questions.

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