

New Energy Efficiency Legislation in Russia

December 2009

Russia

Russian leaders have admitted that the modernisation of the economy will not be possible until there is some development of energy effective systems. This is demonstrated by the adoption of the Federal Law No. 261-FZ “On Energy Saving and Energy Efficiency Increase and Amending Certain Legislative Acts of the Russian Federation” (hereinafter referred to as the “Law”) which represents an important step forward notwithstanding its deficiencies and gaps (which are supposed to be filled by relevant bylaws).

The Law is a central act embracing general principles of Russian policy in the sphere of energy efficiency (EE) and energy saving (ES). It was signed by the President on 23 November 2009 and published officially on **27 November**. The majority of the provisions of the Law enter into force from the day of its official publication, though modifications to the Tax Code (Part I No. 146-FZ dated 31 July 1998 and Part II No. 117-FZ dated 5 August 2000) will enter into force on 27 December 2009, and modifications to the Code of Administrative Offences No. 195-FZ dated 31 December 2001 – on 22 June 2010.

The Law replaces the previous Federal Law “On energy efficiency” No. 28-FZ dated 3 April 1996 which is distinguished by its declarative nature and absence of real measures allowing real development of energy saving technologies in Russia.

Furthermore, approval of the Law is being accompanied by **various legislative changes**, including a wide array of amendments to the Russian Tax Code, Code of Administrative Offences, Federal Law “On public procurements for the delivery of goods, works accomplishment and services rendering” No. 94-FZ dated 21 July 2005 etc. Moreover, the adoption of the Law, as a framework act, requires the development of numerous bylaws: according to the Explanatory Note attached to the Draft Law, 17 Decrees of application will be adopted by the Government (covering such issues as EE requirements for goods, including electric bulbs, EE requirements for buildings and constructions, EE classes of goods and apartment buildings, EE requirements for public procurements, requirements for regional and municipal programs in the sphere of EE¹, etc.). In addition, plural bylaws will be adopted by relevant federal ministries before 1 May 2010.

¹ Please note that several Draft Government Decrees have been already prepared and, consequently, relevant Decrees will be enacted in the very near future.

The declared aim of the Law is to create a legislative, economic and organisational stimulus for ES and increasing EE. Its effect extends to all kinds of activities associated with the use of energy resources, including, inter alia, water supplied, transferred and consumed using centralised water supply systems. The legal regulation of these activities is founded on the following **basic principles**:

- efficient use of energy resources;
- support and encourage ES and increase in EE;
- systematic and integrated character of ES and EE programs;
- planning and integration of activities increasing ES and EE;
- use of resources with account to resource, technological, ecological and social conditions.

EE Requirements for Circulation of Goods

According to the Law, goods produced on the territory of the Russian Federation and imported to Russia must contain information on their **EE classes** in the attached technical documentation, as well as on their tags and labels. This requirement will concern (i) domestic energy-consuming devices² from 1 January 2011; (ii) computers, computer electronic devices and “organisational” hardware (fax machines, copiers etc.) from 1 January 2012; and (iii) other goods as defined by the relevant Government Decree³. The specification of EE classes will be realised by the Ministry of Industry and Trade with the concurrence of the Ministry of Economic Development (MED). However, the Draft Government Decree provides for 7 (from “A” (maximum efficiency) to “G” (minimum efficiency)) classes of goods, depending on their technical characteristics,

² According to the Draft Government Decree, these devices will include TVs, refrigerators, domestic air-conditioners, electric cookers, cars etc.

³ The Draft Decree extends this requirement to lifts used for the transportation of people and heating appliances from 1 January 2012.

constructive peculiarities, productivity, volume of energy resources consumption and other criteria.

Please note that the final definition of EE class for specific types of goods will be the responsibility of **producers and/or importers**. Obviously, this will represent an important marketing policy issue for certain producers.

Failure to comply with these requirements will result in **administrative liability**⁴.

Moreover, the EE requirements for the circulation of goods cover the widely debated issues concerning the introduction of **energy efficient bulbs**. The Law prohibits the circulation of incandescent lamps with power exceeding 100W for the purposes of alternating current and lightning from 1 January 2011. Optional rules stipulating the prohibition of incandescent lamps with power exceeding 75W from 1 January 2013 and with power exceeding 25W from 1 January 2014 are also fixed by Law but they are supposed to be revised in future, depending on the first results of the EE program in Russia. Even more severe rules are fixed for the public sector: no public procurements for the supply of incandescent bulbs of all power characteristics shall be allowed from 1 January 2011, except for supply of electric bulbs for premises used for large groups of people (halls of theatres and cinemas, lecture auditoriums, restaurants, etc.).

