



Russia's Accession to the WTO and Its Implications for the United States

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Summary

In 1993, Russia formally applied for accession to the General Agreement on Tariffs and Trade (GATT). In 1995, its application was taken up by the World Trade Organization (WTO), the successor organization of the GATT. Russia is the largest economy not in the WTO. However, after a number of fits and starts during the 18-year process, Russia's accession to the 153-member WTO will conclude when, as expected, the WTO members invite Russia to join the WTO during the December 15-17, 2011, Ministerial Conference.

The immediate policy issue for Congress will be whether to enact legislation authorizing the President to grant permanent normal trade relations (PNTR) status for Russia, a status that all WTO members are required to provide each other. Some Members of Congress have indicated that they view congressional consideration of PNTR legislation as the opportunity to ensure that the conditions on which Russia is invited to join the WTO address U.S. concerns.

In joining the WTO, Russia will have committed to bring its trade laws and practices into compliance with WTO rules and other market-opening measures. In doing so, it will take a major step in integrating its trading system with the rest of the world. Those commitments include:

- nondiscriminatory treatment of imports of goods and services;
- reducing tariffs and binding tariff levels;
- ensuring transparency when implementing trade measures;
- limiting agriculture subsidies; enforcing intellectual property rights (IPR) of foreign holders of such rights;
- forgoing the use of local content requirements and other investment measures that limit imports; and
- opening government procurement contract opportunities to foreign firms. In joining the WTO, Russia will also commit to accepting WTO dispute settlement procedures.

In return, Russia will have a voice in shaping and implementing the international trade regime. It will be able to hold its WTO partners accountable for adhering to WTO rules in conducting their trade relations with Russia, making those trade relations more predictable and stable. In addition, Russian economic reformers anticipate that WTO membership will make Russia a more attractive location for foreign producers and investors to do business by locking in trade-liberalizing reforms, which could increase Russia's economic growth.

Concerns among U.S. stakeholders regarding Russia's WTO accession are not so much over whether Russia should be admitted into the WTO but rather whether the conditions for its accession are adequate to ensure that Russia fulfills its obligations and provides meaningful trade and investment opportunities for U.S. firms. U.S. IPR holders remain cautious that Russia will enforce its commitments on IPR protection. Russia is currently a relatively small U.S. trading partner. However, U.S. manufacturing, agriculture, and service providers view WTO accession as an opportunity to broaden the bilateral trading relationship. In Russia, agriculture interests and some manufacturers, such as auto producers, are concerned that WTO membership will expose them to foreign competition that will adversely affect their interests.

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Introduction

In 1993, Russia formally applied for accession to the General Agreement on Tariffs and Trade (GATT). Its application was taken up by the World Trade Organization (WTO) in 1995, when it was established to succeed the GATT. The WTO is a 153-member organization that administers a set of multilaterally negotiated rules on trade and trade-related activities. After a number of fits and starts during the 18-year process, Russia's accession to the WTO may be drawing to a conclusion.

Since China and Taiwan joined in December 2001/January 2002, eight countries have acceded to the WTO. Yet, none of those eight accessions has drawn as much interest from Congress and the U.S. policymaking establishment as Russia's pending accession. This interest can be attributed to several factors. Russia is the largest economy that is not a member of the WTO, and therefore, its accession could have important influence on the future of the WTO and its members. In addition, WTO accession is generally considered one of the remaining post-Cold War steps toward bringing Russia into the system of multilateral economic organizations. (Russia is already a member of the International Monetary Fund and the World Bank.)

In addition, for some Members of Congress and other U.S. stakeholders, the experience of China's WTO accession in 2001 has fueled interest and raised concerns regarding Russia's accession. They argue that the United States must not repeat what they view as the mistakes made with China's accession by ensuring that Russia accedes only under conditions that reinforce WTO rules and principles.

The WTO requires each member to extend to other members "immediate and unconditional" most-favored-nation (MFN), nondiscriminatory status, which is called permanent normal trade relations (PNTR) status in U.S. trade law. In order for the United States to comply with this rule and for the United States to have a trade relationship with Russia in the WTO, Congress would have to pass legislation removing the so-called Jackson-Vanik free emigration requirements as they apply to Russia. Therefore, congressional interest in Russia's accession to the WTO is closely tied to congressional action on PNTR for Russia.

This report provides a brief overview of the WTO itself, the accession process in general, and the commitments that Russia has made to join the WTO. The report discusses U.S. policy on Russia's accession and the accession in the context of the U.S.-Russia economic relationship. It outlines the congressional role in the process and the potential impact of WTO accession for Russian trade with the United States.

The WTO and the Accession Process

The WTO's membership of 153 countries and customs areas spans all levels of economic development, from the least developed to the most highly developed economies. The WTO came into existence in January 1995 as a part of the agreements reached by the signatories to the General Agreement on Tariffs and Trade (GATT) at the end of the Uruguay Round negotiations. The WTO's primary purpose is to facilitate trade among its members by administering the roughly 60 agreements and separate commitments made by its members as part of the GATT 1994 (for trade in goods), the General Agreement on Trade in Services (GATS—for trade in

services), the agreement on trade-related aspects of intellectual property rights (TRIPS) and other multilateral trade agreements.

Membership in the WTO commits its members to fundamental principles in trade with one another. These principles include:

- **Most-favored nation treatment (MFN):** The imports of goods and services originating from one member country will be treated no less favorably than imports of goods and services from any other member country.
- **National treatment:** Imports of goods and services are treated no less favorably than like goods and certain services produced domestically.
- **Transparency:** Government laws and regulations that affect foreign trade and investment are to be published and made available to all members.
- **Lowering trade barriers through negotiations:** Members agree to participate in negotiations (rounds) to lower trade barriers further and bind tariff levels. Members have conducted eight rounds of negotiations to lower trade barriers with the ninth round—the Doha Development Agenda (DDA)—in progress since 2001.
- **Reliance on tariffs to protect sensitive sectors:** In order to promote predictability and openness in commerce, the WTO requires members to use tariffs and avoid using quotas or other nontariff measures when restricting imports to counter the effects of unfairly traded imports or surges in fairly traded imports. The WTO has a general prohibition on the use of quantitative restrictions on exports and imports.
- **Dispute resolution:** The WTO provides a mechanism for the binding settlement of disputes between members when the dispute involves alleged violations of WTO agreements.
- **Trade policy reviews:** The WTO regularly reviews each member's trade regime to ensure that it conforms to WTO rules. Trade among WTO members accounts for over 90% of total world trade.¹

Article XII of the agreement that established the WTO provides that, “[a]ny state or customs territory having full autonomy in the conduct of its trade policies is eligible to accede to the WTO on terms agreed between it and WTO members.” The accession process begins with a letter from the applicant to the WTO requesting membership. The WTO General Council, the governing body of the WTO when the Ministerial Conference is not meeting, forms a working party (WP) to consider the application. Membership in the WP is open to any interested WTO member.

