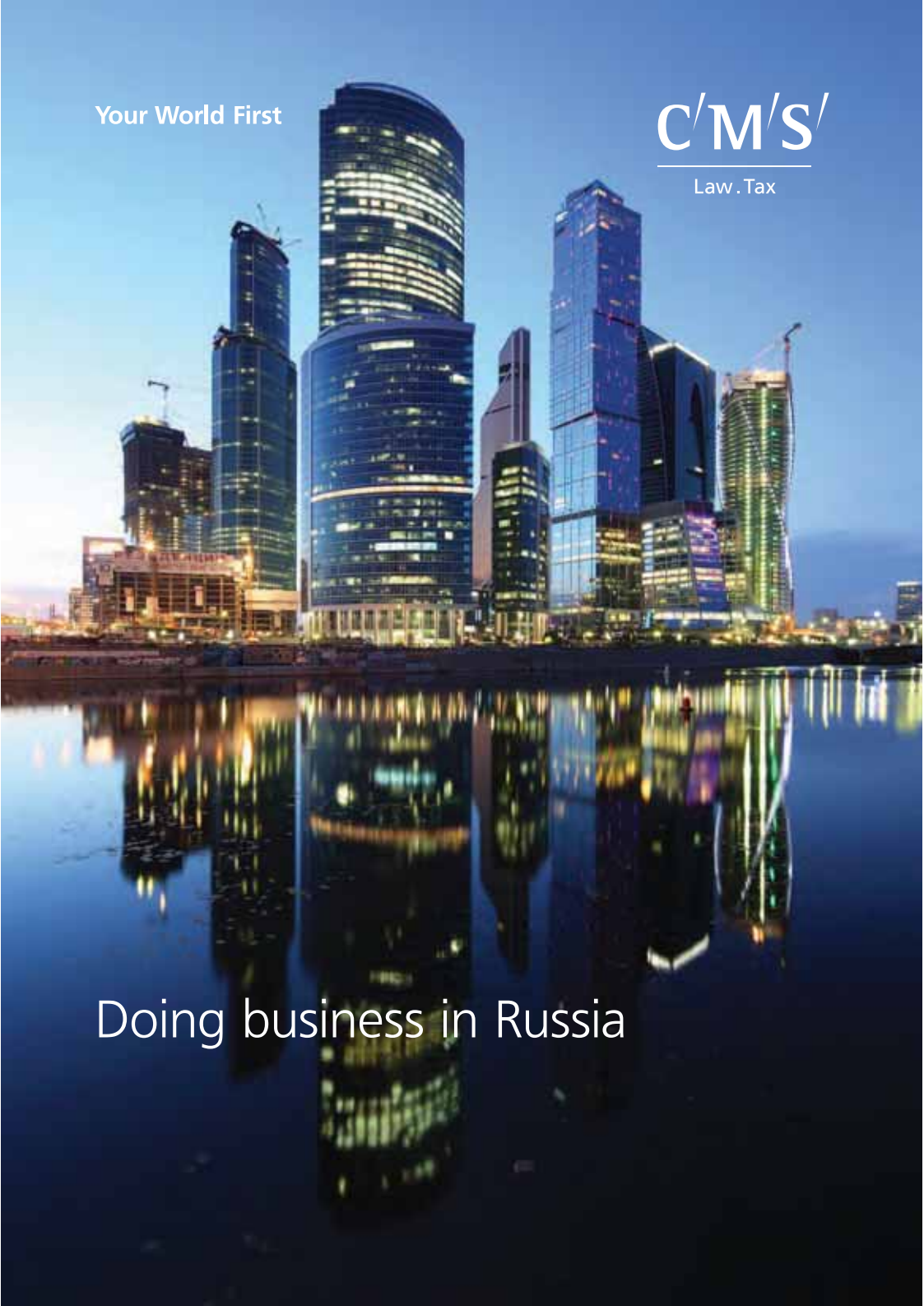
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Doing business in Russia

Dear reader,
CMS is at the forefront of providing clients with specialist, business-focused advice in law and tax matters. With 3,000 legal professionals in 58 offices around the world, who are trained in project management and work in sector-based teams, our key focus is on our clients and fulfilling their objectives.

In a competitive legal market, we stand apart through our deep commitment to understanding our clients' business and our insider knowledge of the countries in which we operate.

From major multinationals and mid-caps to start-ups, we at CMS, Russia have now been welcoming investors to Russia for over 20 years. Our history and expertise in the local market allow us to provide our clients with efficient, business-oriented and strategic advice.

As part of our commitment to clients, our professionals have put together this introductory guide to the Russian legal system and the principal laws and regulations that are of interest to investors in this challenging but opportunity-full market. It is of course no substitute for the expert advice tailored to your project that we will be pleased to provide to you on request.

Russian legislation is changing rapidly and, although this guide describes the laws as of 5 May 2014, please contact us to check that it remains up-to-date. We would also recommend that you subscribe to our free CMS, Russia news service through which you will receive our legal and tax alerts, invitations to our events and other news. You can do this by getting in touch with any of the CMS, Russia key contacts listed at the end of this guide or our Marketing Department (cmsmoscow-marketing@cmslegal.ru).

We wish you every success.

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The President

Under the Constitution of the Russian Federation, originally adopted on 12 December 1993 and from time to time amended (the "**Constitution**"), the President is the Head of State. Commencing with the current presidency, the term of office of the President is six years (previously it was four). The President may only serve two consecutive terms.

The President appoints the Prime Minister and the Chairman of the Central Bank of Russia. Both appointments must be endorsed by the lower chamber of the Russian parliament (the State Duma).

The President determines the main trends of Russia's domestic and foreign policy and represents the country in both domestic and foreign affairs. He is Commander-in-Chief of the Russian armed forces.

The President has broad authority to

issue decrees and directives that in practice have the force of law. Under certain circumstances, he has the right to dissolve the State Duma. As anticipated, on 4 March 2012, Vladimir Putin was elected to a third term as President. He replaced Dmitry Medvedev, who had served one term in office.

The federal Government

The Government of the Russian Federation ("*Pravitelstvo*") exercises executive power at the federal level, with the Prime Minister acting as its head. The Government is required to enact the decisions made by the President and the laws adopted by the federal legislature.

The federal legislature

The Federal Assembly ("*Federalnoye Sobraniye*")(the "**Parliament**") consists of two chambers: an upper chamber called the Federation Council ("*Soviet Federatsii*") and a lower chamber called the State Duma ("*Gosudarstvennaya Duma*"). The Parliament exercises legislative power in Russia at the federal level.

There are 170 seats in the upper chamber of Parliament. They are occupied by representatives of the executive and legislative branches of the Russian regions.

The State Duma is the lower chamber of Parliament and consists of 450 deputies who are elected by proportional representation. State Duma members were previously elected for four-year terms. However, since the December 2011 election, their term of office has been extended to five years.

Federal bills may originate in either the upper or the lower chamber of Parliament. Alternatively, they may be submitted by the President, the federal Government, regional legislatures, the Constitutional Court and the Supreme Court. Bills are first considered by the State Duma and must pass three readings. After being adopted by a majority in the State Duma, bills are considered by the Federation Council. If a bill is rejected by the Federation Council, a Conciliatory Commission may be established. This consists of representatives of the State Duma and Federation Council who review and amend the bill before it is presented to the State Duma again for consideration.

Once a bill is adopted by the Federation Council, it must be signed by the President. The President has the right of final veto which, if exercised, can only be overridden by a resolution passed by two-thirds of the members of the State Duma and the Federation Council.

The judiciary

The judiciary is split into three branches:

— the courts of general jurisdiction;
— the commercial ("*arbitrazh*") courts;
— the Constitutional Court.

