

NEW CUSTOMS EXEMPTIONS FOR CERTAIN TYPES OF PASSENGER AIRCRAFT

August 17, 2010

To Our Clients and Friends:

On July 16, 2010 the Commission of the Customs Union (“CU”) adopted a resolution (the “Resolution”) providing certain substantial customs concessions for airlines of CU member states. In particular, the Resolution provides for:

- full conditional exemption from customs duties and taxes (together, “customs payments”) in respect of a range of temporarily imported civil passenger aircraft;
- partial conditional exemption from customs payments, for a period of up to 34 months, in respect of certain imported civil passenger aircraft;
- full exemption from customs duties in respect of civil passenger aircraft imported into Kazakhstan and Belarus; and
- full exemption from customs payments in respect of aircraft engines and spare parts and equipment used for the repair and maintenance of civil passenger aircraft of foreign manufacture.

The Resolution comes into effect on August 19, 2010; however, certain provisions will take effect only after the relevant regulatory framework is put into place.

FULL CONDITIONAL EXEMPTION FOR TEMPORARILY IMPORTED AIRCRAFT

Aircraft are fully conditionally exempt from customs payments if they have:

- an aircraft operational empty weight of more than 20 MT, but not more than 120 MT; and
- a maximum aircraft seat capacity of between 111 and 161, or 219 to 300 seats.

Such aircraft include, for example, Airbus 319, Airbus 320 and Boeing 737, popular among Russian airlines.

These aircraft are fully conditionally exempt if:

- the agreements in relation to the purchase of the aircraft were executed and the aircraft placed under a temporary importation customs regime prior to December 31, 2013; and
- the temporary importation period does not extend beyond December 31, 2018.

The exemption is granted for the full period defined in cross-border agreements between counterparties within the CU member states, but not beyond December 31, 2018. If the term of the agreement ends after this date, then the temporary import period may be extended by up to 34 months, and for such aircraft a partial conditional exemption from customs payments will apply after December 31, 2018 (whereby for each full or partial calendar month that the aircraft is located within the customs territory of the CU there is a charge of 3% of the sum of all customs payments that would be payable if the aircraft had been released for domestic use).

On the expiration of the temporary import period, the aircraft must either be re-exported or released for domestic use with payment of all or the remainder of customs payments due as of the date of placement of the aircraft under the temporary import regime (unless the total amount of the customs payments was paid in full during the temporary import period with partial conditional exemption). At present, for all aircraft eligible for full conditional exemption, the customs duty payable upon release for domestic use is 20% plus VAT (calculated as a percentage of the sum of the customs value of the aircraft plus customs duty), at a rate established by the laws of the CU member state in whose jurisdiction the aircraft is placed under the customs regime. In Russia, the VAT applicable to civil passenger aircraft is 18%.

In accordance with the Customs Code of the CU, when temporarily imported goods are released into free circulation, interest accrues¹ on the amount of the deferred customs payments. Pursuant to the Resolution, for aircraft released for domestic use that were temporarily imported under the Resolution, no interest is charged on deferred customs payments or payment by installment.

The legal drafting and wording of the Resolution raise a number of questions, addressed below.

No List of Goods Temporarily Imported with Full Conditional Exemption from Customs Duties and Taxes

In accordance with the Resolution, this exemption is introduced by way of inclusion of a new paragraph in the List of Goods Temporarily Imported with Full Conditional Exemption

¹ *In Russia, such interest is equal to the Bank of Russia refinancing rate.*

from Customs Duties and Taxes, specifying the aircraft covered by the exemption. However, as of the date of this Client Update, no such list has been established at the CU level. According to sources in the Russian Federal Customs Service speaking off-the-record, a draft list will probably be considered by the CU Commission in mid-August or early September. At the same time, there were many disagreements regarding the list, and to date not all of them have been resolved. Thus, until such list is approved and takes effect, it is unlikely that full conditional exemption from customs payments in respect of temporarily imported aircraft will, in practice, be granted.

A similar list exists in Russian customs legislation,² however, the goods included in this list are, as a rule, imported for non-commercial purposes (for example, facilitating foreign economic activity and international cooperation in certain areas, such as international aid). Thus, the implementing rules could contain further conditions, such as the purpose of import or intent of use.

Application of the Resolution to Existing Agreements

The exemption will apply to aircraft covered by the agreements executed after the Resolution comes into force, but it is unclear whether it also applies to the agreements executed before that date. It is therefore questionable whether the below listed options are possible and, if so, in what form.

- Can aircraft that are already imported be placed under full conditional exemption for the period up to December 31, 2018 without terminating the existing customs regime, and after December 31, 2018 can the temporary import period be extended for 34 months and the customs payments already made be taken into account? In this case, the customs value and rates of customs payments would be applicable as of the date of the initial importation, so this scheme may be less efficient than the options below.
- Can the existing customs regime be terminated and the aircraft placed under the temporary import procedure with full conditional exemption on the basis of existing agreements executed prior to the effective date of the Resolution (August 19, 2010) or does one need to re-export the aircraft and sign a new agreement? If the term of the agreement continues beyond December 31, 2018, it seems likely that it should be possible to: (a) extend the maximum term of temporary import to 34 months, or (b) terminate the temporary import procedure with full conditional exemption and declare

² *Approved by Decree No. 599 of the Government of the Russian Federation dated August 16, 2000 (as amended) on the List of Goods Temporarily Imported/Exported with Full Conditional Exemption from Customs Duties and Taxes.*

the aircraft under the temporary import procedure with partial conditional exemption for a period of up to 34 months. In the event of (a) the rates of customs payments and the customs value should, more than likely, be determined as of the date of placement of the aircraft under the temporary import procedure with full conditional exemption (with all of the customs payments already made not taken into account), while in the event of (b), the rates of customs payments and the customs value will have to be determined as of the date that the aircraft is declared for purposes of the temporary import procedure with partial conditional exemption, that is, after 2018. However, there is a risk that the Customs Code of the CU might change before December 31, 2018, and as a result this option may not be available.