More than 60 member countries, including the United States, are part of the WP on Russia's accession. The U.S. delegation is led by the Assistant U.S. Trade Representative for WTO and Multilateral Affairs and includes representatives from the other relevant departments and agencies.

¹ Based on WTO background information located at <http://www.wto.org>.

The applicant submits a memorandum to the WP that describes in detail its current trade regime and then responds to questions on the trade regime from the WP members. Once WP members are satisfied that they have all the relevant information, negotiations on the terms of accession begin under the WP's aegis. In general, the acceding country negotiates "multilaterally" with the WP itself on a schedule of commitments pertaining to WTO rules, that is, determining what the acceding country needs to do to bring its trade regime into compliance with WTO rules on goods, services, and other investment measures. It negotiates informally with a self-selected subgroup of the WP on a schedule of commitments pertaining to agricultural support and export subsidies which, when completed, is brought to the full WP for approval. The acceding country negotiates market-opening concessions and commitments on tariffs on goods and a schedule of commitments on services bilaterally with each WP member that chooses to do so. However, WP members may also raise issues bilaterally on rules. The bilateral agreements are submitted to the WTO Secretariat, where they are consolidated into draft schedules on goods and services that will apply to all WTO members once accession is completed. The WP operates by consensus; therefore, any one WP Member can halt proceedings by objection.

The commitments on rules, the schedule on goods, and the schedule on services are included in the WP report. The WP develops and attaches to the report a draft Protocol of Accession, which sets out the terms of accession for the acceding country, and also attaches as an annex a draft Decision for the General Council to invite the applicant-country to accede to the WTO. The package is placed before the General Council (or the Ministerial Conference if it is in session) for approval. Article XII requires the package be approved by at least two-thirds of the WTO members, but in practice approval has been determined by consensus. If approved, the Protocol of Accession is submitted to the applicant, which must accept it by signature or ratification.

Article XII places no deadline or timeframe on the accession process. The length of time can depend on a number of factors, including the complexity of issues at hand and the ability of the WTO negotiators and the negotiators from the applicant to address them. It can also depend on the political will of all relevant parties. Since the establishment of the WTO in 1995, 25 countries have acceded. The shortest amount of time for completing the process has been 2 years and 10 months (the Kyrgyz Republic), and the longest has been 15 years and 5 months (China). Russia's application has already exceeded that record.

Russian Economic Policy and WTO Accession

WTO accession has been supported by some Russian policymakers who have sought to restructure and reform the Russian economy in the post-Soviet era. The fits and starts of the accession process have closely mirrored the advances and retrenchments that have occurred over the last two decades in Russian economic reform efforts.

Russia's transition from central planning was bound to be more difficult and longer than that of the Central and East European states. The communist system was much more entrenched there than in the rest of the Soviet Bloc. Furthermore, Russia does not have a legacy of a market economy to draw on as was the case with some of the Central and East European countries. Russia has had to deal with the legacy of a Soviet economy that was administered to meet the needs of the military, while private sector production and investment and consumer demand were given low priority.

Although former President Boris Yeltsin launched the accession process in 1993, the motivation for the project was tempered by political instability. This included Yeltsin's confrontation in 1993 with the Supreme Soviet, the then-parliament, which consisted largely of former communists. Instability was also caused by Yeltsin's re-election to the presidency by the slimmest of margins, barely winning over the communist party candidate. This period was also one of major economic instability, including very high inflation, high interest rates, a plummeting ruble foreign exchange rate, severe economic contractions, and a mismanaged privatization program—all of which led to a major financial crisis in August 1998. These factors contributed to a political and economic environment not conducive to the economic reforms that an economy in transition would need to undertake in joining the WTO.²

During his first presidential term (2000-2004), Vladimir Putin promoted Russia's integration into the world economy as part of his strategy to revive the Russian economy and retrieve the country from the chaos of the Yeltsin period. This strategy included promoting Russia's accession to the WTO. He proclaimed that this strategy included, "speed[ing] up the work on Russia's accession to the WTO on conditions that are acceptable to us and generally work[ing] to make Russia competitive in all senses of the word."³ The government implemented many of the laws required for reform and also to make its trade regime more consistent with WTO rules, including reform of its customs code.⁴

However, during his second term (2004-2008), Putin retrenched on economic reform by reasserting state control over critical economic sectors, including oil and natural gas, and halting other structural reforms that were intended to diversify the economy away from its dependence on oil and other natural resources. This period was first marked by the arrest in October 2003 of Mikhail Khodorkovskiy, the head of the Yukos oil firm. The government charged him with tax evasion, but popular consensus asserts that he was arrested for challenging Putin politically. He is currently serving a prison term. The arrest of Khordorkovskiy and the brake on reforms generated skepticism regarding Putin's commitment to Russian economic restructuring, which lasted through the end of his second term. It also led to growing apprehension among foreign investors about the viability of Russia as a host for foreign investment. Nevertheless, the Russian economy enjoyed strong economic growth as world oil prices continued to increase and the government practiced prudent fiscal and monetary policies that produced government surpluses and lower inflation.

Putin's support for WTO accession appeared to wane as well.⁵ Nevertheless, Russia made progress towards accession by completing most of its bilateral market access negotiations, including those with the European Union (EU) in 2004, the United States in 2006, and most other participating members by 2009.

The Russian economy was hit hard by the global financial crisis that surfaced in 2008, resulting in an economic downturn, the effects of which are still being felt. It also represented the beginning of the present phase of Russian economic policy that coincides with the presidency of Dmitri Medvedev, who has governed in tandem with Putin as prime minister. The crisis exposed weaknesses in the Russian economy, including its significant dependence on the production and

² Ibid, p. 51.

³ Office of the President of Russia, *Annual Address to the Federal Assembly*, April 3, 2001, <http://www.kremlin.ru>.