There is a federal system of courts and a system of local courts in each Russian region.

The **courts of general jurisdiction** deal with criminal, civil and administrative cases involving individuals who are not engaged in business activities. Cases are heard by the district court unless they fall

within the jurisdiction of the magistrates courts or martial courts. The senior court of general jurisdiction is the **Supreme Court** of Russia (the "**Supreme Court**"). Decisions of the lower courts can be appealed through the intermediate courts, as far as the Supreme Court.

The **commercial ("*arbitrazh*") courts** deal with economic disputes involving individuals engaged in business activities and disputes between legal entities and their participants (i.e. their shareholders). The commercial court system initially consisted (in an increasing order of hierarchy) of the regional commercial courts, the commercial courts of appeal, the federal district commercial courts and the **Supreme Commercial Court** of Russia (the "**SCC**").

On 5 February 2014, the President signed a bill that abolishes the SCC as an independent judicial institution and the highest commercial court in Russia. As a result, the **Supreme Court** will become the highest judicial authority in civil matters, economic disputes (the initial jurisdiction of the SCC), criminal, administrative and other matters after the transition period expires on 7 August 2014.

The Intellectual Property Court, which was created on paper at the end of 2011 as part of the commercial court system, started operating in July 2013 (please see the *IP Court* section on page 155).

The **Constitutional Court** has jurisdiction to decide on the constitutionality of federal and regional legislation and regulations. This court also resolves jurisdictional disputes between the federal and regional authorities and is able to interpret and provide guidance on the provisions of the Constitution.

Regional and local political structure

In accordance with the Constitution (in its version of 5 February 2014), the Russian Federation consists of 85 'constituent subjects', i.e. regions within the federation. Regions are granted with a certain degree of autonomy over their internal economic and political affairs. As cities of federal significance, Moscow, Saint Petersburg and Sevastopol enjoy the status of region.

Since 1 June 2012 the head of the executive branch of each region is directly elected in regional elections. Regional governors were previously appointed by the legislative body of their respective region on the recommendation of the President of Russia.

The Constitution sets out a general list of powers that are of exclusive federal jurisdiction. Some powers are jointly exercisable by the federal and regional authorities. The regional authorities are then allocated all residual powers. Regional powers include the authority to manage municipal property, establish regional budgets, collect regional taxes and to maintain law and order. The Constitution also gives regional bodies the authority to pass laws, provided those laws do not contradict the Constitution or existing federal laws.

At the lowest level of the political system, local government was restruc-

tured as part of a major reform that started in 2004. This resulted in the creation of an intricate two-tier local government system where municipalities are subdivided into city districts on the one hand and municipal districts on the other, with municipal districts being further subdivided into urban and rural settlements. Municipalities have their own budgets and depending on how much authority the regional government has delegated to them, they may enjoy certain limited taxation powers. They are also involved in the management of municipal land (they can act as landlords in lease agreements, allocate land plots for construction and act as seller during the privatisation of public land).

Legal environment

General background

Russia has a system of civil law. The legal structure developed at a rapid pace during the 1990s. During this period significant reforms were enacted in almost every area of law as the country moved away from its Soviet command economy. The Russian Civil Code (the "**Civil Code**") sets out the foundation of civil law and civil relations, including business relations.

2013 marked a turning point in the on-going Civil Code reform process with:

— the phased entry into force of four sets of amendments: (i) mainly affecting real estate; (ii) relating to transactions, resolutions of general meetings, powers of attorney and limitation periods; (iii) dealing in particular with securities circulation, as well as the protection of honour, dignity and business reputation; and (iv) introducing new conflict of laws rules;
— the enactment of the fifth set of amendments, which mainly amends provisions on pledges; and
— two bills passing their first (bill No. 47538-6/2 on corporate law) and second readings (bill No. 47538-6/7 on intellectual property) in the State Duma.

The momentum carried into 2014 as the sixth (intellectual property) and seventh (corporate) sets of amendments were enacted in March and May respectively, to come into force for the most part in October or September 2014.

There remains, however, many gaps and ambiguities in both the current and the newly adopted legislation.

The Constitution, federal laws and regional laws form the foundation of the Russian legal system. Presidential Decrees, Orders of the Russian Government and the decisions of various ministries are used to support and interpret the provisions of primary legislation.

The Constitution states that general principles of international law and international treaties are part of the Russian legal system. Consequently, if Russia is a signatory to an international treaty containing provisions contrary to the provisions of any domestic legislation, the provisions of the international treaty will prevail.

WTO

Following 18 years of negotiations, Russia finally joined the World Trade Organisation in summer 2012 (please see the *Customs regulations* chapter on page 63).

At the time, WTO accession sent a positive signal to foreign investors. However, notable changes such as a material drop in tariffs on imported goods and changes to the quotas for foreign participation in the insurance sector have not yet come into effect because of the long grace periods that are allowed. For example, under WTO rules, foreign insurance companies will be able to open branch offices in Russia, but this is not required to take effect until nine years after accession.

Foreign investment

Legal regulation

The main legislative act governing foreign investments is Federal Law No. 160-FZ "On Foreign Investment in the Russian Federation" dated 9 July 1999 (the "**Foreign Investment Law**"). This law states that foreign investors and investments will be treated no less favourably than domestic investors and investments, subject to certain wide-ranging exceptions.

Exceptions/restrictions may be introduced, amongst others, to protect the Russian constitutional system; the morality, health and rights of third parties; or in order to ensure state security and/or defence. Some of the sectors concerned are commented on separately below. By and large, foreign investment is permitted in most sectors of the Russian economy, including investment in portfolios of government securities, stocks and bonds, direct investment in new businesses, in the acquisition of existing Russian-owned companies and in joint ventures.

Foreign investors are protected against nationalisation or expropriation, unless this is provided for by federal law. In these cases, foreign investors are entitled to receive compensation for their investment and other losses.

Exclusions/restrictions

In addition to the so-called 'strategic industries law' (please see the *Common forms of business structures for foreign investors* chapter on page 32), restrictions on foreign investment exist notably in the insurance and banking sectors.

Federal Law No. 4015-1 "On Insurance" dated 27 November 1992 currently prohibits foreign investors from owning more than 25% of the total market for domestic insurance. Insurance companies in which foreign shareholders own more than 49% of the charter capital may not engage in certain types of insurance business, including, for example, life assurance.

In the banking sector, the Central Bank of Russia has the right to use reciprocity as a criterion to specify the types of business that subsidiaries or branches of foreign banks may be licensed to operate in Russia. In practice, however, branches of foreign banks are not able to carry out any banking activities on the Russian market. Additionally, a ceiling on

the total amount of foreign bank capital, as a percentage of the total bank capital in Russia, can be imposed by federal law, but no such limit applies at the time of writing. Under WTO rules, any such ceiling may not be less than 50%.

Lobbying

Given how slowly the legal culture has developed in Russia, businesses tend not to expend their lobbying efforts on attempting to influence the drafting of new laws or the actions of those drafting them. Instead, businesses tend to seek *de facto* special treatment, such as tax deferments, customs benefits, operation licences and the right to engage in certain kinds of activity. In doing so, however it may be that these companies expose themselves unduly to 'political risk' upon any change of administration and companies entering the market need to consider how secure such concessions might be for their business in the long term.

There are not many legally recognised lobbying associations with a large membership base. Prominent examples of associations that do exist are the Association of Russian Banks, the Chamber of Commerce and Industry, the Federation of Independent Trade Unions of Russia and the Russian Gas Association.

Common forms of business structures for foreign investors

General approach

Russian legislation provides for several types of business structure, of which the most commonly used are limited liability companies, joint-stock companies, representative offices and branches, as well as limited and unlimited partnerships. A basic description of each of these is set out in Part I of the Civil Code of 1994 (the "**Civil Code**"). Some other specialised structures also exist but are not commonly used by foreign investors.

