



UKRAINE-RELATED CHALLENGES FOR BUSINESS: what to know and how to respond?

7 JULY 2014

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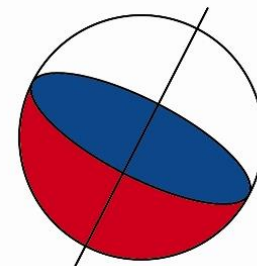
Helge Masannek

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***US and EU sanctions:
summary of key norms and
implications for Russia***

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US and EU sanctions Summary of key norms and implications for Russia

Helge Masannek
Director Taxes & Legal, Attorney (Germany)
AEB Business Meeting
Moscow, 7th July 2014

- Overview of sanctions
 - ✓ EU
 - ✓ US
 - ✓ Russia's reactions
- Who shall follow the sanctions?
- Who is sanctioned?
- What is forbidden?

1st stage

- 6th March: Talks on cooperation agreement and visa-free regime suspended

2nd stage

- “Regulations concerning restrictive measures in respect of actions undermining or threatening the territorial integrity, sovereignty and independence of Ukraine”
- Economic sanctions, asset freeze, travel ban
 - 5th March (2014/119/CFSP)
 - 17th March (2014/145/CFSP)
 - 12th May (2014/265/CFSP)
- Currently sanctions against 61 individuals and 2 legal entities
- Council Regulation 692/2014 as of 23rd June 2014: Import ban for goods originating in Crimea or Sevastopol (exception: goods with Ukrainian certificate of origin)

3rd stage

- Industry sectors restrictions – not introduced (yet?)

- Currently sanctioned: 52 individuals and 19 legal entities
(Economic sanctions, asset freeze and travel ban)
 - ✓ Executive Order 13660 (6th March)
 - ✓ Executive Order 13661 (17th March, additional persons)
 - ✓ Executive Order 13662 (20th March, additional persons)

- 3rd April 2014: “The Support for the Sovereignty, Integrity, Democracy, and Economic Stability of Ukraine Act of 2014”
 - ✓ Legislative basis for further sanctions (asset blocking, exclusion from the US and revocation of visa) and financial support for Ukraine

- 28th April: Export and re-export prohibition to Russia of certain goods
 - ✓ Covered: high tech goods subject to the Export Administrative regulations (especially dual use goods)
 - ✓ U.S. Commerce Department’s Bureau of Industry and Security revoked existing export licenses

More countries follow

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- Implementing the EU sanctions:
 - ✓ Norway
 - ✓ Montenegro
- Switzerland
- Canada
- Australia
- Japan
 - ✓ no sanctions, but freezing of bilateral talks on economic, security, visa and border topics

- Handelsblatt, 12th May: „Pressure on Brussel“, „Many phone calls have been necessary“
 - ✓ Alexei Miller, Gazprom: gaz supply

- **Travel bans**
 - ✓ Russia bans entry to 9 US politicians

- **Law on “National Payment System”**
 - ✓ Adopted on 5th May 2014 in response to Visa and Mastercard freezing services to Russian banks under US sanctions
 - ✓ Prohibition of international payment systems to cut off services to Russian clients and obliges them to base their processing centers in Russia
 - ✓ International payment systems shall make security deposits in Russia's central bank equal to the average value of two days' worth of transactions
 - Visa and MasterCard: total \$3.8 billion
 - ✓ Law came into force on 1st July 2014
 - ✓ If a payment system unilaterally freezes operations:
 - Penalty of 10 million rubles (\$280,000) for every day of suspended service if “nationally significant”
 - Smaller operators: 10% of their security deposits for each day
 - ✓ Amendments to the law expected

■ EU sanctions

- ✓ **Legal entities or citizens acting in the EU, place of company registration or citizenship does not matter**
 - E.g. European branch of a Japanese company delivers goods to a Russian buyer
- ✓ **EU-citizens and companies registered in the EU, no matter where they act**
 - E.g. French general director of an OOO signs a contract with a Russian customer
 - E.g. Russian branch of an Austrian company renders services to a Russian customer
- ✓ **Not obliged to follow the sanctions**
 - Subsidiaries of EU companies in Russia (OOOs)
 - But if general director EU-citizen, he/she shall follow the sanctions, PR/non-legal consequences should be taken into account