⁴ Åslund, Anders, "Why Doesn't Russia Join the WTO?," *The Washington Quarterly*, April 2010, p. 55.

⁵ Ibid., 57.

export of oil and other natural resources. Russia faced a rapid decrease in the prices for oil and other commodities. It also exposed severe weaknesses in the financial system as the financial crisis restricted Russia's access to foreign banking credits, on which many Russian companies depend. Russia also faced investor unease caused in part by its military confrontation with Georgia in August 2008.

By mid-2009, Russia appeared to be close to completing the accession process. However, on June 9, 2009, Putin announced that Russia would be abandoning its application to join the WTO as a single entity and would instead pursue accession with Belarus and Kazakhstan as a customs union, which set back the process for about a year and also raised doubts about Putin's commitment to join the WTO. However, after meeting resistance from WTO members and officials, Russia and the other two countries decided to pursue accession separately, while continuing to coordinate their trade policies within the customs union.

On June 24, 2010, during their meeting in Washington, DC, President Obama and President Medvedev pledged to resolve the remaining bilateral issues regarding Russia's accession to the WTO. The United States also pledged to provide technical assistance to Russia to speed up the process of Russia's accession. On October 1, 2010, USTR announced that the United States and Russia had resolved most bilateral issues, including those related to intellectual property rights (IPR). In addition, Russia completed negotiations with the EU and the other trading partners.

Russia's Commitments and Major Issues

Russia filed the "Memorandum on the Foreign Trade Regime" that began the process for GATT/WTO accession in 1994. The WTO established the Working Party (WP) on the accession in 1995. From 1995 through 1997, the process consisted of Russian representatives answering questions from WP members to clarify the description of the trade regime contained in the Memorandum. It is on the basis of the Memorandum and numerous supplementary documents that the WP members determined what steps Russia needed to take in order to ensure its foreign trade regime complies with WTO rules. Negotiations with WP members and bilateral WTO-member trading partners began in 1998.⁶

By 2009, Russia had completed most of its bilateral negotiations (although some outstanding issues with Georgia remained unresolved until November 2011). The WTO Secretariat reconciled the tariff schedules and other commitments on market access for goods and services that Russia negotiated bilaterally and the commitments on trade in agriculture that are included in the final working party report that is attached to the Protocol of Accession. On November 10, 2011, the WP formally approved the accession package and sent it for consideration by the forthcoming Ministerial Conference in December 2011, at which time the Conference is expected to invite Russia to join the WTO.

In order for Russia to accede to the WTO, it must agree to comply with the terms of all WTO agreements, including GATT 1994, the GATS, and TRIPS. What follows is a discussion of some of the proposed commitments Russia has made through its bilateral negotiations and negotiations with the Working Party. The record of the negotiations and the draft WP report are classified. The

⁶ Åslund, Anders, "Why Doesn't Russia Join the WTO?," *The Washington Quarterly*, April 2010, p. 51.

discussion below is based on open sources and discussions with U.S. officials involved in the negotiations.

Manufactured Goods

WTO members are required to set limits or *bindings* on tariff rates. Frequently the *bound* tariff rates are higher than the actual or *applied* tariff rates, allowing the country some flexibility in its tariff policies but also providing exporters to the market assurances that tariffs will not exceed established ceilings. Russia's average applied tariff rate on manufactured goods was 9.5% in 2011, down from an applied rate of 12.1% in 2005.⁷ Russia maintains high tariff rates on imports of some sensitive products, including both new and used cars and cigarettes.⁸

Russia has agreed to bind its tariffs on manufactured goods at an average rate of around 7.3%.⁹ Within this group, Russia will reduce:

- tariffs on wide-body aircraft to no higher than 7.5% (from 20.0%), tariffs on narrow-bodied aircraft to no higher than 12.5% (from 20.0%), and tariffs on aerospace engines to an average of no higher than 5% (from 10.0%);¹⁰
- automobiles to 12.0% (from 15.1%);¹¹
- construction equipment to an average bound rate of no higher than 5.5%;¹²
- agricultural equipment, including combine harvesters and threshers, to an average bound tariff of no higher than 5.6% ;
- medical equipment to an average bound tariff of no higher than 4.9%;
- high-tech instruments to an average rate of no higher than 4.4%;
- chemicals to an average bound tariff of 5.2% (down from 6.7%) ;
- machinery (e.g., submersible pumps, chain saws, filtering equipment) to an average bound tariff of no higher than 7.2%;
- electrical equipment to 6.2% ;
- consumer goods (e.g., appliances, furniture, recreation goods) to a average bound tariff of no higher than 2.0%; and
- textiles, apparel, footwear, and travel goods to average bound tariff of 11.1%.

⁷ World Trade Organization, Tariff Profiles.

⁸ Economist Intelligence Unit, *Country Commerce 2010*, November 2010, p. 75.

⁹ World Trade Organization, News Items, *Working Party Seals the Deal on Russia's Membership Negotiations*, November 10, 2011, http://www.wto.org/english/news_e/news11_e/acc_rus_10nov11_e.htm.

¹⁰ Some of the following data were reported by the WTO and represent the final commitments made by Russia. Other data were reported by the Department of Commerce and were based on Russia's commitments under the bilateral accession agreement with the United States and may not reflect the lowest rates agreed to in the other bilateral negotiations.

¹¹ Russian officials have indicated that the current tariff is 30% and would be reduced first to 25% then eventually to 15%. *International Trade Daily*, November 15, 2011.

¹² In some cases, the comparable current tariff rates are not available.

Furthermore, Russia has committed to eliminate tariffs on information technology products (currently a 5.4% tariff) listed in the WTO Information Technology Agreement (ITA), such as computers, and agreed to implement 95% of these commitments during the first three years of its accession.¹³

Agricultural Goods

Russian restrictions on imports of agricultural products, particularly meats, have been a sensitive issue in trade relations with the United States, the EU, Brazil, and other agriculture-exporting countries and, therefore, were a very contentious issue during the WTO accession negotiations. Russia applies high tariffs and tariff-rate quotas (TRQs) on agricultural imports.¹⁴ Exporters have also claimed that Russia has applied sanitary and phytosanitary (SPS) controls, which are ostensibly used to protect the health and safety of consumers from food contaminants, as protectionist measures. Russian agricultural subsidies have also been an issue in the accession negotiations.