An individual is also entitled to conduct commercial activities in Russia, provided that he/she has the legal status of an individual entrepreneur. Foreign nationals can only register as individual entrepreneurs when they hold a temporary or permanent residence permit. The legal framework for individual entrepreneurs is also set out in the Civil Code.

With recent amendments to Civil Code, Russian legal entities and corporate institutions are to undergo major transformations, striving for conformity with their continental peers. This overview describes the new regime that comes into force on a series of dates during 2014 and on 1 January 2015. We expect that further amendments will follow in 2015 to ensure all corporate regulations are in compliance with the new rules provided in the Civil Code.

Main types of structure

Russian legal entities

The new classification divides all Russian legal entities into unitary entities (no 'shareholding' provided to the founder(s)) and corporations. Corporations, in turn, can be public or private. Private corporations will provide more flexibility to their members in corporate governance issues and will be subject to more limited disclosure obligations. Conversely, public corporations will have to disclose more information about their activities and the management structure of public corporations will be regulated by mandatory rules to a greater extent.

According to the new classification, joint-stock companies will be classified as corporations that can be either public or private and limited liability companies will be classified as private corporations. Thus, the present classification of joint-stock companies as open and closed will no longer apply.

We expect that foreign investors in Russia will mostly use the limited liability company and the private joint-stock company forms for their activity in Russia.

Other special forms of legal entity exist, such as the economic partnership which is designed primarily for the holding in common of IP rights (but of little application beyond that).

In addition to the new classification rules, Russian corporate law has significantly developed in other ways to create a more usable infrastructure for foreign investments. In particular, foreign law can now govern a shareholders agreement with foreign participation, a shareholders agreement prevails for the parties in case of discrepancies with the charter, the corporate governance of a joint venture can now be more flexibly customised by the parties according to their business requirements, etc.

All these changes presumably aim to increase the attractiveness of Russian legal entities for direct investment and push through the government driven concept to promote the 'de-offshorisation' of the Russian economy.

Limited liability company

A limited liability company ("*obshchestvo s ogranichennoy otvetstvennostyu*" – an "**LLC**") is designated by the abbreviation "OOO" or "LLC" before or after its name. It is one of the simplest forms of Russian legal entity and is often used by foreign investors for a wholly owned subsidiary.

Russian legislation prevents an LLC being wholly owned by another company

("*khozyaystvennoye obshchestvo*"), where that holding company is itself wholly owned by (i) another single legal entity or (ii) a single individual.

The establishment, reorganisation and liquidation of an LLC is mainly governed by the Civil Code, Federal Law No. 14-FZ "On Limited Liability Companies" dated 8 February 1998 (the "**LLC Law**") and Federal Law No. 129-FZ "On State Registration of Legal Entities and Individual Entrepreneurs" dated 8 August 2001 (the "**Registration Law**"). At the time of writing, the LLC Law and Registration Law have not been amended yet to reflect recent amendments to the Civil Code.

Charter capital and contributions

The **charter capital** of an LLC is divided into participatory interests ("*doli*"). Unlike the shares issued by a joint-stock company, these participatory interests are not classified as securities and therefore do not need to be registered with the Central Bank of Russia (the "**CBR**")[1].

Each holder of a participatory interest is referred to as a 'participant'.

The minimum charter capital of an LLC is currently RUB 10,000 (EUR 213[2]). The amount of the monetary fund for the charter capital must not be less than amount of the minimum charter capital.

Contributions to the charter capital of an LLC may be made in cash or in kind (i.e. securities, property or other tangible or intangible rights or assets having a monetary value, etc.). All contributions in kind must be valued by an independent valuer.

A participant may not be released from the obligation to pay its agreed contributions to the charter capital. In case of a charter capital increase, contributions to the charter capital can be made by set off against any existing monetary debt that the company owes to the participant, provided that all the participants agree.

Exemptions from import duties and import VAT may be available for certain types of equipment contributed to the charter capital of a company by a foreign participant.

Net asset requirements and creditor protection

An LLC must ensure that the value of its net assets does not fall below the amount of its charter capital. Failure to comply with this requirement may result in the company being required to decrease its charter capital accordingly or to increase the value of its net assets by one of the available ways.

Also, if the value of the company's assets is less than the minimum charter capital amount, it may be subject to compulsory liquidation.

LLCs are required to file information on their net asset value with the Unified Federal Register of Activities of Legal Entities (the "**Activities Register**"). This

[1] Starting from 1 September 2013, the CBR performs the function of the securities market regulator and registers the shares issued by joint-stock companies. The Federal Service for Financial Markets that used to bear this responsibility has been liquidated.

[2] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience throughout this guide.

requirement aims to increase the transparency of the financial state of the company and protect its creditors.

Participation

If the number of participants in the company exceeds 50, the company is obliged either to reduce the number of participants or to re-register as a joint-stock company within one year. Failure to do so may lead to compulsory liquidation.

All LLCs must maintain a register of participants. This register sets out the names of the participants and the number of participatory interests that each participant has in the company.

As a general principle, the participants' liability for the company's debts is limited to the payment (in full) of the amount of their participatory interests. In a limited number of cases, the corporate veil can be pierced resulting in participants having unlimited liability for the obligations of the company. This can happen if, for example, a participant gives binding instructions to the company that lead to the insolvency of the company.

Management structure

The managing bodies of an LLC are:

— the general participants meeting;
— the collective management body – board of directors (optional);
— the collective executive body – management board (optional); and
— the sole executive body (one or several executives) – general director.

Major decisions such as amending the company's charter, changing the charter capital, distributing profits and approving the annual reports and balance sheets of the company must be taken by the **general participants meeting**.

The annual general participants meeting must be held not earlier than two months and not later than four months after the end of the company's financial year (which always corresponds to the calendar year). Extraordinary general participants meetings may be held at any time. General participants meetings must be convened according to the procedure set out in the company's charter and the LLC Law.

Unless otherwise expressly provided for by the company's charter, participants number of votes at the general participants meeting will normally correspond to the proportion of the company's charter capital that such participant holds.

Generally, decisions are adopted by a simple majority of votes of all participants except for those matters in respect of which the LLC Law requires a qualified majority (e.g. liquidation of the company). In addition, a qualified majority can be set out by the company's charter for other matters at the discretion of the participants.

Most of decisions (except approval of the company's annual reports and balance sheets) may be adopted without holding a participants meeting.

The general participants meeting has exclusive competence in respect of the

list of matters specified by the Civil Code and LLC Law. This list can be extended in the company's charter at the discretion of the participants.

Resolutions of the general participants meeting must be notarised unless otherwise provided for by the charter.

A **board of directors** is an optional supervisory body. Its authority typically includes appointing/dismissing the general director or approving major transactions, interested-party transactions and other transactions.

The LLC can also have a **management board**. By law, the general director chairs the management board. Unlike the general director, however, members of the management board must obtain a power of attorney from the general director in order to enter into transactions on the company's behalf.

Powers of the board of directors and the management board are to be defined by the charter at the discretion of participants.

The **general director** (sole executive body) manages the day-to-day running of the company and deals with all other issues not falling within the authority of the other management bodies. The general director acts on behalf of the company, represents its interests, enters into transactions on its behalf, issues powers of attorney and hires and dismisses employees. The general director represents the company without a power of attorney. The general director's powers may be limited by the company's charter and his/her employment contract.

