PROBLEMS OF LEGAL SUPPORT OF ENERGY COMPANIES IN THE COURSE OF PROCURING FOREIGN-ORIGIN GOODS, WORKS AND SERVICES PERFORMED OR PROVIDED BY FOREIGN ENTITIES

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In accordance with Decree No. 925 of the Russian Federation dd. September 16,2016 On Priority of Russian-Origin Goods, Works and Services Performed by Russian Entities over Goods of Foreign Origin, Works and Services Performed or Provided by Foreign Entities, Russian-origin goods, works and services performed by Russian entities are privileged over goods of foreign origin, works and services performed or provided by foreign entities in the course of procuring goods, works and services by way of bidding, auction, and other forms of procurement, except for single-source procurement.

In fact, customer companies are obliged to give Russian manufacturers of radio-electronic products an advantage of 30 percent of the offered price, and of 15 percent in all other cases.

The study analyses problems of legal support for energy companies in procuring goods of foreign origin, works and services performed or provided by foreign entities and gives the legal analysis of the judicial practice, explanations by public authorities, local by-laws of energy companies, and provisions of international treaties.

Keywords: *energy law, energy legislation, contractual regulation in the sphere of energy; procurement procedures.*

For the purposes of supporting Russian manufacturers, Decree of the Russian Federation No. 925 dd. September 16, 2016 On Priority of Russian-Origin Goods, Works and Services Performed by Russian Entities over Goods of Foreign Origin, Works and Services Performed or Provided by Foreign Entities (hereinafter referred to as "Decree No. 925").

The said Decree No. 925 stipulates privileging the goods of Russian origin or supplied by Russian entities over the goods supplied by foreign entities.

According to current legislation, the preferential treatment is manifested in that in the course of a procurement process where the winner is determined based on assessment criteria, bids comparison, and the lowest contract price, the commission (procurement organizer) is obliged to compare the bids' prices with the values given by a Russian bidder deemed to be reduced by 15 percent.

While the contract should be entered into at the contract price specified by the bidder.

This can be irrelevant in case of minor procurements for an energy company. But when it comes to crucial production facilities, replacement of foreign equipment (in most cases, material and technical resources (MTR) required for repairs of out-of-service equipment) with Russian one can lead to major accidents. Energy companies' attempts to specify more detailed characteristics of MTR or their manufacturer result in disagreements with supervising authorities who deem such requirements as competition limiting behavior.

Thus, a company faces the risk to get products of possibly the same quality but with a shorter service life due to poor compatibility with an existing plant.

Speaking of service procurement, such limitations lead to unnecessary resellers adding their commission to the existing financial burden.

Let us consider a particular situation: engaging a legal advisor in the territory of a foreign state. For example, we are opening a branch or representative office in the territory of a foreign state, or we are already operating a branch and a claim has been filed against it in accordance with the national legislation rules. We have to engage an expert in local legislation and announce bidding / invite quotations for advisory/consulting services. The customer will stipulate in the procurement documentation that the services will be provided in the territory of a foreign state. However, if both foreign and Russian legal entities are among the bidders, the energy company will have to privilege certain ones. Thus, a foreign bidder, even with the lowest price quotation, will most probably lose to a Russian rival.

In such situation, the company is not only forced to choose not the best financial proposal but, in the future, will also have to partially cover the expenses resulting directly from the fact that the service provider is not the resident of the country where the case is heard/service provided. Such expenses include business trip expenses invoiced to the customer and/or engagement of additional advisors (since provision of such services often requires the knowledge of national legislation in addition to international law).

Besides, Decree No. 925 does not apply to single-source procurement (at a single supplier/contractor) which seems rather reasonable. Single-source procurement agreements are usually required due to the uniqueness of the subject of procurement or the impossibility to conduct bidding. Thus, granting preferential treatment becomes irrelevant and impossible.

For example, Rosneft's Procurement Regulations allow single-source procurement for goods with the exclusive rights therein belonging to the rights holder according to legislation [1]. Due to that, holding a bidding process is impossible, since at the time when the corresponding need arises the company needs a particular product with specific features, and the rights in that product are protected by the copyright rules.