Market Access

Russia's WTO commitments regarding agricultural trade resulted mainly from bilateral negotiations with the United States, the EU, and members of the Cairns group of agriculture exporters.¹⁵ Russia agreed to bind tariffs on a range of products either at current rates or at lower rates. According to the WTO, Russia agreed to reduce and bind its tariffs on:

- dairy products to 14.9% from 19.8%;
- cereals to 10.0% from 15.1%;
- oilseeds, fats, and oils to 7.1% from 9.0%; and
- wood and paper to 8.0% from 13.4%.¹⁶

Russia's TRQ on pork would be 400,000 tons, and its TRQ on poultry imports would be 350,000 tons. Russia will set its quota on beef imports at 530,000 tons.¹⁷ Some quotas are subject to specific WTO member allocations. According to the WTO, Russia will set and bind its tariff on:

- beef at 15% within the TRQ and 55% outside the TRQ;
- pork at 0% within the TRQ and 65% outside the TRQ (and would replace the TRQ with a flat 25% tariff on January 1, 2020);

¹³ Under its 2006 bilateral agreement with the United States, Russia committed to "join the Information Technology Agreement (ITA)." Office of the United States Trade Representative, *Trade Facts: Results of Bilateral Negotiations on Russia's Accession to the World Trade Organization (WTO)—Non-Agricultural Market Access*, November 19, 2006.

¹⁴ Under TRQs countries allow an established volume of products to be imported into the country at one often relatively low tariff rate but any imports beyond the quota at a higher, oftentimes prohibitive, tariff rate.

¹⁵ The Cairns group includes: Argentina, Australia, Bolivia, Brazil, Canada, Chile, Costa Rica, Colombia, Guatemala, Indonesia, Malaysia, New Zealand, Pakistan, Paraguay, Peru, Philippines, South Africa, Thailand, and Uruguay.

¹⁶ World Trade Organization, News Items, *Working Party Seals the Deal on Russia's Membership Negotiations*, November 10, 2011, http://www.wto.org/english/news_e/news11_e/acc_rus_10nov11_e.htm.

¹⁷ *International Trade Daily*, November 15, 2011.

- selected poultry products at 25% within the TRQ and 80% outside the TRQ; and
- some whey products at 10% within the TRQ and 15% outside the TRQ.¹⁸

Sanitary and Phytosanitary (SPS) Measures

As a WTO member, Russia would be obligated to adhere to the provisions of the WTO Sanitary and Phytosanitary (SPS) Agreement when imposing measures to protect human, animal, or plant life or health. The main objective of the SPS Agreement is to prevent WTO members from using such measures as disguised protectionism. The Agreement allows members to apply their own standards but requires that they be based on science; that they should be applied only to the extent necessary to protect human, animal, and plant life; that they should not discriminate between countries where similar conditions prevail; and that they should distort trade as minimally as possible. Under the agreement, members are encouraged to apply internationally accepted standards but may use higher standards if they are based on science. In addition, members are expected to practice equivalence in order to facilitate trade. That is, if an exporting country can demonstrate that its inspection measures achieve the same level of safety protection as the importing country, then the importing country is expected to accept the exporting country's standards and procedures as "equivalent" to its own.

Reaching agreement with Russia on how it would implement the SPS agreement and bring its regulations into compliance with that agreement has been one of the most challenging aspects of Russia's accession process. The difficulty was related in part to Russia's practice of using rigid SPS requirements for imported animal and plant products. For example, Russia has required certification that imported grains are pest free, a process that could be cumbersome and costly. Russia has also required that imported meats only be shipped from facilities that are on a Russian government-approved list as meeting Russian safety requirements. For the United States, these requirements have adversely affected exports of meats, especially poultry and pork, dairy products, and grains and oilseeds. The United States and other agriculture exporting countries have argued that Russia's SPS requirements do not conform to international standards and are not based on accepted science as required under the WTO SPS Agreement.¹⁹ Russia's bilateral accession negotiations with the United States, EU, and members of the Cairns Group, as well as with the WTO Working Party, focused on ensuring that Russia would pass and implement laws and resolutions requiring agencies to follow international SPS standards.

Another challenge emerged with the formation of the Customs Union (CU) with Belarus and Kazakhstan. Russia has signed agreements with its CU partners that cede authority over customs matters to the CU and require that customs regulations, including SPS regimes, be harmonized among the three CU countries. For example, CU authorities, rather than national agencies, will now issue SPS certificates. In the process of the harmonization, not all of the Russian measures, such as provisions on equivalence and adherence to international standards, were reflected in the CU regulations. WP members have been working to ensure that Russia's commitments to adhere to the SPS Agreement are reflected in the CU regulations.

According to the WTO, Russia has committed, among other things, to:

¹⁸ World Trade Organization, News Items, *Working Party Seals the Deal on Russia's Membership Negotiations*, November 10, 2011, http://www.wto.org/english/news_e/news11_e/acc_rus_10nov11_e.htm.

¹⁹ Office of the United States Trade Representative, *2011 Report on Sanitary and Phytosanitary Measures*, March 2011, p.71-74.

- develop and apply international standards on SPS measures through membership in the Codex Alimentarius, the World Organization for Animal Health (OIE) and the International Plant Protection Convention;
- negotiate veterinary export certificates that include requirements different from those of the customs union if an exporting country makes a substantiated request prior to January 1, 2013, to negotiate such a certificate; and
- refrain from suspending imports from establishments based on results of onsite inspection before it had given the exporting country the opportunity to propose corrective measures.²⁰

Subsidies

Russia has agreed to eliminate all agricultural export subsidies. It had been pressing WP members to allow it to have a cap of \$9 billion on permitted trade-distorting agricultural subsidies, which are called “amber-box” subsidies in the WTO. Its current use of such subsidies has been below that level, but Russian agricultural interests argued that they needed the flexibility of the higher ceiling on trade-distorting subsidies to be able to meet the challenge of increased foreign competition from increased agricultural imports once they join the WTO.²¹ As a result of the negotiations, Russia would be allowed a \$9 billion cap and would reduce these subsidies to \$4.4 billion by 2018. Russia will also be required to limit product-specific subsidies to 30% of allowable trade-distorting subsidies.²²

Export Duties

Russia maintains export duties on hydrocarbons, scrap metals, and other strategic materials. In 2007, it introduced export duties on raw lumber to give an advantage to its domestic lumber processors. This has been a sensitive issue for the EU. At the end of 2010, after intense negotiations with the EU, Russia agreed to abandon a planned increase from 25% to 80% in export duties and instead to establish export quotas with export duties 13%-15%, depending on the type of lumber.²³ On October 21, 2011, EU Trade Commissioner Karel De Gucht announced that the export duty issue had been resolved to the EU's satisfaction. The issue is particularly sensitive to Finland, which is dependent on imports of Russian raw lumber for its lumber processing industry.²⁴

Services

Throughout its bilateral negotiations on Russia's accession to the WTO, the United States assigned priority to obtaining Russian commitments to open its fledgling services sector,

²⁰ World Trade Organization, News Items, *Working Party Seals the Deal on Russia's Membership Negotiations*, November 10, 2011, http://www.wto.org/english/news_e/news11_e/acc_rus_10nov11_e.htm.