The powers of the sole executive body can be provided to several executives of the company for individual or joint representation, which must be reflected in the Unified State Register of Legal Entities. This is a major development as it opens up the possibility of pluralising the executive authority in a Russian company. It is not clear at time of writing, how this will be formalised in the legislation but what seems to be envisaged is something close to the German concept of "*Geschäftsführer*".

A foreign national may be appointed as the general director of an LLC subject to compliance with work permit regulations (please see the *Employment/Migration* chapter on page 103).

The general participants meeting may transfer the general director's authority to a management company (in whole only). In such case the management company will act on the basis of the management agreement entered into with the company.

Audit

The charter may provide for an **internal auditor** (either an individual or an internal audit commission established under the company's own charter). In some cases a company must have an internal auditor – as with companies having more than fifteen participants – without which the general participants meeting will not be able to approve the company's annual reports and balance sheets (as they must first be approved by

the internal auditor).

An **external auditor** may also be appointed by the general participants meeting to audit the company's financial and business activity. If certain turnover or asset value thresholds are exceeded, or if the company conducts certain regulated activities, an external auditor must be appointed.

Transfer of participatory interests
Participatory interests are freely transferable between participants. However, the charter may specify that a transfer of participatory interests requires the consent of the other participants and/or the company.

A participant may transfer its participatory interest to third parties, subject to a statutory pre-emption right in favour of the other participants and, if so provided for by the charter, in favour of the company itself.

The procedure for selling participatory interests and for determining their offer price is set out in the LLC Law, although the company's charter and/or participants agreement may provide a different procedure.

A participatory interest transfer agreement must be notarised and the participatory interest is transferred immediately upon notarisation of the agreement. This creates difficulties in the context of Russian agreements for the sale and purchase of participatory interests under which exchange and completion are to occur on different dates and especially where the sale agreement is conditional.

By way of exception, notarisation is not required for the transfer of:

— company-owned participatory interests to current participants or third parties;
— participatory interests to the company; or
— participatory interests from one participant to another as a result of the exercise of pre-emption rights.

Where notarisation is not required, the transfer of title to the participatory interests is effective when the transfer is recorded in the Unified State Register of Legal Entities.

The charter may prohibit the transfer of participatory interests to third parties or make such transfer subject to the consent of other participants or the company. If such consent is not given, the company itself is obliged, by law, to purchase the relevant participatory interests.

Right to withdraw
Participants in an LLC are entitled to withdraw from the company without the consent of other participants if (i) this is permitted by the company's charter or (ii) the transfer of participatory interest to a third party or another participant is prohibited and/or blocked by other participants.

If a participant withdraws from the company, its participatory interest will be transferred to the company on the date when the withdrawal notice is served to the company. The company is then

obliged to pay the exiting participant the 'actual value' of its participatory interest in cash. The company may, however, pay the exiting participant in kind provided that the participant agrees to this.

The 'actual value' of the exiting participant's participatory interest is calculated in accordance with accounting data as provided in the LLC Law. The statutory payment procedure and timing may be varied in the company's charter.

Expulsion of a participant
Participants owning at least 10% of the company's charter capital may bring court proceedings to expel any participant that grossly violates its obligations or prevents or materially impedes the company's activities.

Joint-stock companies

Joint-stock companies belong to corporations as well and are regulated by the Civil Code (as amended), Federal Law No. 208-FZ "On Joint-stock Companies" dated 26 December 1995 (the "**JSC Law**"), the Registration Law and Federal Law No. 39-FZ "On Securities Market" dated 22 April 1996 (the "**Securities Market Law**").

A joint-stock company ("*aktsionernoye obshestvo*" – a "**JSC**") can either be public or private (non-public). Public JSCs are capable of offering their shares by public offering and must contain *public* in their company name.

Private JSCs, on the other hand, enjoy more flexibility:

— the powers can be distributed between corporate bodies in various ways (e.g. management bodies can take over most questions of the general shareholders meeting);
— the management bodies themselves can be omitted (e.g. the board of directors can act both as a management and supervisory body, a single director may replace the management board); and
— shareholders may define shareholders' rights in the charter non-proportionally to their stakes in the company, limit the number of shares or votes held by one shareholder, provide for a pre-emptive right or consent on transferring shares to a third party.

As with LLCs, Russian legislation prevents a JSC being wholly owned by another company ("*khozyaystvennoye obshchestvo*"), where the holding company is itself wholly owned by (i) another single legal entity or (ii) a single individual.

Charter capital and contributions
The **charter capital** of a JSC is divided into shares (which may be split into ordinary shares and preference shares). These shares are deemed to be securities for the purposes of Russian securities legislation and must therefore be registered with the CBR.

The minimum charter capital for a JSC is currently RUB 100,000 (EUR 2,128).

As with LLCs, **contributions** to the charter capital may be paid in cash or in kind. Other types of securities, such as corporate bonds, must be paid in cash only. Contributions in kind must be valued by an independent valuer. It is

possible to pay for new shares issued in a closed subscription by way of a debt-for-equity swap.

The charter capital may be increased by issuing shares or increasing the nominal value of the shares already in issue. Each capital increase must be filed and registered with the CBR, which is a lengthy process.

As a general principle, the liability of the shareholders for the company's debts is limited to the payment (in full) of their shares. In a limited number of cases however, the corporate veil can be pierced, resulting in the shareholders having unlimited liability for the obligations of the company. This can happen if, for example, a shareholder gives binding instructions to the company that lead to the insolvency of the company.

Net asset requirements and creditor protection

A JSC must ensure that the value of its net assets does not fall below the amount of its charter capital. Failure to comply with this requirement may result in the company being required to decrease its charter capital accordingly or to increase the value of its net assets by one of the available ways.

Also, if the value of the company's assets is less than the minimum charter capital amount, it may be compulsorily liquidated.

JSCs must disclose information on the value of their net assets in the Activities Register in addition to other filing requirements.

At least 5% of the charter capital of any JSC must be allocated to a reserve fund. This fund is created specifically to cover losses and to redeem bonds and shares of the company.

Management structure

The managing bodies of a JSC are:

— the general shareholders meeting;
— the collective management body (optional for private JSCs) – board of directors, supervisory board;
— the collective executive body (optional for private JSCs) – management board; and
— the sole executive body (one or several executives) – general director.

The annual **general shareholders meeting** must be held not earlier than two months and not later than six months after the end of the company's financial year (which always corresponds to the calendar year). Extraordinary general shareholders meetings may be called by the general director, the board of directors, the external auditor, the internal auditor of the company or by shareholders owning at least 10% of the voting shares in the company.

At general shareholders meetings most decisions may be passed by a simple majority of the shareholders attending the meeting (e.g. a decision to appoint executives of the company). However, a limited number of more significant decisions require not less than 75% of the votes of the shareholders attending the meeting (e.g. decisions on the liquidation or reorganisation of the company, amendments to the charter or

approval of a new version of the charter). Each share entitles the holder to one vote.

Subject to certain exceptions, shareholders may adopt decisions without holding a meeting. In the case of public JSCs, decisions must be certified by the company's registrar. A private JSC may also use a notary for certifying its decisions.

The **collective management body** (e.g. board of directors, supervisory board) is responsible for the general management of the company but may not interfere with the exclusive competence of the general shareholders meeting.

Members of the collective management body are elected by an annual/extraordinary general shareholders meeting and serve until the next annual general shareholders meeting. There is no limit on the number of times that a member of the collective management body may be re-elected.

The **collective executive body** (e.g. management board) consisting of at least five members is a mandatory body for a public joint-stock company. Unlike the executives, members of the collective executive body must obtain a power of attorney in order to conclude transactions on the company's behalf.