In addition to that, Rosneft's Procurement Regulations stipulate single-source procurement for technologically sophisticated equipment. For example, equipment/machinery used in offshore project implementation, as well as works/services that can be performed/provided exclusively by the manufacturer of such equipment by virtue of its copyright or developments using unique and/or innovative technology.

It is expedient to procure component parts for such equipment at the supplying manufacturer irrespective of its country of origin. Such rules in the Rosneft's Procurement Regulations are aimed at minimizing the risks of the equipment-related accidents and equipment failures caused by the incompatibility of the supplied MTR with the existing equipment.

One should note that the present rules of international law limit heavily the application of Decree No. 925 in general.

In accordance with Clause 8 of Decree No. 925, granting preferential treatment to Russian products is subject to the General Agreement on Tariffs and Trade (GATT) of 1994 and Treaty on the Eurasian Economic Union dd. May 29, 2014.

Members of the Customs Union are the following states: Russia, Kyrgyzstan, Kazakhstan, Armenia, and Belarus. Accordingly, Decree No. 925 will not apply to procurement bidders residing in the counties listed.

Presently, the World Trade Organization numbers about 158 member states whose

interests should be respected in accordance with the General Agreement on Tariffs and Trade (GATT) of 1994.

Member countries are not allowed to impose any limitations on imported goods, whether limitations of duty amounts or any artificial limitations, including qualitative ones.

The Protocol on the Procedure for Regulating Procurement (Annex No. 25 to the Treaty on the Eurasian Economic Union) establishes that the signatory countries must, for the procurement purposes, offer national treatment not less favorable than that applied to goods, works and services of domestic origin, as well as to potential suppliers and suppliers of their state, offering such goods, or performing works and providing services [2].

However, the World Trade Organization recognizes the states' rights to establish preferences in a range of specific spheres, such as defense and security, including armed forces supplies, protection of human life and health, gold and silver circulation, and protection of works of art and items of historic and archeological value.

Proceeding from that clause, one can conclude that in case of metal products procurement by defense industry undertakings, a Customer Company may apply preferential treatment stipulated in Decree No. 925, while, in the course of the same procurement, an energy company may not privilege Russian companies since it is not engaged in producing goods required for armed forces' supplies.

Judicial position supports the same position. Let us consider Judgement of the Moscow Circuit Commercial Court in Case No. A40-37602/2018 dd. February 27, 2019 as an example. [3]

The court considered the case on claim by Kommet, LLC, (hereinafter referred to as the "Claimant") against Chernyshev Moscow machine-building enterprise Joint-Stock Company regarding dissolution of the assorted rolled-metal products (sheets) supply agreement entered into by Chernyshev Moscow machine-building enterprise Joint-Stock Company (hereinafter referred to as the "Defendant") and Trade House Steel Works Red October Joint-Stock Company (hereinafter referred to as the "Supplier") after electronic bidding.

The Defendant recognized the Supplier as the bidding winner, but, in accordance with Clause 3 of Decree No. 925, reduced the goods price offered by the Claimant by 15 percent applying the preferential treatment to the Russian goods over the goods manufactured in the People's Republic of China (hereinafter referred to as the "PRC").

The Claimant refused to sign the received agreement with the reduced price specified believing that the Defendant had had applied the preferential treatment unlawfully and, subject to Clause 8 of Decree No. 925, had no right to privilege the Claimant's goods. Apart from that, the Claimant insisted that, despite the bid stating PRC as the goods country of origin, the goods were actually manufactured in the territory of the foreign state of Taiwan.

In protocol dd. January 25, 2018, the Defendant recognized the Claimant as having evaded from entering into the agreement in connection with the counter-claims regarding the agreement's terms and conditions not subject to change (namely, the goods price) and entered into agreement with the bidder with the second low price (the Supplier).

The Claimant disagreed with that decision and applied to court. The court of three instances supported the Defendant's position and recognized its actions as legitimate.