Agreements Executed for a Term Ending After December 31, 2018

The Resolution provides that aircraft are eligible for the full conditional exemption “in the event that agreements... are executed... prior to December 31, 2013 and for a term exceeding such date by no more than 5 years.” This wording could be interpreted to mean that aircraft in respect of which agreements are executed for a term in excess of five years after the date indicated are not eligible at all for full conditional exemption. However, as we understand it, given a systematic interpretation of the Resolution, this wording should mean that for such agreements a full conditional exemption is only possible for a period up to December 31, 2018, while for the remainder of the term of the agreement (not more than 34 months) a partial conditional exemption will be in place.

The Resolution provides that if the agreement continues to be in force after December 31, 2018, the temporary import period may be extended by 34 months. However, the Resolution does not specify from what date (the date of the customs declaration or after December 31, 2018) such an extended period will come into effect, and at what point (upon the initial declaration or not later than December 31, 2018) the person making the declaration needs to apply for the extension. The logical assumption would be that what is intended is an extension of the temporary import period for 34 months after December 31, 2018, so that upon the expiry of the 34-month period and after payment of all customs payments by installment under the partial conditional exemption (3% per month), the aircraft would be deemed released for domestic use. However, the question of when the application for extension must be made, as well as whether this rule applies to agreements executed prior to the effective date of the Resolution, remains open.

TEMPORARY IMPORT OF AIRCRAFT FOR A PERIOD OF UP TO 34 MONTHS

The Resolution restores the possibility of temporary import of aircraft with partial conditional exemption from customs payments for a period of up to 34 months, as provided

in the Customs Code of the Russian Federation (the “Russian Customs Code”).³ Pursuant to the Resolution, any civil passenger aircraft (other than aircraft falling under a full conditional exemption in accordance with the above,) may be temporarily imported to the CU for a period of up to 34 months with partial conditional exemption from customs payments. Such aircraft do not have to be classified as fixed production assets, and the persons using such aircraft do not have to hold ownership title thereto (as required by the Russian Customs Code). Provided that all customs payments are duly made, upon the expiry of the 34-month period the aircraft is deemed released for domestic use, with no additional payments. Under paragraph 4 of the Resolution, in this case no interest is charged on deferred customs payments or payment by installment.

EXEMPTION FROM CUSTOMS IMPORT DUTIES

The Resolution also exempts a range of aircraft spare parts and equipment from customs import duties.

For Belarus and Kazakhstan, the following are exempt from customs import duties:

- aircraft imported prior to July 1, 2014 with an aircraft operational empty weight of more than 20 MT, but not more than 120 MT, and a maximum aircraft seat capacity of more than 50, but not more than 300 seats, to be operated for international flights and/or domestic flights within the territory of the state of import of the respective aircraft and/or between CU member-states; and
- the aircraft specified in the first paragraph above imported to Belarus and Kazakhstan during their term of operation after undergoing repairs and maintenance outside the customs territory of the CU.

For all CU member-states: exemption from customs import duties for aircraft engines, spare parts and equipment used for the repair and maintenance of aircraft of foreign manufacture. The implementation of this rule requires the adoption of a resolution by the CU Commission on the procedure for granting customs concessions in respect of aircraft engines, spare parts and equipment, which has not yet been done. Until such resolution is adopted and enters into force, it is unlikely that this exemption will be granted in practice. It is expected that such resolution will be adopted before the end of October. It is also not

³ Presently, the Russian Customs Code is applied to the extent that it does not contravene the CU Customs Code. For application of the Russian Customs Code, see Letter No. 01-11/31847 dated June 29, 2010 of the Russian FCS on Non-Applicability of Certain Provisions of the Customs Code of the Russian Federation No. 61-FZ dated May 28, 2003.

clear whether there might be additional criteria established for the application of the exemption, and whether such a concession might extend to foreign aircraft engines, spare parts and equipment used for the repair of Russian-manufactured aircraft.

This concerns only an exemption from customs import duties, and such exemption does not apply to VAT charged at the border of the CU at rates established by the laws of the respective CU member state.

SUSPENSION OF THE TEMPORARY IMPORT REGIME

The Resolution sets forth that the temporary import regime may be suspended if aircraft (together with any goods used for the repair and technical maintenance thereof) is placed under an inward customs processing procedure or under a special customs procedure (*i.e.*, a customs procedure defining the requirements and terms of use and/or control of certain categories of goods within or outside the customs territory of the CU – such as, for example, temporary export).

A special customs procedure may be applied to aircraft with an aircraft operational empty weight of more than 20 MT, but not more than 120 MT, and a maximum aircraft seat capacity of more than 50, but not more than 300 seats, as well as to aircraft engines, spare parts and equipment used in the civil aviation industry, upon the export thereof from the customs territory of the CU for the repair and/or technical maintenance thereof, including capital repairs and/or upgrading, provided they are re-imported within a period of six months. It is not clear from the Resolution at what point the period for re-import commences; more than likely, it will start on the day that customs clearance on export of the aircraft from the territory of the CU is completed.

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We would be happy to answer any questions you may have regarding the above, as well as any other aspects of aviation law.

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