■ US sanctions

- ✓ **Legal entities or citizens acting in the US, place of company registration or citizenship does not matter**
 - E.g. US branch of a Japanese company delivers goods to a Russian buyer
- ✓ **US citizens and companies registered in the US, no matter where they act**
 - E.g. US general director of an OOO signs a contract with a Russian customer
 - E.g. Russian branch of a US company renders services to a Russian customer
- ✓ **Not obliged to follow the sanctions**
 - Subsidiaries of US companies in Russia (OOOs)
 - But if general director is a US citizen, he/she shall follow the sanctions, PR/non-legal consequences should be taken into account

Who is sanctioned?

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- Individuals and legal entities on the lists
- Any company that belongs to 50% or more to a listed person/company
 - ✓ Task: Check your counterpart!
 - ✓ Problem: offshore-companies
- Any person that is controlled by a listed person (“dominant influence”/”owns directly or indirectly a 50% or greater interest”)
 - ✓ Problem: Nominee shareholders

What is forbidden (EU)?

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- It is forbidden to:
 - ✓ ...buy or sell goods to or from the listed persons
 - ✓ ...transfer money or receive money
 - ✓ ...make available all other economic resources or funds, including:
 - cash, cheques, monetary claims
 - deposits with financial institutions
 - publicly- and privately traded securities and debt instruments, including stocks and shares
 - interest, dividends or other income
 - credit, guarantees
 - letters of credit
 - documents showing evidence of an interest in funds
 - etc.

What is forbidden (USA)?

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“All property and interests in property that are in the United States, that hereafter come within the United States, or that are or hereafter come within the possession or control of any United States person (including any foreign branch) of the following persons are blocked and may not be transferred, paid, exported, withdrawn, or otherwise dealt in...”

- A EU company may receive payment for a contract which has been signed before the sanctions, if the goods has already been delivered
- Special needs: acute medical treatment etc.
- Legal protections against sanctions
- Official delegations (UN, UNESCO, EU etc.)

- US Department of the Treasury's Office of Foreign Assets Control (OFAC) can grant licenses on engaging in certain activities that otherwise would be prohibited
 - ✓ E.g. wind down a transaction involving listed persons started prior to sanctions, processing payments for certain transactions (food, medicine, humanitarian goods etc.)

Consequences for breach of sanctions

■ EU

- ✓ Depending upon legislation of respective member state, e.g.
 - Germany:
 - Administrative penalty up to 0,5 million €
 - Imprisonment up to 10 years
 - France:
 - Administrative penalty up to 10 times the transaction value
 - Imprisonment up to 5 years

■ US

- ✓ Administrative penalty up to \$ 1 million per transaction
- ✓ Imprisonment up to 20 years

Thank you for your Attention!

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- Import, Customs Clearance, Certification
- IT Services / ERP
- Interim Management
- Office Sublease
- Recruiting
- Visa and Work Permit
- Business Workshops

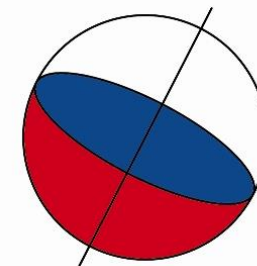
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***Prospects for the retention
and further development of
USA and EU's sanctions
against Russia. Risks of new
sanctions being introduced***



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*Crimea's admission to
Russia: legal implications,
risks and solutions for
business*