²¹ Tarr and Volchkova, p. 208-211.

²² *Inside U.S. Trade*, October 20, 2011.

²³ *International Trade Daily*, November 15, 2011..

²⁴ European Commission Directorate-General for Trade, *EU and Russia Agree to Terms for Moscow's Eventual WTO Accession*, Press Release, October 21, 2011.

especially financial services, to foreign providers. In some cases, the objective was to get Russia to lock in or bind established regulations and practices, and in other cases, the objective was to get Russia to liberalize rules and practices. Because of their leading role among global companies, U.S. services providers would be poised to take advantage of a more open Russian services sector. The United States took the lead in services negotiations, and the final proposed schedule of Russian commitments largely reflects the commitments the United States obtained during the negotiations.²⁵

Regarding financial services, the United States obtained Russian commitments in **insurance and banking**. Russia will allow 100% foreign ownership of non-life insurance companies upon accession and will phase out restrictions on foreign participation in mandatory life insurance and restrictions on the number of licenses granted to foreign life insurance companies during the first five years of membership.²⁶

Furthermore, Russia will raise the ceiling on total foreign ownership in the Russian banking sector from 15% to 50%, will allow 100% foreign ownership of banks and other non-insurance financial entities, and will allow foreign financial services companies to provide asset management services, credit card services, and other payment services. The United States and other WTO members had pressed Russia to allow foreign banks to open branches. Russia refused but will allow foreign banks to open subsidiaries which come under the regulatory control of the Russian central bank. (Russia agreed to discuss the issue of bank branching again when it negotiates its membership in the Organization of Economic Cooperation and Development.)

In the area of **telecommunications services**, Russia agreed to eliminate the government monopoly on land-line long distance services and to allow foreign-owned telecommunications companies to operate in any telecommunications sector. Russia also agreed to establish an independent telecommunications regulator separate from the Ministry of Communications to avoid conflict of interests.

Russia agreed, upon accession, to increase market access for foreign providers of **professional services and business services**, including lawyers, architects, accountants, engineers, health care professionals, advertising, and market and management services. It will also permit foreign-owned companies to establish 100%-owned business service companies in Russia.

Among its other commitments in services, Russia will allow foreign-owned providers of **distribution services, including express delivery and wholesale and retail services**, to establish wholly owned subsidiaries in Russia upon accession. Russia will also open its market to foreign **audio-visual service** suppliers in motion picture distribution and projection services and sales of television and radio programs to TV and radio stations. Russia will also allow foreign audio-visual companies to operate as 100% foreign-owned entities. Furthermore, Russia has made commitments to open its services markets to providers of **energy services and computer and computer-related services**.

²⁵ This analysis of the services commitments is largely based on October 2011 discussions with USTR officials who participated in the negotiations.

²⁶ Office of the United States Trade Representative, *Trade Facts: Results of Bilateral Negotiations on Russia's Accession to the World Trade Organization—Bilateral Market Access Agreement on Services*, November 19, 2006.

Intellectual Property Rights

The lack of intellectual property rights (IPR) protection has tainted the business climate in Russia for U.S. investors for some time. The Office of the United States Trade Representative (USTR) has consistently identified Russia as a “priority watch list” country, most recently in April 2011.²⁷ According to the USTR report, Russia has improved its IPR protection. However, the USTR has found that implementation of IPR laws has been slow and enforcement weak, especially in the area of Internet piracy.²⁸

IPR protection was a pivotal issue in Russia’s bilateral negotiations with the United States and in its negotiations with the WP. Intellectual property owners, such as software creators, movie companies, and music producers, view WTO accession as an opportunity to secure Russian commitments to stronger IPR protection. Under the November 2006 agreement with the United States, Russia made commitments to improve its IPR regime and to meet its obligations under the WTO’s Trade-Related Intellectual Property Rights (TRIPS) agreement. A number of these commitments became effective immediately.

As a result of bilateral negotiations with the United States and other WP members, Russia has

- committed to fight optical disc piracy more effectively by permanently closing down production of optical media containing pirated and counterfeit material;
- enacted legislation to deny licenses to past offenders;
- been shutting down websites that illegally distribute music and other copyrighted works and enacted laws to stop websites from doing so in the future;
- enacted laws to protect pharmaceutical test data from unauthorized use;
- enacted criminal penalties to deter piracy and counterfeiting;
- strengthened border enforcement against piracy; and
- brought Russia’s laws in compliance with international standards under TRIPS.

The United States remains cautious regarding Russia’s enforcement of these commitments. Assistant USTR Chris Wilson said that the United States needs to see “on-the-ground results” from Russia.²⁹

Trade-Related Investment Measures (TRIMS)

The WTO TRIMS agreement is intended to prevent members from employing restrictions on foreign direct investments that distort trade in goods. Such measures include local content requirements that require that a certain level of inputs (raw materials, parts) used by foreign-invested firms be of domestic origin. The TRIMS agreement also prohibits WTO members from

²⁷ Section 301 of the Trade Act of 1974 (P.L. 93-618), as amended, is the principal U.S. statute for identifying foreign trade barriers due to inadequate intellectual property protection. The 1988 Omnibus Trade and Competitiveness Act (P.L. 100-418) created the “Special 301” provisions, which require the USTR to conduct an annual review of foreign countries’ intellectual property policies and practices.

²⁸ Office of the United States Trade Representative, *Special 301 Report*, April 30, 2011.

²⁹ *International Trade Reporter*, June 30, 2011.

using trade-performance requirements, for example, requiring foreign direct investors to export specific shares or amounts of their output.