The **sole executive body** can consist of a single person or several persons. In the case of several persons constituting the sole executive body, they may be authorised to act individually or jointly and this must be disclosed in the Unified State Register of Legal Entities. The sole executive body is responsible for the day-to-day running of the company and can represent the company without a power of attorney. Executives constituting the sole executive body are appointed and dismissed by the shareholders, unless the company's charter stipulates that this decision falls within the authority of the collective management body (e.g. board of directors, supervisory board). If the latter is the case, there is a legal procedure in order to avoid deadlocks relating to the appointment or dismissal of executives when, for any reason, the collective management body fails to agree on this matter.

Legal entities may be appointed as the sole executive body.

A foreign national may be appointed as the general director of a JSC subject to compliance with work permit regulations (please see the *Employment/Migration* chapter on page 103).

Audit

JSCs are required to appoint an **external auditor** to audit the annual accounts. The **revision committee** (unless specifically excluded) audits the company's financial and business activity. Before the annual general shareholders meeting, the revision committee prepares an annual report and balance sheet. The report is then communicated to all the shareholders that are entitled to attend the meeting.

Furthermore, the revision committee may audit the company at any time:

— at its own initiative;
— upon a decision of the general shareholders meeting; or
— upon demand of a shareholder or a group of shareholders holding at least 10% of the voting rights in the company.

Issue and transfer of shares

The shares of a JSC, whether public or private, are treated as securities and as such are subject to the registration requirements of the Securities Market Law. When issuing new shares, all JSCs must carry out the requisite filings with the CBR[3]. The documents that must be filed include the decision to issue shares, the report on the results of the share issue and other documents as well as, in certain cases, a prospectus for the share issue.

A share transfer takes effect when it is recorded in the register of shareholders that all JSCs are required to maintain. The register of shareholders must be kept by an independent company duly licensed by the CBR with no exceptions.

A **public JSC** may make both closed and public offerings of its shares. There are no statutory pre-emption rights or restrictions on the transferability of shares in the company whether to other shareholders or third parties. When the charter capital is increased by issuing additional shares, however, existing shareholders do have the benefit of statutory pre-emption rights.

Shares of a **private JSC** are freely transferable between shareholders, although it is possible to introduce contractual restrictions by means of a shareholders agreement. Share sales to third parties are subject to statutory pre-emption rights of the other shareholders in the company (and the company itself if so provided in the charter). The statutory procedure and terms for exercising the pre-emption rights is mandatory and therefore may not be varied in the company's charter.

Redemption of shares

In certain cases where a shareholder disagrees with decisions taken at a general shareholders meeting, it may be able to require the company to purchase its shares. This applies when:

— a decision has been taken to reorganise the company;
— a decision has been taken to adopt charter amendments or to adopt a revised charter limiting the rights of the shareholder in question; or
— a major transaction has been approved.

The shares will be redeemed at a price no less than the market value of the shares as determined by an independent valuer in accordance with the methods prescribed in the JSC Law.

Expelling a shareholder

A shareholder of a **private JSC** may expel another shareholder through court action for causing harm to the company or impeding its activity.

[3] Starting from 1 September 2013, the CBR performs the function of the securities market regulator and registers the shares issued by JSCs. The Federal Service for Financial Markets that used to bear this responsibility has been liquidated.

In case of a **public JSC** a shareholder that has acquired more than 95% of the voting shares in accordance with a special procedure may 'squeeze out' the minority shareholders.

Economic partnership

The economic partnership ("*khozyaystvennoye partniorstvo*") is designed for the new technology sector and is meant to provide more flexibility for its participants than the existing LLC and JSC forms.

In general terms, an economic partnership shares many common features with a Russian LLC but with the advantage that the rights and obligations of participants, the management of the company and profit distribution are regulated by a much more flexible and less regulated notarised management agreement.

The law therefore affords much more flexibility to economic partnerships than is the case with the LLC or JSC company form. However, the prohibition on an economic partnership acquiring or holding shares/interests in other companies and partnerships and on advertising its business, generally preclude the use of this business structure for commercial trading operations or as holding companies for joint ventures.

Summary of legal forms

For ease of comparison between the legal entities described above, please refer to the comparative table on pages 22-24.

Other business structures

Although foreign individuals and legal entities can set up wholly owned subsidiary companies and may participate in the various forms of partnership prescribed under Russian law, using a representative office or a branch remain effective ways for a foreign legal entity to enter into the Russian market. An investment partnership is also a relatively new form of unincorporated legal structure which may be relevant to investment funds.

Representative office

Status

A representative office ("*predstavitelstvo*") is not a separate legal entity but, rather, is an office set up to represent the interests of the parent company. This does not prevent it, in practice, from conducting business in Russia (and many representative offices do so) and being treated by the tax authorities as a separate profit centre from the parent company. However, as a matter of civil law, a representative office's lack of separate legal identity limits the types of business activities it may undertake. For example, a representative office may not formally import goods for purposes other than its own needs, nor may it register title to immovable property in its own name. A representative office may also experience difficulties in obtaining licences and permits to conduct certain types of business.

A representative office may, however, carry out representative functions on behalf of the parent company, including arranging marketing and advertising in

COMPARATIVE TABLE

	Public joint-stock company ("Public JSC")	Private joint-stock company ("Private JSC")	Limited liability company ("LLC")	Economic partnership
1	2	3	4	5
Activities	Any type of activity (subject to licensing requirements)			Any type of activity (subject to licensing requirements) except for incorporating other legal entities, issuing bonds and other emissive securities, advertising
Term	Unlimited term, unless otherwise provided in charter			
Number of shareholders/ participants	Unlimited	1 to 50[4]	1 to 50	2 to 50
Minimum charter capital	RUB 100,000 (EUR 2,128)		RUB 10,000 (EUR 213)	None
Type of interest in charter capital	— Ordinary shares — Preference shares		Participatory interests	
Issue of financial instruments	— Bonds — Other emissive securities			Prohibited
Subscription for shares	— Public subscription — Closed subscription	Closed subscription only	N/A	
Contributions to the charter capital	— Monetary funds — Contributions in kind			— Monetary funds — Contributions in kind, except securities other than certain bonds
Payment of the charter capital	— 3/4 prior to the state registration of the company — The remaining 1/4 within one year of the state registration of the company		The whole charter capital within four months of the state registration of the company	Subject to the management agreement
Capital increase	Only after the charter capital has been fully paid up			Subject to the management agreement
Capital decrease	— After notification of creditors and repayment of debts — Mandatory decrease in certain cases			

[4] We expect this requirement to be lifted and the number of shareholders in a private JSC no longer to be limited once the JSC Law is brought in conformity with the recent Civil Code amendments.

1	2	3	4	5
Managing bodies	— General shareholders meeting — Collective management body — Collective executive body — Sole executive body	— General shareholders/participants meeting — Collective management body (optional) — Collective executive body (optional) — Sole executive body		— Director — The management structure is subject to the management agreement, e.g. any other managing bodies (board of directors, management board) are optional and subject to the management agreement
Transfer of shares/ participatory interests between shareholders/ participants	No restrictions	No restrictions, unless otherwise provided for in a shareholders agreement	Without restrictions, unless the charter provides for participants'/ company's consent or unless provided for in a participants agreement	Without restrictions, unless otherwise provided for by the management agreement
Transfer of shares/ participatory interests to third parties	No restrictions	— Subject to shareholders' pre-emption right — Can be subject to company's pre-emption right under the charter	— Subject to participants' pre-emption right — Can be subject to company's pre-emption right under the charter — Can be restricted by the charter — Can be subject to participants'/ company's consent — Subject to mandatory notarisation	Subject to all participants' consent and participants' pre-emption right
Exiting the company / partnership (redemption/ withdrawal)	Shareholders may require the company to redeem their shares in limited cases: when they do not agree with certain decisions, including the reorganisation of the company, charter amendments which limit their rights, and the conclusion of major transactions		A participant may withdraw from the company if (i) permitted by the company's charter or (ii) the transfer of participatory interest to a third party or	Subject to the management agreement