It is noteworthy that interesting business opportunities may arise in the future in the sphere of waste products treatment (collecting old bulbs). Indeed, according to the Law, a special program providing for organisational, financial and other conditions in the sphere of waste products treatment shall be adopted by the Government and enacted upon in 2011. The Government will probably introduce an incentive system in this sphere, in particular, for foreign companies, as Russian companies do not possess the relevant equipment and technologies for treating waste products.

The Law provides for the adoption of EE requirements for lighting equipment and electric bulbs **by 1 March 2010**.

EE requirements for buildings, structures, installations

According to the new EE rules, buildings, structures and installations must comply with **obligatory requirements** fixed by the Ministry of Regional

⁴ A penalty for executives at the rate of RUB 10,000 – 15,000 (approx. EUR 227-341), for individual entrepreneurs at the rate of RUB 20,000 – 35,000 (approx. EUR 455-795) possibly followed with confiscation of goods, for legal entities at the rate of RUB 100,000 – 150,000 (approx. EUR 2,273-3,409) with possible confiscation of goods.

Development in concurrence with the Ministry of Energy (ME) and MED under a special Decree adopted by the Government. The EE requirements will be revised every 5 years and include:

- indicators characterising specific quantities of energy resources consumption in the buildings/constructions;
- requirements relating to the architectural, functional, technological, constructive, engineering and technical solutions influencing the EE of buildings/constructions;
- requirements relating to separate elements of buildings/constructions;
- requirements relating to equipment and technologies used in buildings/constructions; and
- requirements relating to technologies and materials applied in course of construction, reconstruction, major repairs.

The said requirements will apply to all types of buildings save for some exceptions (e.g. religious buildings, structures and installations, buildings of cultural heritage, temporary structures with service of less than two years, buildings commissioned before the entry into force of the Law etc.), as stipulated by the Law.

The EE requirements will indicate the persons (developers/builders/owners) responsible for their implementation. One of the most important requirements will be the indication of the **EE classes** of apartment buildings on their facades. The details of the of EE classes corresponding to the relevant list accepted in the EU countries will be defined by the federal ministries specified above. Furthermore, the Draft Decree stipulates for obligatory requirements for developers and builders concerning the equipment of new buildings.

The Law also requires that every building be provided with **energy accounting meters** (“**energy gauges**”) and fixes deadlines for the installation of such equipment. Thus, commercial and industrial buildings and constructions will be equipped with water, natural gas, thermal energy and electrical energy meters by 1 January 2011. In apartments and dwelling houses, the energy gauges (both collective (for the whole building) and individual (for separate apartments)) will be in place by 1 January 2012.

Finally, failure to comply with EE requirements in designing, construction, reconstruction and capital repairs, as well as failure to comply with gauge fitting requirements entails administrative responsibility⁵.

⁵ A penalty for executives at the rate of RUB 20,000 – 30,000 (approx. EUR 455-682), for individual entrepreneurs at the rate of RUB 40,000 – 50,000 (approx. EUR 909-1,136), for legal entities at the rate of RUB 500,000 – 600,000 (approx. EUR 11,364-13,636).

The Law also fixes **special types of liability** for builders and developers: in cases of non-compliance with EE requirements and obligations connected with installation of energy accounting meters, during design, construction, reconstruction or capital repairs, the owner can claim free rectification of breaches within a reasonable period of time, or reimbursement of costs incurred in rectifying these infringements.

Some other types of administrative infractions will also be introduced in the Code of Administrative Offences by the Law. In several cases the rules of civil (e.g. compensation of damages) and disciplinary (observation, reprimand, dismissal) responsibility will also apply.

EE Requirements for Public Sector

In general, the public sector represents one of the most important priorities of the Law. For example, it fixes the **obligation of budgetary institutions to ensure a reduction by 15% of water, fuel, natural gas, thermal energy, electrical energy, coal and black oil consumption within 5 years** from 1 January 2010 based on 2009 figures. At the same time, the yearly reduction of energy consumption may not be less than 3%. Furthermore, companies with state participation as well as companies carrying out regulated types of activities are obliged to approve and realise programs aimed at EE increase. Requirements for programs of tariff-regulated organisations will be fixed by relevant federal ministries.

The Law also states new conditions of public procurements in the energy sphere and introduces new type of contracts named "energy service agreements".

1. Public procurements

According to new rules set by the Law and Draft Government Decree on obligatory rules to public procurements, all orders by state or municipal clients will be realized according to obligatory ES and EE requirements fixed by MED and ME with the concurrence of the Ministry of Education and participation of "Russian corporation of nanotechnologies (Rusnano)". These requirements will concern certain types of goods (e.g. new contemporary goods produced with highly energy effective technologies etc.), works (e.g. operating and capital repairs, construction and development etc.) and services and include:

- minimum parameters of consumption (use)/energy efficiency of energy resources; and

- technological solutions influencing the energy efficiency of goods/works/services ordered.