Economic and Business Risks Update

Business Activity in Crimea Today

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Moscow Office

July 7, 2014

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Ukrainian Law Perspective

Crimea and Sevastopol: Legal Regime

- Declaration of “Verkhovnaya Rada” dated March 20, 2014
- Law “On Ensuring Rights and Freedoms of Citizens and Legal Regime in Temporarily Occupied Territory of Ukraine” dated April 15, 2014
 - Territory of Ukraine – Ukrainian legislation applies
 - Special regime of entry/exit for individuals and goods (contemplated)
 - No restriction on business activities – subject to the special legal regime to be defined in a separate Law (not yet adopted)
 - Non-compliance with Ukrainian law requirements by Ukrainian or foreign legal entities and individuals may result in administrative, criminal and civil liability
 - Acts/decisions of Crimean authorities established in violation of Ukrainian law are invalid *ab initio* and do not have legal consequences

Banking and Currency Control

- **Russia:** Federal Constitutional Law No. 6-FKZ – a special transition period – the banks may continue operating based on Ukrainian license, subject to filing with the Russian Central Bank of a set of required documents
- Banks that do not follow the above requirements are closed down
 - The Russian Central Bank already prohibited operation in Crimea/Sevastopol of more than 18 Ukrainian banks, these banks are allowed to transfer their assets to third parties but cannot perform banking operations
- Hryvna is no longer allowed as a payment instrument starting from June 1, 2014
- **Ukraine:** Resolution of National Bank of Ukraine (“**NBU**”) No. 260 of May 6, 2014 (came into force on the same day):
 - 2 Crimean banks are declared closed and their licenses are canceled (i.e., “Chernomorskiy Bank of Development and Reconstruction” and Bank “Morskoy”)
 - All Ukrainian banks are completely prohibited from providing any financial services and operating in Crimea (Crimean branches, if any, must be closed)
 - Confirmed that general Ukrainian currency control rules apply
 - UAH (Hryvna) is the only valid currency in Crimea/Sevastopol, all settlements between Crimea and mainland of Ukraine shall be made in Hryvna

Property Rights (Ukraine)

Law of Ukraine “On Ensuring Rights and Freedoms of Citizens and Legal Regime in Temporarily Occupied Territory of Ukraine”

- ✓ Acquisition and termination of ownership rights to real estate *must comply* with mandatory requirements of Ukrainian legislation
- ✓ Any transaction, which contradicts Ukrainian legislation, *will be void* and will entail no legal consequences