1	2	3	4	5
			another participant is prohibited and/or blocked by other participants	
Expulsion of a shareholder/ participant	Squeeze out procedure by a shareholder who has acquired more than 95% of the voting shares	Shareholders may be expelled from the company through court action initiated by another share-holder	Participants owning at least 10% of the company's charter capital may bring a court action to expel any participant which grossly violates its obligations, or prevents or materially impedes the company's activities	— Participants may bring a court action to expel any participant which grossly violates its obligations, or prevents or materially impedes the partnership's activities, or — Without bringing a court action if a participant fails to pay its interest
Liability of the company/ partnership	The company/partnership is not liable for the obligations of the shareholders/ participants			
Liability of shareholders/ participants	Liability is limited to the value of their shares/participatory interests (unless it can be demonstrated that their binding instructions to the company/partnership led to its insolvency)			

Russia, negotiating the terms and conditions of agreements on behalf of the parent company and facilitating the conclusion of agreements by the parent company. It may also assist in other commercial and legal transactions between the parent and Russian organisations, including the rental of property.

At one time, an accredited representative office enjoyed a range of benefits that were not available to branches or companies. These benefits have been gradually withdrawn, although foreign employees of a representative office may still obtain personal accreditation. This involves certain practical benefits for the accredited foreign employee, such as the right to import and export personal effects free of customs duty and VAT, and it assists with obtaining multi-entry visas although employees of a representative office are currently excluded from the 'highly qualified specialist' simplified visa regime (please see the *Employment/Migration* chapter on page 105). From 1 January 2015, they will become eligible for this regime. There has been considerable debate about whether accredited employees of a representative office do actually require work permits, but, in practice, having a work permit will avoid any unwanted difficulties with Russian federal and local migration authorities.

A representative office may hold a number of different types of bank account, including foreign currency and rouble

Table showing main differences between a representative office and a branch (at the time of writing)

Business structure	Representative office	Branch
Formation	Two-step accreditation procedure (accreditation with the accrediting body followed by registration in the register held by the State Registration Chamber of the Russian Ministry of Justice (the "**SRC**"), unless the latter is the accrediting body)	Single-step accreditation procedure with the SRC
Capacity	Technically restricted to representation, but functions in practice are often wider. Unable to hold title to property, or to import or export goods. May be unable to obtain certain permits	Wider capacity. Usually able to obtain requisite licences and permits
Taxation	Capable of constituting a permanent establishment for Russian tax purposes and is subject to Russian taxation accordingly	Will constitute a permanent establishment for Russian tax purposes and is subject to Russian taxation accordingly
Foreign staff	Does not benefit from the highly qualified specialist regime (please see the *Employment/Migration* chapter on page 103)	May benefit from the highly qualified specialist regime
Maximum accreditation or renewal term	3 years	5 years

accounts. These accounts enable the representative office to make payments in Russia to both residents and non-residents subject to certain currency control restrictions established by CBR regulations and other applicable legislation.

As a representative office is merely an extension of a foreign parent company, the latter remains responsible for the liabilities of the representative office.

Management

A representative office acts on the basis of regulations approved by the parent company and is managed by the head of the office who is authorised to conduct the business of the office and to represent the foreign company under a power of attorney. A representative office should also have a chief accountant.

There is no requirement for either the head of the office or the chief accountant to be Russian nationals although an accountant who understands the intricacies of Russian tax and accounting law is a practical necessity.

Branch

Status

A branch ("*filial*") is also an office set up to represent the interests of the parent company. In addition to carrying out the functions of a representative office a branch may formally carry out profit-

making activities.

As a branch is merely an extension of a foreign parent company, the foreign company remains responsible for the liabilities of the branch.

Foreign employees of a branch should also be personally accredited in the same manner as the employees of a representative office and, in addition, they must hold work permits in order to work in Russia (please see the *Employment/ Migration* chapter on page 103).

Management
Management issues are the same as those concerning representative offices (please see the relevant paragraph above).

Other
The Civil Code also provides for a range of other business structures, including simple partnerships (which are not legal entities) as well as full and limited partnerships. These legal entities are rarely encountered in practice.

Since 1 January 2012, it has been possible to form an **investment partnership** (*"investitsionnoye tovarishchestvo"*), which is not a legal entity but a variation of a simple partnership (for ease of comparison between the two types of partnership, please refer to the comparative table on pages 27-28). This is similar to the concept of limited liability partnerships that exist, for example, under German law (*"Kommanditgesellschaft"*) and English law.

An investment partnership is designed to be the appropriate organisational form for collectively accumulating funds for investment under Russian law. It is intended only for the joint acquisition and sale of shares for investment in unquoted companies and economic partnerships, corporate bonds and futures instruments. An investment partnership acts on the basis of an investment partnership agreement which must be notarised but does not require state registration.

There are also non-commercial organisational forms that may be used for charities, trade associations and other not-for-profit organisations.

Registration, liquidation and reorganisation of business structures

Registration of a Russian legal entity
The Registration Law establishes a single procedure for the registration of legal entities, regardless of their organisational/legal form and the type of business activities they conduct.

Scope of registration
A company is duly registered under Russian law once it has undergone:

- state registration (in the Unified State Register of Legal Entities);
- tax registration; and
- registration with the Federal Service for State Statistics and the social funds (pension and social security (the "**Social Funds**")).

Registration mechanics
The tax authorities are responsible for the state and tax registration of

Table showing main differences between simple and investment partnerships

	Simple partnership	Investment partnership	
1	2	3	
Activities	Any type of commercial and non-commercial activities (subject to licensing requirements)	Joint investment activities: acquisition and sale of shares in unquoted companies, corporate bonds and futures instruments	
Term	Unlimited term, unless provided for in the partnership agreement	The term of the investment partnership agreement must not exceed 15 years	
Number of participants	2 or more	2 to 50	
Type of partnership	Simple partnership	General partnership (managing partners) / limited partnership (non-managing partners)	
Contributions to the shared capital	— Monetary funds — In kind contribution — Professional and other knowledge, skills — Business reputation — Business connections	**For managing partners** — Monetary funds — In kind contribution (except excisable goods) — Professional and other knowledge, skills — Business reputation	**For non-managing partners** Monetary funds
Payment of the shared capital	Provided for in the partnership agreement		
Managing bodies	Any partner, unless stipulated for in the partnership agreement	— Managing partners — Investment committee, if provided for in the investment partnership agreement	
Transfer of rights and obligations	No special requirements	**For managing partners** Not allowed	**For non-managing partners** Allowed in the manner stipulated in the investment partnership agreement
Withdrawal	— **Indefinite-term partnership**: allowed with three months' notice	**For managing partners** Subject to all partners' written consent	**For non-managing partners** Allowed if provided for in the investment partnership agreement
	— **Fixed-term partnership**: subject to other partners' consent with compensation for damages to other partners		

1	2	3	
Expulsion of a partner	N/A	On the basis of a court decision where a partner has breached the investment partnership agreement or any other reason stipulated by the investment partnership agreement	
Responsibility of partners within the entrepreneurial activity	Joint liability over all property	**For managing partners** Joint subsidiary liability over all property	**For non-managing partners** Limited to paid contributions

companies, as well as for forwarding documents to the Federal Service for State Statistics and the Social Funds. The registration procedure has also been impacted by the current reform of Russian corporate law. Therefore, further changes to the registration procedure may be introduced in the coming years.