The above-listed federal ministries and state corporation "Rusnano" will be charged to monitor yearly the market of energy efficient goods, works and services and review EE requirements for public procurements once every three years.

2. Energy service agreements

Energy service agreements will regulate actions aimed at ES and greater EE of energy resources use by the client. This kind of agreements must include the following **obligatory conditions**: (i) volume of energy resources saving guaranteed by the contractor; (ii) expiration date of the agreement (may not be less than the term necessary for the achievement of the volume of energy resources saving set by the agreement); and (iii) other obligatory conditions provided for by Russian legislation.

The **discretionary terms** of energy service agreements may include, inter alia, a clause on the price fixed subject to results attained or planned due to the realisation of the contract, (e.g. subject to the value of energy resources savings), and a clause stipulating the obligation of the executor to install and use the energy accounting meters etc.

Clauses of energy service agreements may be included in contracts of sale and purchase, supply or transfer of energy resources (except natural gas). Model conditions of these contracts will be developed by relevant federal ministries.

Please also note that important peculiarities relating to the conclusion of energy service agreements with public organisations (concerning pricing policies, mechanisms of conclusion etc.) are now introduced by the Federal Law "On public procurements for the delivery of goods, works accomplishment and services rendering" subsequently amended by the Law.

Control Mechanisms

The Law provides for two main types of energy control: **voluntary** (energy surveys) and **obligatory** (energy audit). As a general rule, energy control is deemed voluntary save as stipulated by the Law⁶ in certain

⁶ According to art. 16 of the Law, an obligatory energy audit must be conducted in respect of stated regulated companies, companies operating in production or transport of energy (water, oil, gas, etc.) or investing in ES and EE, and financed by federal or regional budgets, as well as companies with yearly energy consumption exceeding RUB 10 million. Listed companies will have to realise their first energy audit by 31

circumstances. All types of energy control are realised by self-regulated organisations on products, technological processes, as well as on legal entities and individual entrepreneurs. Energy control is aimed at:

- collecting objective data on the volume of energy resources used;
- definition of EE indicators;
- definition of ES and increase in EE potential; and
- development of a list of possible programs targeted at EE increase and evaluation.

The results of energy control must be reflected in **energy passports** comprising information on availability of energy accounting meters, volume of energy resources used and the modifications of this volume etc. All information contained in the energy passports will be included to the **State Energy Register** kept by ME.

In order to encourage private investors to participate in the EE program, the Law also proposes a range of **incentives**, both in the economic and tax spheres.

For example, tariff-regulated companies transferring energy resources will be able to apply two alternative incentives during a maximum 5 year period: either to gross-up their proceeds by the amount of expenses incurred for actions aimed at energy resources losses reduction, or retain economy generated due to investments in EE and ES.

The tax incentives include, in particular, investment tax credits up to 30% for companies investing in EE and ES technologies, accelerated depreciation of assets belonging to the category of objects with high EE or sites classified in top EE classes and partial compensation of interest on loans granted by Russian banks for the purpose of investing in ES and increased EE technologies (for more details, please refer to our CMS Tax Outlook # 8 of November 2009 "Tax Aspects of New Energy Efficiency Legislation in Russia").

Furthermore, in order to draw the attention of the public to EE and ES matters, the Law provides for a wide range of measures aimed at **informing** people and raising their awareness, including:

- state information system in the sphere of EE and ES (including national report of MED presented yearly to the Government and concerning the results of implementing measures in the sphere of EE and ES);
- publication of regional and municipal programs;
- organization of educational programs, exhibitions of equipment and technologies of high EE;
- informing consumers about EE classes of goods etc.

December 2012 and subsequent energy audits – not less than once every 5 years.

In general, it is difficult to anticipate what impact the Law will have in Russia insofar as, despite its integrated character, it only relates to the reduction of energy consumption. This means that legal mechanisms proposed by other laws will need to be developed (e.g. in particular, the Federal Law "On concession agreements" No. 115-FZ dated 21 July 2005 and Draft Law on heat supply adopted in the first reading on 11 November 2009) in order to stimulate investments in EE technologies at **production** level.

In any event, the Law clearly represents a significant move towards an increase in public awareness of the importance of ES and presents substantial business opportunities for companies working in various sectors of the economy.

If you are interested by any matter arising out of this legislative development and/or are contemplating any investment in the sphere of ES and EE increase, we would be pleased to meet and discuss this further with you.

If you have any questions on the matters referred to in this **CMS NEWSLETTER**, please do not hesitate to contact Dominique Tissot, Partner, at +7 (495) 7864000 or Dominique.Tissot@cmslegal.ru or your regular contact at CMS, Russia.

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