On April 15, 2005, the Russian government began to implement a program to promote domestic auto production. Under the program, auto producers located in Russia that produce at least 25,000 vehicles annually; used at least 30% local content; and performed welding, painting, and assembly operations within their Russia-based operation would qualify for reduced import duties on imported components. As of February 2011, the requirements were increased to include a minimum of 350,000 vehicles produced annually; 60% local content; stamping operations as part of the locally based production process; and the establishment of research and development centers in Russia to perform engineering, design, and testing of vehicles and parts. Both the United States and the EU argued that the program violates the prohibition against local-content requirements under the TRIMS agreement. The United States obtained a Russian commitment to terminate the program by 2018. However, the EU, a major auto parts supplier to Russia, negotiated further to minimize the adverse impact the program would have to its auto parts-supplying firms. As a result, the EU obtained a commitment from Russia for compensation to remedy the adverse impact of the program on EU auto parts exports.³⁰

Other Commitments

During the accession negotiations, the United States and, in particular, the EU had concerns about the Russian government policy on subsidizing **natural gas prices** for domestic users. They argued that such subsidies gave Russian producers in energy-intensive industries, such as steel production, an unfair advantage over foreign competitors. Russia agreed to price natural gas at market prices to commercial users but could still subsidize prices to households and other non-commercial users.³¹

The **WTO Government Procurement Agreement (GPA)** is a plurilateral pact, that is, only those members who have signed it are obligated to comply with its provisions. Those signatories agree to open up certain government contracts for purchases of goods and services to firms from other signatories. Signing the GPA is not a *prime facie* condition of WTO membership. However, as part of the conditions of its accession, Russia has agreed to join the GPA and to notify its intention to the GPA Committee at the time of its accession and to negotiate the terms of its membership in the GPA within four years of its accession.³²

Impact of WTO Accession on Russia

WTO accession has several economic policy implications for Russia. Perhaps the most important implication would be introducing greater certainty in its trade relations with other WTO members since WTO rules govern how members trade with one another, and a member can appeal to the WTO if it believes that another WTO member has violated those rules. At the same time, Russia

³⁰ European Commission Directorate-General for Trade, *EU and Russia Agree to Terms for Moscow's Eventual WTO Accession*, Press Release, October 21, 2011.

³¹ World Trade Organization, News Items, *Working Party Seals the Deal on Russia's Membership Negotiations*, November 10, 2011, http://www.wto.org/english/news_e/news11_e/acc_rus_10nov11_e.htm.

³² Ibid.

will have to adhere to WTO rules, reducing its ability to impose new trade restrictions in dealing with other members. For example, upon accession, Russia could not arbitrarily raise tariff rates on imports or exports of sensitive products beyond its bound rates or quantitative restrictions on exports and imports. Its trade actions could be subject to WTO dispute settlement procedures initiated by other WTO members, which could lead to sanctions against Russia. WTO accession is also expected to improve the Russian business climate, because traders and foreign investors would consider Russia a less risky place to do business. Furthermore, accession would give Russia a seat at the table in negotiating and implementing the rules.

In addition to the policy implications, WTO accession will likely have some economic effects for Russia. According to a World Bank study, in the medium term, WTO accession would increase Russia's gross domestic product (GDP) by 3.3% and, in the longer term, would increase it by 11%. The study concluded that a small increase in GDP growth would come from more efficient allocation of resources as a result of reduction of tariffs and increased competition from imports. Another small increase would come from improved terms of trade, that is, increased prices for Russian exports relative to imports, as a result of increased demand for Russian exports. The remainder of the increase in GDP, and by far the largest contributor according to the study, would result from measures Russia would take to liberalize foreign investment in services. The study argues that the availability of services from foreign providers of banking, insurance, telecommunications, transportation, and other services would increase the productivity of Russian firms and contribute to overall Russian economic growth. Those manufacturing industries likely to benefit the most from accession include non-ferrous metals, ferrous metals, and chemicals, while machinery and equipment, food and light industry, and construction materials would be adversely affected by increased foreign competition.³³

WTO Accession and U.S.-Russia Economic Relations

Successive U.S. Administrations have supported Russia's accession to the WTO. Most recently the Obama Administration included the issue as a priority in its 2011 trade agenda as part of its efforts to "reset" U.S. relations with Russia.³⁴

The U.S. government has provided advice to the Russian government on how to make its trade and investment regime WTO compatible and to educate Russian firms on the implications of WTO accession. Because the United States is the world's largest economy and has a lot of influence within the WTO, its support is critical to the success of Russia's application. However, the United States has also insisted that Russia enter the WTO on terms that provide meaningful trade liberalization and that require Russia to adhere to WTO agreements upon accession.

U.S. support for Russian accession is just one part of post-Cold War U.S. trade and economic policy that has encouraged Russia to establish a market economy. This policy is itself part of a

³³ Jensen, Jesper, Thomas Rutherford, and David Tarr, *Economy-Wide and Sector Effects of Russia's Accession to the WTO*, May 26, 2004, p. 15-21.

³⁴ Office of the United States Trade Representative, *2011 Trade Policy Agenda and 2010 Annual Report of the President of the United States and the Trade Agreements Program*, Chapter I, p. 6.

larger U.S. foreign policy strategy to anchor Russia in the world community and to reshape the U.S.-Russian relationship into one of cooperation.

U.S. support for Russia in the trade and investment areas has come in the form of technical assistance, trade preferences (including tariff preferences under the U.S. Generalized System of Preferences (GSP) program which gives duty free treatment to many developing countries), and financial assistance to U.S. exporters to, and investors in, Russia through the U.S. Export-Import Bank and the Overseas Private Investment Corporation (OPIC).

U.S.-Russia trade and investment flows have increased in the post-Cold War period, reflecting the changed U.S.-Russian relationship. Many experts have suggested that the relationship could expand further. Between 2000 and 2008, U.S. exports rose 343%, from \$2.1 billion to \$9.3 billion, but declined in 2009 in the wake of the global recession. U.S. exports span a range of products, including meat, machinery parts, and aircraft parts. U.S. imports increased more than 244%, from \$7.8 billion to \$26.8 billion from 2000 to 2008, but declined in 2009. The surge in the value of imports is largely attributable to the rise in the world prices of oil and other natural resources—which comprise a large share of U.S. imports from Russia—rather than to an increase in the volume of imports. U.S.-Russia bilateral trade increased in 2010 as both countries showed signs of recovery.