The time taken for registration is five days from the date of submitting the documents to the registration authorities. In practice, the whole process of company incorporation, including collecting the documents required, opening the current bank account and registering with the Social Funds, takes approximately from one to two months to complete (i.e. for the company to be fully operational). However, delays are possible.

The application to register the company can be (i) filed by the founder(s) in person[4] or (ii) submitted by a representative acting on the basis of the power of attorney given by the founder(s) or (iii) sent by post which adds significant time to the registration process or (iv) presented in electronic form via the Federal Tax Service website (http://www.nalog.ru) or the unified portal of the government and municipal services (http://www.gosuslugi.ru). Specifically, the electronic filing form stipulates that the documents should contain an applicant's electronic signature or that an applicant be allowed to have a notary verify his/her signature by electronic signature. However, in practice foreign entities and individuals cannot receive an electronic signature due to the Russian security requirements and, in such case, documents must be submitted in paper form.

Before documents are submitted for state registration, the new company must identify its future premises (as the address must be specified in the documents to be filed for state registration). It should have a lease agreement entered into by (one of) the founders or a letter from the premises owner guaranteeing that, upon registration, the premises will be leased to the company.

The registration application must be notarised and, if signed abroad, legalised. Foreign documents must also be accompanied by a certified Russian translation. The most practical approach is to execute the company charter and

[4] When a company or companies incorporate a Russian legal entity the applicant must be the CEO of the founding parent company(ies).

the supporting documents in Russia on the basis of a power of attorney (except for the application which must be signed in person by the CEO or the founder as stated above).

The new requirements of Russian corporate law state that the corporate resolutions of legal entities must be duly certified by a notary or a professional registrar (depending on a form of the legal entity). Although this requirement seems not to cover foundation resolutions, certification of the foundation resolutions by a notary would help to avoid practical difficulties until Russian law or practice sets out this exception explicitly.

Payment of charter capital

The whole charter capital of an LLC must be paid within four months of its state registration.

At least 3/4 of the charter capital of a JSC must be paid prior and the remaining 1/4 within one year of the state registration.

If a founder fails to pay the total amount of its shares/participatory interests within these time limits, then the non-paid shares/participatory interests become the property of the company.

Registration of the initial share issue

As shares in JSCs are treated as securities, there are certain additional registration requirements imposed by the CBR.

The share issue registration process consists of the following stages:

- passing a decision to issue shares;
- state registration of the share issue;
- subscription for shares; and
- state registration of the report on the issue of the shares.

Anti-monopoly control

As a general rule, the formation of a company is not subject to merger control.

In exceptional cases, however, the prior consent of the Federal Anti-monopoly Service (the "**FAS**") will be required when a company is incorporated by:

- the contribution of assets or shares/participatory interests or rights in another company; or
- the merger of one company with another or consolidation of several companies,

provided that, in either case, certain asset values or revenue thresholds are exceeded (please see the *Anti-monopoly issues* chapter on page 40).

Market regulator pre-registration clearance

If the company to be set up in Russia is a bank or non-banking credit organisation with foreign investment, then the parent company/ies will require the prior clearance of the CBR.

Licensing

Once a company has been set up, it may need to obtain the requisite licence(s) or other authorisations before it can legally conduct certain kinds of business. Failing this, it may be subject to sanctions, and the contracts it will have concluded in relation to any licensed activity may be

subsequently set aside by the courts as potentially voidable.

Accreditation and registration of a representative office and a branch

The procedure for opening accredited representative offices and branches of foreign legal entities in Russia has been significantly impacted by the current reform of Russian corporate law. In particular, Federal Law No. 106-FZ "On Amendments to Certain Legislative Acts of the Russian Federation" dated 5 May 2014 introduced material amendments to the accreditation procedure, which will come into force on 1 January 2015.

The function of accrediting representative offices and branches of foreign legal entities will be transferred from the State Registration Chamber and the Chamber of Commerce and Industry to an authorised federal executive authority (except for the representative offices and branches of foreign civil aviation companies and credit organisations that will be accredited by Rosaviation and the CBR respectively).

This authority has not been yet identified and the relevant information is expected from the Government of the Russian Federation in the near future. We expect this could be the Federal Tax Service, which is currently responsible for the registration of Russian legal entities.

Presumably, the transfer of the accreditation authority to a different state body will result in further significant changes to the registration procedure that will follow shortly.

As a result of accreditation, the representative office/branch will be included in the State Register of Accredited Representative Offices/Branches of Foreign Legal Entities. Information from the State Register of Accredited Representative Offices and Branches of Foreign Legal Entities will be also publicly available on the Internet.

In addition, representative offices and branches must be locally registered with the Federal Service for State Statistics, the tax authorities and the Social Funds. We expect that this procedure might be also impacted by upcoming amendments.

All documents submitted to the accrediting body and registration authorities must be prepared in Russian (or translated into Russian) and duly legalised where applicable. The parent company is responsible for organising the accreditation and various registrations but can be represented by a person acting on the basis of a power of attorney.

Company reorganisation

The Civil Code provides for five forms of company reorganisation: merger, consolidations, de-mergers, spin-offs and transformation. Representative offices and branches may not be reorganised into legal entities.

Company reorganisation is a complex process that may take from three to twelve months to complete. It usually involves an audit by the tax authorities (including tax reconciliation of any missing financial reports, any arrears or overpayments) and notification to the company's creditors.

The reorganisation procedure has been amended significantly and can now involve different forms of reorganisation being carried out simultaneously or simultaneous reorganisation of legal entities of different forms (subject to certain limitations).

The creditors of a company can demand early execution or termination of the current obligations of a company participating in the reorganisation (e.g. a bank may ask to early repay a loan), however, this right of the creditors is significantly limited by the amended Civil Code.

We expect that further development to Russian corporate law will bring additional important changes to the reorganisation process.

Liquidation

A legal entity can be liquidated:

— voluntarily, by a decision of its shareholders/participants;
— by the court in the circumstances listed in the Civil Code; or
— through bankruptcy.

For more details, please see the *Corporate bankruptcy* chapter on page 84.

Voluntary liquidation of a company is complex and time consuming as it involves an audit by the tax authorities and notification to its creditors.

Closing branches or representative offices is almost as cumbersome as voluntarily liquidating a company. The only major difference is that there is no requirement to notify creditors of the closure of representative offices or branches.

Shareholders and participants agreements

The amendments to the Civil Code introduced a new definition of 'corporate agreement' that covers both shareholders and participants agreements.

These corporate agreements can be governed by non-Russian law (e.g. English law) if one of the parties to such agreement is a foreign company. This does not mean that the mere choice of foreign law will exclude the relevance of Russian law (its mandatory rules cannot be overcome) and the foreign law precedent commonly used in international joint ventures will still need some adaptation for a Russian company but importantly, more general provisions of such agreements and boiler plate clauses can now be retained.

A corporate agreement can be entered into by all the shareholders or some of them. The company itself still cannot be a party to the corporate agreement. The shareholders must notify the company upon the conclusion of a corporate agreement.

A corporate agreement can be entered into with a person who is not a shareholder to the company provided that such person has a legitimate interest in respect of the company (e.g. a creditor, a potential investor).

The corporate agreement survives the exit from the company of one of the participants/shareholders unless otherwise is provided in such agreement.

Private corporations (LLCs and private JSCs) are not obliged to disclose the content of corporate agreements. Public corporations must disclose the content of the corporate agreement within the limits provided by the JSC Law.

Subject to certain conditions and limitations, corporate resolutions adopted and transactions entered into by the company in violation of the corporate agreement can be now invalidated.

Although Russian law provides for shareholders and participants to regulate their affairs by a shareholders/participants agreement, many of the commonly used devices in such agreements are still of doubtful enforceability under Russian law according to current academic opinion. Thus where put/call options or drag and tag rights are required, or where the company is to be a party, it is still the practice to structure the joint venture through an offshore holding company under an English, or other common law, governed shareholders agreement.