The Defendant is one of major defense undertakings and manufactures turbojets for combat aviation. Manufactured engines are supplied to the armed forces of the Russian Federation and imported to foreign states.

Articles XX–XXI of the GATT of 1994 establish the states' right to privilege national goods and services in a range of specific spheres. [4] Consequently, the Defendant granted lawfully preferential treatment to Russian goods.

Thus, undoubtedly, provisions of Decree No. 925 should be applied taking into account the rules of the international treaties signed by the Russian Federation, however, given the specific nature of energy companies' operations, application of such provisions is almost impossible.

Judicial practice allows no preferential treatment in the spheres other than public morals protection, defense and security, including armed forces supplies, protection of human life and

health, gold and silver circulation, and protection of works of art and items of historic and archeological value.

So, let us analyze examples from other spheres.

Siltek, LLC (hereinafter referred to as the "Claimant") filed a claim with court against Russian Post requesting invalidation of the results of the open invitation for electronic quotations (for supplies of self-adhesive bags for the needs of the Federal Postal Service Department of Novosibirsk Region, a branch of Russian Post). [5]

The unlawful (in the Claimant's opinion) preferential treatment of the organization recognized as the winner of the open invitation for quotations was the ground of the complaint.

Five bids were received during the open invitation for quotations out of which four bidders (including the winner of the open invitation for quotations, PTK-VAKUMPAK-M, LLC) offered to supply goods of Russian origin and one bidder (the Claimant) offered to supply goods of foreign (Chinese) origin.

Summarizing the results of the bidding process, Russian Post applied the preferential treatment stipulated in Clause 3 of Decree No. 925 and named PTK-VAKUMPAK-M, LLC, winner. One should note that the courts of three instances supported the Claimant and satisfied the claims to invalidate the agreement dd. September 27, 2018, made with the winner of the open invitation for quotations (Judgement of the Moscow Circuit Commercial Court No. A40-253934/2018 dd. July 25, 2019).

Since the bidders participating in the invitation for quotations offered the goods originating from the Russian Federation and a WTO member (China), the preferential treatment stipulated in Decree No. 925 should not have been granted to either bidder, and the Claimant's bid should have been considered on the same terms as other bids.

Antimonopoly authorities also occasionally make mistakes in applying the rules set forth in Decree No. 925.

Thus, for example, FAR-EASTERN GRIDS COMPANY JOINT STOCK COMPANY (hereinafter referred to as the "Customer") announced launching of a bidding process in the form of open request for quotations for supply of the "Loader-digger" item. Three bidders applied, one of them offering goods of Russian origin (Uralskaya Marka, JSC) and two others (Spetstekhnika, LLC, and Tekhservis Khabarovsk, LLC, who has lodged the complaint) offered goods of foreign (Indian) origin. [6]

The procurement commission named Uralskaya Marka, JSC winner after the final ranging of the bids applying Decree No. 925 and granting preferential treatment to the goods of Russian origin in the form of reducing the initial price specified by that bidder by 15%.

Tekhservis Khabarovsk, LLC applied to the Administration of the Federal Antimonopoly Service for Amur Region (hereinafter referred to as "AFAS for Amur Region") stating that the procurement commission's actions created preferential conditions for the bidders and, thus, permitted limitation of competition.

However, the antimonopoly authority (same as the courts of the first two instances) supported the Defendant and dismissed the complaint. Later, the cassation instance court reversed all of the resolutions (Judgement of the Far East District Court No. Ф03-733/2019 dd. May 23, 2019).

The court stated that in the course of procurement process, one should observe the following principles: procurement transparency, equal rights, justice, non-discrimination, and absence of unreasonable limitation of competition among the procurement participants.

This corresponds to the main principle of energy law, which is ensuring the balance of interests of participants of public relations in the sphere of energy, as well as to the tasks of energy law order [7].

It is prohibited to apply requirements to procurement participants, goods, works and services being procured, and contractual terms and conditions, or evaluate and compare procurement bids using criteria or a procedure, not specified in the procurement documentation.