Table I. U.S. Merchandise Trade with Russia, 1993-2010

(in billions of dollars)

Year	U.S. Exports	U.S. Imports	U.S. Trade Balances
1993	3.0	1.7	1.3
1994	2.6	3.2	-0.6
1995	2.8	4.0	-1.2
1996	3.3	3.6	-0.3
1997	3.4	4.3	-0.9
1998	3.6	5.7	-2.1
1999	2.1	5.9	-3.8
2000	2.1	7.7	-5.6
2001	2.7	6.3	-3.5
2002	2.4	6.8	-4.4
2003	2.4	8.6	-6.2
2004	3.0	11.9	-8.9
2005	3.9	15.3	-11.3
2006	4.7	19.8	-15.1
2007	7.4	19.3	-11.9
2008	9.3	26.8	-17.5
2009	5.4	18.2	-12.8
2010	6.0	25.7	-19.7

Source: U.S. Department of Commerce Data, Bureau of the Census, Compiled by Global Trade Information Systems, Inc., World Trade Atlas.

Despite the post-Cold War increase in bilateral trade, Russia and the United States are still only moderately important trade partners to each other. Russia accounted for 1.3% of U.S. imports and 0.5% of U.S. exports in 2010, and the United States accounted for 3.1% of Russian exports and 5.1% of Russian imports. Russia was the 37th-largest export market and 17th-largest source of imports for the United States in 2010, while the United States was the 11th-largest export market for Russia and its 4th-largest source of imports.³⁵

Similarly, investment relations are modest. According to Russian government data, by the end of 2010, the United States accounted for less than 2.5% of total accumulated foreign direct and portfolio investment. The first three countries were Cyprus (20.7%), the Netherlands (13.5%), and Luxembourg (11.7%), countries that are known mostly as financial centers, suggesting that at least 50% of the investments might have been repatriated Russian funds.³⁶ U.S. exporters and investors claim that a number of factors make them cautious about entering the Russian market: the lack of adherence to international standards of accounting; weak enforcement of intellectual property rights; the lack of protection of shareholders rights; burdensome taxation; poor legal protection of contract sanctity; and government corruption.

Russia's accession to the WTO could have some qualitative and quantitative effects on the relationship in absolute terms. As a number of observers have pointed out, WTO accession would likely bring more stability and predictability to the relationship, reducing the opportunities for unilateral actions. For example, Russia would be limited on how high it could raise its tariffs, as it did on car imports during the recession. It would also be obligated to adhere to WTO agreements on implementing SPS measures, safety and certification procedures, and other trade-related measures.

In addition to these qualitative effects, Russia's WTO accession could have some quantitative effects. One study forecasts that U.S. exports of agricultural products, including meats, grapes, apples, and processed foods, would increase two or three times as a result of reduction in Russian tariffs and standardization of SPS measures.³⁷ The United States could also realize an increase in exports of civil aircraft and aircraft parts, telecommunications equipment, and pharmaceuticals as a result of lower Russian tariffs. Furthermore, improvements in Russia's enforcement of intellectual property rights and concessions on foreign investment could raise the level of investor confidence and increase the level of U.S. business investment in Russia, including investment and trade in services.³⁸

The Role of Congress and PNTR for Russia

“Normal trade relations” (NTR), or “most-favored-nation” (MFN), trade status is used to denote nondiscriminatory treatment of a trading partner compared to that of other countries.³⁹ The WTO

³⁵ *World Trade Atlas*, Global Trade Information Services, Inc.

³⁶ Russian Federal Statistics Service, <http://www.gks.ru>.

³⁷ Åslund, Anders and Gary Clyde Hufbauer, *Why It's in the U.S. Interest to Establish Normal Trade Relations with Russia*, Peterson Institute for International Economics, 2011, p. 5. (Draft)

³⁸ Ibid.

³⁹ MFN has been used in international agreements and at one time was used in U.S. law to denote the fundamental trade (continued...)

requires that WTO members apply MFN tariff treatment “immediately and unconditionally” to the goods of every other WTO member. Title IV of the U.S. Trade Act of 1974 applies conditions on Russia’s status—compliance with freedom of emigration criteria under Section 402, the so-called Jackson-Vanik amendment—that are not applied to other WTO members. (See the **Appendix** for more details on Title IV and the Jackson Vanik amendment.) Therefore, the United States would not be in compliance with the MFN principle without Congress lifting the applicability of Title IV as it applies to Russia and authorizing the President to grant Russia unconditional MFN, or what is often called permanent NTR (PNTR) before Russia enters the WTO. If a WTO member determines that it cannot, for any reason, comply with this or any other WTO rule toward a *newly acceding* member, it can “opt-out” of its obligations toward that member by invoking the non-application provision (Article XIII of the WTO). In so doing, the WTO member declares that the WTO obligations, rules, and mechanisms (e.g., the binding dispute settlement mechanism) will not apply in its trade with the new member in question. The United States continues to invoke Article XIII in its trade with Moldova since it joined in 2001.

If the United States were to invoke “non-application” at the time of Russia’s accession, it would continue to conduct its trade relations with Russia under the provisions of the 1992 “Agreement on Trade Relations Between the United States and Russia.” Article I of this agreement provides for MFN (NTR) and nondiscriminatory treatment in the application tariffs and other customs duties. Article II of the agreement extends MFN treatment to the application of technical regulations and standards (technical barriers to trade). Therefore, any commitments on tariffs and the application of technical barriers Russia will have made on joining the WTO would still apply to its trade with the United States per the MFN provisions of the 1992 agreement, according to Assistant USTR Chris Wilson.⁴⁰

However, Russia would not be obligated to apply the range of other commitments, such as those regarding services, trade-related investment measures, intellectual property rights, and sanitary and phytosanitary measures. In addition, the two sides would not have the use of WTO dispute settlement procedures to resolve issues in their bilateral trade. The United States has invoked Article XIII temporarily at the time of the accession of some countries, for example, Armenia, Georgia, and Vietnam. Once PNTR was extended to these countries, the United States disinvoked the nonapplication clause.

At this writing, no legislation has been introduced in the 112th Congress to authorize PNTR for Russia. Therefore, if the WTO invites Russia to join, the United States may invoke Article XIII, at least temporarily. The likely time it would announce this step would be before the meeting of the December 15-17 WTO Ministerial Conference.