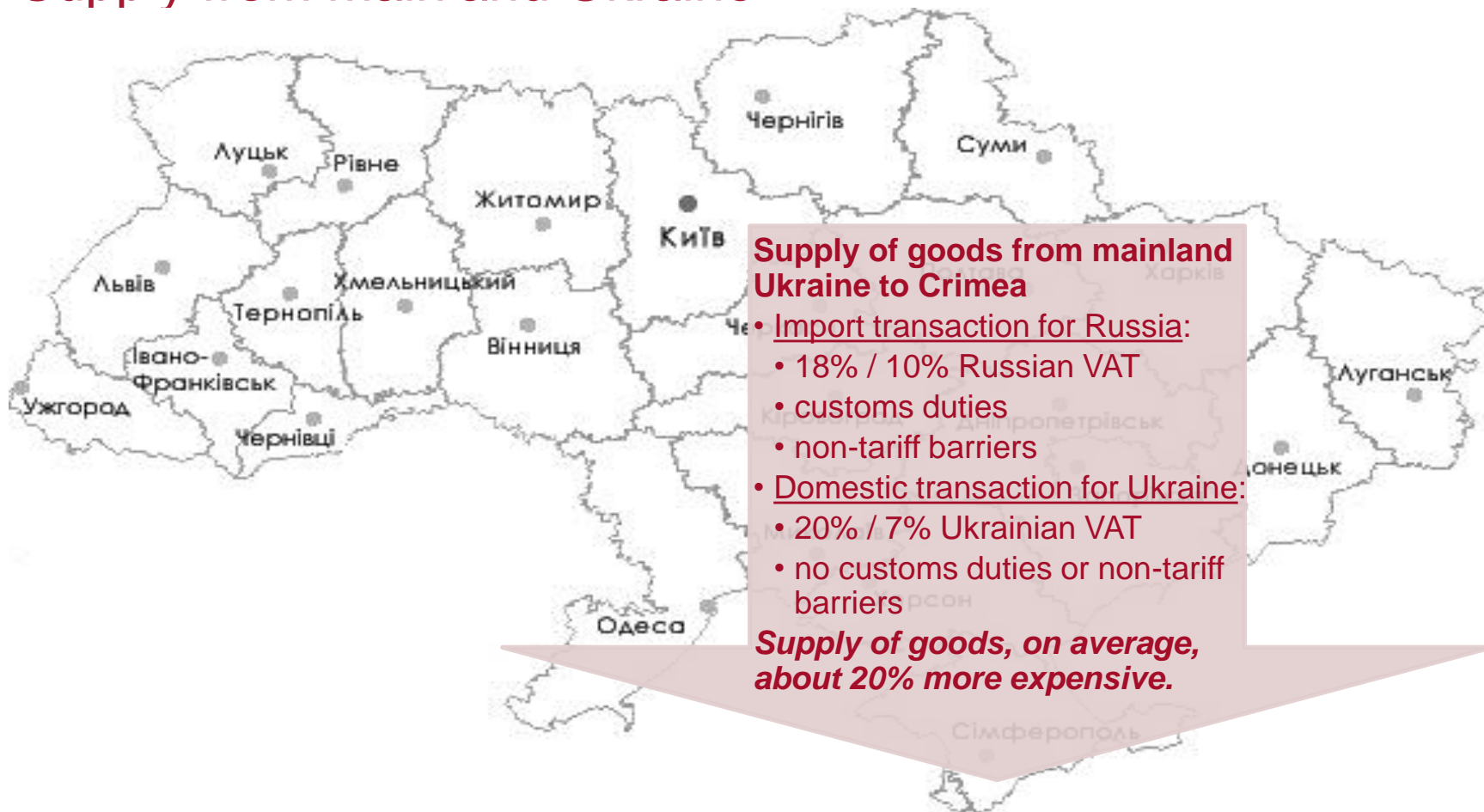
Property Rights (Ukraine - continued)

- Property rights to real estate are *subject to registration* with the Ukrainian State Register of Property Rights to Real Estate
- Who registers transfer of title to the property located in Crimea?
 - State registrar where one of the parties is located (if outside of Crimea)
 - State registrars in **Dnipropetrovs'k, Odessa, Khmelnytsky and Chernigiv regions** if the application is made to the Crimean state registrars, and/or
 - State registrars in **Kherson and Zaporizhzhya** region – upon application



Order of the Ministry of Justice “*On Measures Ensuring Rendering of Services in State Registration of Property Rights to Real Estate*” dated March 14, 2014

Tax/Customs: Supply from mainland Ukraine



Tax/Customs: Supply to mainland Ukraine



Supply of goods from Crimea to mainland Ukraine

• Export transaction for Russia:

- 0% Russian VAT
- customs duties
- non-tariff barriers

• Domestic transaction for Ukraine:

- Crimean supplier unlikely to charge 20% Ukrainian VAT
- VAT invoice unlikely to be registered
- no customs duties or non-tariff barriers

Supply of goods likely without VAT and, thus, cheaper.

Tax & Customs Landscape

UKRAINE

General rules remain applicable:

- reporting and filing
- payment of taxes and collections
- customs control of goods imported from Russia into Crimea

Occupation period rules:

- tax breaks designed for Crimean taxpayers registered in Crimea and city of Sevastopol for the duration of occupation (being drafted by the Ministry of Revenue and Duties of Ukraine)
- Crimean legal entities and individual entrepreneurs may re-register in mainland Ukraine and pay taxes at its new address (in force)
- customs control of individuals at the border with Crimea (as per Draft Law No. 4473-1 *On Provision of Rights and Freedoms of Citizens of Ukraine on the Occupied Territories* of 19 March 2014)