Requirements stipulated for procurement participants should be applied equally to all of them. Taking into account that GATT of 1994 directly stipulates granting equally favorable treatment for WTO member states (India being one of them), the commission had no right to apply

preferential treatment under Decree No. 925. The Ministry of Economic Development of the Russian Federation supports a similar position with its letters regarding the application of Decree No. 925 written in reply to particular applications and published at the website "Contract system navigator"; those letters are also relevant for the legal analysis of the issues considered in this study [8]. Let us look at some of the Ministry's explanations in more detail.

1. According to letter No. Д28и-1631 of the Ministry of Economic Development of the Russian Federation dd. April 14, 2017, the country of the goods' origin is established based on the declaration of the goods' origin or the certificate of the goods' origin.

2. It is mandatory that procurement documentation should contain details stipulated in clause 5 of Decree No. 925. In that case, substitution of the manufacturer's country is not permitted, except for cases when the goods are replaced with the products of Russian origin of the same quality and with the same technical and functional features as specified in the supply agreement (letter No. Д28и-1629 of the Ministry of Economic Development of the Russian Federation dd. April 17, 2017).

3. According to letter No. Д28и-1656 of the Ministry of Economic Development of the Russian Federation dd. April 24, 2017, the Customer is required to describe the subject matter of the agreement specifying the procurement identification code in accordance with the All-Russian Classifier of Types of Economic Activity (hereinafter referred to as "OKVED"), with sections and subsections being mandatory fields and classes, subclasses, groups, subgroups, and types being recommended fields, as well as in accordance with the in the All-Russian Classifier of Products by Types of Economic Activity (hereinafter referred to as "OKPD2"), with sections and classes being mandatory fields and subclasses, groups, subgroups, and product (works, services) types, as well as product (works, services) categories and subcategories being recommended fields.

4. In letters No. Д28и-2858 dd. October 21, 2016, , No. Д28и-2839 dd. October 21, 2016, No. Д28и-55 dd. January 9, 2017, No. Д28и-42 dd. January 9, 2017, No. Д28и-3197 dd. December 6, 2016, No. Д28и-3107 dd. November 18, 2016, the Ministry of Economic Development of the Russian Federation confirms that goods of Belarusian manufacture and those originating from the Eurasian Economic Union member states, as well as works and services performed and provided by the said entities are granted preferential treatment same as goods of Russian origin , works and services performed and provided by Russian entities.

5. It is allowed to privilege goods originating from the WTO member countries, but only in the spheres of defense and security, including armed forces supplies, protection of human life and health, gold and silver circulation, and protection of works of art and items of historic and archeological value (letter No. Д28и-1656 of the Ministry of Economic Development of the Russian Federation dd. April 24, 2017).

Based on the above, one can make the following conclusions.

Undoubtedly, Decree No. 925 sets an important economic task of supporting domestic equipment manufacturers. However, without relevant legal support for the development of Russian industry and ensuring its competitiveness such efforts will not have effect.

Firstly, no energy company can afford procurement of poor-quality equipment. Thus, it is crucial to evade the blind striving to place as much orders in the domestic market as possible, and when choosing among the support for the domestic manufacturer and citizens' security, the security should be prioritized.

Secondly, as it has been considered above, the imports substitution policy should not interfere with the business efficiency of an undertaking. By virtue of article 3 of Federal Law 223-FZ, customers should be governed by the principle of the intended and economically efficient funds spending and develop measures aimed at reducing customer's costs.

Accordingly, where it is more reasonable and profitable to choose a bidder providing services in the territory of a foreign state, creating limitations hindering the satisfaction of such need is inexpedient.

Today, Decree No. 925 can be applied to World Trade Organization member states only in certain fields, such as public morals protection,

defense and security, including armed forces supplies, protection of human life and health, gold and silver circulation, and protection of works of art and items of historic and archeological value.

In all other spheres of operation, the rules of the provisions of the General Agreement on Tariffs and Trade of 1994 and Treaty on the Eurasian Economic Union dd. May 29, 2014 will limit the application of Decree No. 925. ■

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