Observations and Outlook

It appears that Russia’s 18-year quest to join the WTO is reaching completion, the longest such process in WTO history. WTO members are expected to invite Russia to join the WTO at the

(...continued)

principle of nondiscriminatory treatment. However, “MFN” was replaced in U.S. law, on July 22, 1998, by the term “normal trade relations.” (P.L. 105-206). MFN is still used in international trade agreements. The terms are used interchangeably in this report.

⁴⁰ The comments were made during a one-on-one discussion with the author.

December 15-17 Ministerial Conference. Should Russia accept, its legislature, the State Duma, would have to ratify the Protocol of Accession. Thirty days after the ratification, Russia would then officially become a WTO Member.

The process had been particularly challenging as a result of domestic political and economic uncertainties that at times seemed to undermine Russia's commitment to undertake the reforms necessary to comply with WTO agreements and rules. The process was also delayed by international crises such as the 1997 and 1998 financial crisis and the 2007-2008 global financial crisis. The process was further complicated in June 2009 with the formation of Russia's customs union with Belarus and Kazakhstan, which is now responsible for most customs matters for the three countries. Also, a dispute between Georgia, a WTO member, and Russia over monitoring of trade between Russia and the two Georgian break-away provinces of Abkhazia and South Ossetia threatened to delay the completion of the accession. On November 9, 2011, the two countries agreed to a suggestion from Swiss mediators that international officials monitor trade between Russia and the two provinces.⁴¹

In joining the WTO, Russia will have committed to bring its trade laws and practices into compliance with WTO rules. In doing so, it will take a major step in integrating its trading system with the rest of the world. Those commitments include nondiscriminatory treatment of imports of goods and services; binding tariff levels; ensuring transparency when implementing trade measures; limiting agriculture subsidies; enforcing intellectual property rights for foreign holders of such rights; and forgoing the use of local content requirements and other trade-related investment measures. Russia will have also joined the WTO, knowing that its fellow WTO members will hold it accountable, through WTO dispute settlement procedures, for fulfilling its WTO commitments. Some U.S. policymakers, for example, view WTO rules as an expanded set of tools with which to manage trade with Russia.

In return, Russia will have a major voice in shaping and implementing the international trade regime in the form of the WTO. It will also be able to hold other WTO partners accountable for adhering to WTO rules in conducting their trade relations with Russia, making those trade relations more predictable and stable. In addition, Russian economic reformers anticipate that WTO membership will make Russia a more attractive location for foreign producers and investors to do business by locking in trade-liberalizing reforms and will boost Russian trade and economic growth.

For the WTO as a whole, Russia's accession will mean that all major economies will be under the WTO umbrella. Russia will help shape the WTO agenda. For some that may be viewed as positive if Russia's interests are congruent with theirs. For others, it may be negative, if those interests are in conflict.

For Congress, the immediate policy issue will be whether to enact legislation authorizing PNTR for Russia. Some Members have indicated that they view congressional consideration of PNTR legislation as an opportunity to ensure that the conditions on which Russia is invited to join the WTO address U.S. concerns. For example, the chairmen and ranking Members of the Senate Finance Committee and the House Ways and Means Committee sent a joint letter to USTR Ron Kirk asking him to make sure that the conditions will require Russia to protect intellectual property rights; commit Russia to adhere to the WTO Information Technology Agreement; not

⁴¹ *International Trade Daily*, November 10, 2011.

impose unacceptable measures to inhibit agriculture imports; and not adversely affect the interests of the U.S. auto industry through its foreign investment policies.⁴² Members may also use debate on PNTR as an opportunity to raise concerns about Russian foreign policy, for example in regards to Georgia, and about human rights, such as the slow prosecution of murderers of investigative journalists.

⁴² *International Trade Daily*, November 2, 2011.

Appendix. NTR Status and Jackson-Vanik

“Normal trade relations” (NTR), or “most-favored-nation” (MFN), trade status is used to denote nondiscriminatory treatment of a trading partner compared to that of other countries.⁴³ Only two countries—Cuba and North Korea—do not have NTR status in trade with the United States. In practice, duties on the imports from a country which has been granted NTR status are set at much lower rates than those from countries that do not receive such treatment. Thus, imports from a non-NTR country can be at a large price disadvantage compared with imports from NTR-status countries.

Section 401 of Title IV of the Trade Act of 1974 requires the President to continue to deny NTR status to any country that was not receiving such treatment at the time of the law’s enactment on January 3, 1975. In effect this meant all communist countries, except Poland and Yugoslavia. Section 402 of Title IV, the so-called Jackson-Vanik amendment, denies the countries eligibility for NTR status, as well as access to U.S. government credit facilities, such as the Export-Import Bank, as long as the country denies its citizens the right of freedom-of-emigration. These restrictions can be removed if the President determines that the country is in *full compliance* with the freedom-of-emigration conditions set out under the Jackson-Vanik amendment. For a country to maintain that status, the President must reconfirm his determination of full compliance in a semiannual report (by June 30 and December 31) to Congress. His determination can be overturned by the enactment of a joint resolution of disapproval concerning the December 31st report.

The Jackson-Vanik amendment also permits the President to *waive* the freedom of emigration requirements, if he determines that such a waiver would promote the objectives of the amendment, that is, encourage freedom of emigration. This waiver authority is subject to an annual renewal by the President and to congressional disapproval via a joint resolution. Before a country can receive NTR treatment under either the presidential determination of full compliance or the presidential waiver, it and the United States must have concluded and enacted a bilateral agreement that provides for, among other things, reciprocal extension of NTR or MFN treatment. The agreement and a presidential proclamation extending NTR status cannot go into effect until a congressional joint resolution approving the agreement is enacted.

In 1990, the United States and the Soviet Union signed a bilateral trade agreement as required under Title IV of the Trade Act of 1974. The agreement was subsequently applied to U.S.-Russian trade relations, and the United States signed similar but legally separate agreements with the other former non-Baltic Soviet states. The United States extended NTR treatment to Russia under the *presidential waiver* authority beginning in June 1992. Since September 1994, Russia has received NTR status under the *full compliance* provision. Presidential extensions of NTR status to Russia have met with virtually no congressional opposition.

⁴³ MFN has been used in international agreements and at one time was used in U.S. law to denote the fundamental trade principle of nondiscriminatory treatment. However, “MFN” was replaced in U.S. law, on July 22, 1998, by the term “normal trade relations.” (P.L. 105-206). MFN is still used in international trade agreements. The terms are used interchangeably in this report.

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