Sanctions for non-compliance with general rules

Tax Code:

- article 117 – violation of rules on registration
- article 120 – failure to file tax reporting documents
- article 126 – violation of rules on payment of taxes

Administrative Offenses Code:

- article 163-1 – violation of tax accounting rules
- article 163-2 – failure to file orders for payment of taxes and collections
- article 163-4 – violation of rules on payment and reporting in relation to personal income tax
- article 164 – business activity without registration

Criminal Code:

- article 201 – smuggling
- article 205 – sham business
- article 209 – money laundering
- article 212 – tax evasion
- article 212-1 – social security contributions evasion
- article 358 – forgery

Tax & Customs Landscape

RUSSIA

Transition period rules:

- taxes, customs and other duties, any other collections to be paid in RUB
- until 1 January 2015, tax and other revenues to be paid to budget of Crimea, city of Sevastopol and other local budgets
- since 1 March 2014, input VAT from Ukrainian taxpayers could not be offset against output VAT but is treated as deductible expense for CIT purposes
- VAT debts for tax periods before 1 March 2014 were written off
- VAT invoices issued since 18 March 2014 not to be registered
- starting from 26 March 2014, 18% / 10% VAT applies to goods supplied to Crimea from mainland Ukraine
- right to recover input VAT incurred on goods supplied from mainland Ukraine

Issues:

- applicability of Ukraine-Russia double tax treaty / domestic rules on taxation of non-residents' income:
 - risk of double taxation, permanent establishment risk
 - loss of foreign tax credit and other treaty benefits
- applicability of the CIS Free Trade Agreement / WTO instruments
- replacement of tax identification codes issued in Ukraine
- registration of branches of Russian / Ukrainian legal entities in Crimea and city of Sevastopol

Jurisdiction of Ukrainian Courts

Law of Ukraine “*On Ensuring Rights and Freedoms of Citizens and Legal Regime on Temporarily Occupied Territory of Ukraine*” of 15 April 2014:

disputes pending at Ukrainian courts in Crimea and all future claims (to be considered by such courts) shall be considered by the following courts:

Administrative and Commercial Cases

Administrative/Commercial
Courts of the Autonomous
Republic of Crimea



Administrative/Commercial
Courts of the Kyiv Region

Administrative/Commercial
Courts of the Sevastopol City



Administrative/Commercial
Courts of Kyiv City

Civil and Criminal Cases

Local courts of the Autonomous
Republic of Crimea/Sevastopol City

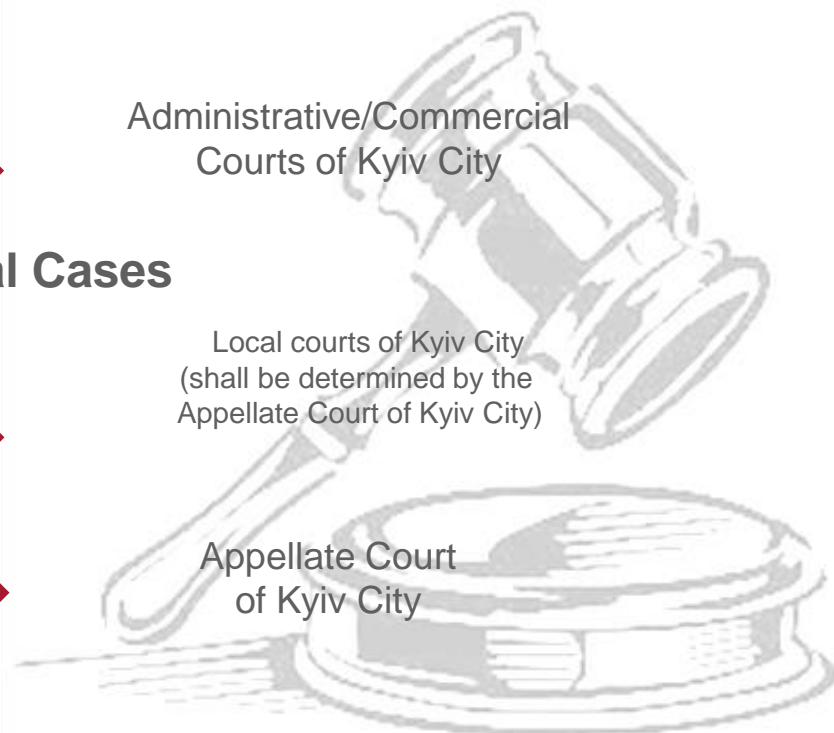


Local courts of Kyiv City
(shall be determined by the
Appellate Court of Kyiv City)

Appellate courts of the Autonomous
Republic of Crimea/Sevastopol City



Appellate Court
of Kyiv City





Russian Law Perspective

Russian legislation on Crimea

- Russo – Crimean Treaty on Accession of Crimea to the Russian Federation, March 18, 2014
- Federal Constitutional Law No. 6-FKZ On Acceptance of Crimea to the Russian Federation and Formation of Two New Subjects of the Federation – Republic of Crimea and City of Sevastopol, March 21, 2014
- Federal Law No. 37-FZ On Functioning of the Financial System of the Republic of Crimea and the City of Sevastopol During the Transition Period, April 2, 2014
- Federal Law No. 39-FZ On Protection of Interests of Individuals Having Deposits with Banks Registered and/or Operating in the Republic of Crimea and the City of Sevastopol, April 2, 2014
- Normative acts of the Russian President, Russian Government, Central Bank of Russia, Federal Tax Service, Federal Customs Service, competent authorities of the Republic of Crimea and the City of Sevastopol

Crimea - Russian legal regime (1)

- **Citizenship** – Automatic Russian citizenship for all residents, unless formally refuse by April 18, 2014. Russian passports already issued
- **Transition period** – until January 1, 2015
- **Local governance** – new governing bodies to be created in Crimea and Sevastopol by way of elections scheduled for September 13, 2015. Until then, present bodies govern, and can adopt local legislation, subject only to compliance with the Russian Constitution
- **Local entities** – may continue operating in their current legal form until January 1, 2015, but they must re-register as Russian legal entities or branches / rep. offices of foreign companies, otherwise, they would be unable to perform any business activities after that date
 - Local subdivisions of the Russian Federal Tax Service are already actively registering legal entities, entrepreneurs willing to legalize under Russian rules. Until January 1, 2015 such registration is exempt from state duty
- **State permits and activity licenses** – documents issued by the time of the Crimea accession to Russia remain valid without limitation, unless otherwise flows from the said documents or the corresponding legal relations
 - Exception: banks, financial organizations, customs brokers

Crimea – Russian legal regime (2)

- **Non-banking financial institutions (security market operators)** that perform depository activities in Crimea - may continue operating without a license until January 1, 2015
- **Currency** – the only legal tender is Russian Ruble starting from June 1, 2014 (Ukrainian Hryvna is no longer allowed for payments)
- **Cash-control equipment** – special transition rules apply until January 1, 2016 as approved by the local government of Crimea on June 4, 2014
- **Administrative, family and other state documents** – all such documents duly issued by competent Ukrainian authorities by the time of the Crimea accession to Russia remain valid without limitation, unless otherwise flows from the said documents or the corresponding legal relations. However, as of the time of the accession and until the end of the Transition Period any such documents should be obtained in line with the Crimea/Sevastopol local legislation. Potentially, this period may last until September 2015. Thereafter, general norms of Russian law would apply

Crimea – Russian legal regime (3)

- **Immovable property** – the Russian Rosregister already established a republican subdivision in the city of Simferopol (Crimea) which will re-register all the residential and commercial real estate under Russian rules within the transition period of 2-3 years. The re-registration is planned to be on a voluntary basis, however, after the expiration of the transition period in absence of a Russian property document no deal with any real estate without Russian documents will be possible
 - Russian State Duma already issued draft law (No. 497399-6) on the 1-year transition period and simplified rules for re-registration of immovable property in Crimea, however, the draft is still under consideration (as of July 7, 2014 the draft law has not passed the 1st reading in the State Duma)
 - Note! Russian law doesn't allow foreign citizens and entities owning land in sea ports, agricultural land and land in "border territories" (list defined by the President's Decrees)

Crimea – Russian legal regime (4)

- **Tax** – Russian tax laws govern, but during Transition Period taxes are payable to the Crimea/Sevastopol budget, and their establishment, incentives and enforcement are governed by local normative acts
- Russian **tax laws already apply** in Crimea (except for land tax and state duty) with respect to local Russian legal entities and their branches/rep. offices that were registered with the Unified State Registrar of Legal Entities (EGRUL), as well as separate subdivisions of foreign companies established in Crimea after March 18, 2014
- **Customs** – Russian/Customs Union rules to apply over the Transition Period. However, during that time no passport of transaction is required. Customs Houses of Simferopol and Sevastopol and 3 customs posts on the border with mainland Ukraine were established, customs control on the ferry line between Kertch (Crimea) and Port Caucasus (Russia) is suspended. Cargo transportation between Crimea and mainland Ukraine is presently allowed based on shipment documents, without customs clearance
- **Labor** – Russian citizens may freely work in Crimea and Sevastopol. Other citizens, including Ukrainian, have to obtain Russian work permit/visa. But the issuance of work permits/visas will start only in 2015. Ukrainian nationals currently work under migration cards, which is formally illegal but informally allowed during the transition period (yet no fines or other administrative sanctions imposed)

Crimea – Russian legal regime (5)

- **Judicial system** – local courts to be formed in Crimea/Sevastopol under Russian law by the end of Transition Period. Until then, existing courts continue performing their activity
 - Russian Federal Law No. 154-FZ dated June 23, 2014 established the judicial system of Crimea, the Russian Supreme Court is to set the date when the courts should start functioning and establish a law enforcement mechanism for court decisions taken in Crimea
- Civil law and administrative cases fully considered (including cassation) by the time of the Crimea accession to Russia are not subject to review
- Civil law and administrative cases not fully considered (appeal and/or cassation still being pending) can be so considered under Russian material and procedural law
- Criminal investigations and cases in progress are finalized under Russian material and procedural law, subject to review and confirmation of the charges by the competent prosecutor in Crimea/Sevastopol
- Criminal investigations, cases and sentence for the crimes non-existent under Russian law shall be suspended

Doing Business in Crimea – Practical issues from the Russian side

- No coordination with Ukrainian rules
- High risk of challenge by Ukraine for violation of its established procedure
- High risk for products originating from Crimea to be banned for exportation to other jurisdictions, the EU already banned Crimean products (such products can be imported to the EU only on the basis of a Ukrainian certificate of origin or under an agreement executed before implementation of this trade ban)
- Financial system – Ukrainian banks quit, Russian banks come in slowly
- Tax – transition to Russian tax rates and payment procedure yet to be developed, chances to credit/refund the taxes overpaid before accession unclear. For Crimean business – clear risk of double taxation (unless Ukrainian legislation on special tax regime for Crimea is adopted)
- Customs – so far, no clearance in trade with mainland Ukraine, but attempt to enforce general Russian customs rules might complicate that trade
- Citizenship – unclear status of those who miss the tight deadlines for refusal from Russian passport, unclear labor and migration rules for Ukrainian residents in Crimea
- Contracts – does failure to duly perform constitute *force majeure*? Problems with execution and enforcement for persons inside and outside Crimea
- Real estate – will limitations for foreign ownership of land apply in Crimea?

Economic and Business Risks Update

Business Activity in Crimea Today

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***Foreign investments in
Crimea and the possible
application of investment
protection treaties with
respect to such investments***



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***AEB member-companies
current experiences in
Crimea***



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Q&A