These amendments are a considerable step toward a domestic Russian alternative to offshore joint ventures structures, but the following key issues with regard to foreign-law shareholders agreements remain:

— Russian law still applies to the *form* of a corporate agreement entered into in relation to a company incorporated in Russia. This means that it must be signed by all the parties as a single document.
— Foreign law cannot disapply the personal law of a legal entity (*lex societatis*) in respect of the issues that fall within its scope as these issues are part of the 'mandatory rules' of Russian law.
— It is now possible to include an option concerning a participatory interest in a Russian LLC as part of the participants agreement itself, but a further Russian notarised transfer agreement is still required.
— Corporate disputes can only be heard by Russian state commercial courts and, although the case law is inconsistent, Russian courts tend to qualify disputes concerning shares in JSCs and participatory interests in LLCs as 'corporate disputes'. This means that, where foreign arbitration is selected as the jurisdiction of the shareholders/participants agreement and an application to enforce the resulting award against a Russian party needs to be filed in Russia, there is a risk that, as the law currently stands, the Russian state courts will refuse to allow enforcement.

Strategic industries

The Foreign Investment Law[5], together with Federal Law No. 57-FZ "On Procedures for Foreign Investment in

[5] Federal Law No. 160-FZ "On Foreign Investment in the Russian Federation" dated 9 July 1999.

Companies of Strategic Significance for National Defence and Security of the Russian Federation" (the "**Strategic Industries Law**"), provides for a strict regulation of all transactions or agreements involving the participation of foreign investors in any entities engaged in activities in those sectors of Russia's economy which are deemed strategic for Russia's defence and security.

Under the Strategic Industries Law, 45 sectors of the economy have been defined as **strategic**, including:

- military technology, nuclear power, aircraft and the space industry;
- natural monopolies, such as pipelines, the maintenance of ports and airports (with limited exceptions);
- companies with a dominant market position in certain markets in Russia;
- communication services, including fixed-line telecommunications, excluding Internet access services;
- television and radio broadcasting; and
- subsoil use.

The following activities have finally been removed from the list of strategic activities:

- the use of encryption equipment, provision of encryption services and servicing of encryption equipment if such activities are carried out by banks **if** the Russian Federation does not hold a share (stake) in the charter capital of such banks; and
- the use of sources of radiation if such activities are of civilian (non-military) nature and are not the main activity of the company.

The Strategic Industries Law does not affect foreign investments which are already governed by other federal laws or by international conventions ratified by Russia.

Restrictions on foreign investors

Under the Strategic Industries Law, transactions that result in foreign investors or Russian corporate groups with a foreign element gaining control over a strategic company must be cleared by the specifically appointed Governmental Commission (the "**Strategic Approval**").

The procedure for obtaining a Strategic Approval is lengthy and cumbersome; however, if Strategic Approval is not obtained for a transaction requiring such approval, the respective transaction is void under Russian law.

If prior approval is obtained, the transaction should be conducted within the timeframe set out in the respective approval.

Foreign investors are deemed to '**gain control**' over a company if they are acquiring:

- directly or indirectly more than 50% of the voting shares in a Russian company operating in a sector deemed to be of strategic importance (a "**Strategic Company**") which does not conduct geological surveys on the subsoil and/or explore and extract minerals on federal subsoil plots (i.e. not

'operating on federal subsoil plots');
- directly or indirectly less than 50% of the voting shares in a Strategic Company that is not operating on federal subsoil plots, if the acquirer gains effective control over the company;
- directly or indirectly 25% or more of the voting shares of a Strategic Company operating on federal subsoil plots; or
- control of a Strategic Company as a result of a change in the number of voting shares in that company.

It should also be noted that certain transactions require **post-transaction notification,** which must be made within 45 days of the change of control taking effect. One example of this is when foreign investors acquire at least 5% of the shares in a Strategic Company.

Restrictions on state and international organisations

The Strategic Industries Law prohibits foreign states, international organisations and organisations controlled by them from gaining control over a Strategic Company.

It also provides that foreign states, international organisations and organisations controlled by them must obtain **prior approval** from the FAS when acquiring:

- directly or indirectly more than 5% of the voting shares of a Strategic Company operating on federal subsoil plots; or
- directly or indirectly more than 25% of the voting shares of a Strategic Company that is not operating on federal subsoil plots or otherwise acquiring the right to block decisions of that company's management bodies.

Anti-monopoly issues

General approach

General legal and regulatory framework

Anti-monopoly issues are primarily governed by Federal Law No. 135-FZ "On the Protection of Competition" dated 26 July 2006 (the "**Competition Law**"), while liability for the violation of anti-monopoly regulations is mainly established (in addition to the Competition Law) by the Code on Administrative Offences and the Criminal Code.

The Federal Anti-monopoly Service (the "**FAS**"), a Russian executive authority, controls and enforces compliance with anti-monopoly legislation.

Trends

At the end of December 2013 the Competition Law was amended to remove the post-completion notification requirements for most transactions which completed from 30 January 2014 onwards (please see the *Transaction clearance* section on page 38). The main rationale behind this change is to minimise the administrative burden, particularly in relation to medium

enterprises, so that the FAS may focus on more significant deals.

The FAS has drafted a new set of amendments to the Competition Law (the so-called 'Fourth Antimonopoly Package'). It is unclear if these are likely to be adopted in 2014. As currently drafted, the Fourth Antimonopoly Package could bring significant changes to the regulatory environment, in particular by:

— allowing the FAS to review joint ventures in accordance with the existing merger control rules;
— making the Competition Law applicable to agreements related to intellectual property;
— introducing rules on the commercial policies of dominant undertakings; and
— adjusting certain procedural aspects, such as widening the use of FAS warnings.

Scope of application of the Competition Law

The Competition Law applies to:

— agreements/actions concluded or carried out in or outside Russia that may in any way influence competition in Russia; and
— agreements/actions concluded or carried out in or outside Russia, between Russian and/or foreign legal entities/individuals, which are related to:
  - main (fixed) production assets and/or intangible assets located in Russia;
  - shares or participatory interests in, or the control over Russian legal entities; or
  - the control over foreign legal entities engaged in business activities in Russia.

The expression "legal entity engaged in business activities in Russia" encompasses all foreign entities that have supplied goods/works/services to the Russian market for an amount exceeding RUB 1 billion (EUR 21.3 million[1]) during the calendar year preceding the date of the respective transaction.

Evidently, the scope of application of the Competition Law is very broad. In practice, it may cover almost any agreement and may apply to any company directly or indirectly connected with the Russian market or Russia in general.

Anti-competitive practices and restriction of competition

The Competition Law covers the following types of anti-competitive practices and activities which may lead to a restriction of competition:

— abuse of a dominant position;
— cartel agreements and concerted actions;
— vertical agreements;
— economic coordination; and
— unfair competition.

[1] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience throughout this guide.

The Competition Law also includes rules on transaction clearance.

Abuse of a dominant position

The general rule is that a company is deemed to be dominant if it has a market share of over 50%. However, in practice, dominance may be established in certain circumstances where a company has a market share of less than 50%.

Dominance of a market is, in itself, not a violation. However, abuse of the dominant position gives rise to liability. In addition to the prohibitions outlined below in the *Cartel agreements and concerted actions* section, dominant entities are prohibited from:

- fixing or maintaining 'monopolistically' high or low prices;
- establishing different prices for the same commodity without technological or economic substantiation; and
- establishing discriminatory conditions.

Cartel agreements and concerted actions

In brief, the following arrangements are expressly prohibited by the Competition Law as agreements (cartels) and concerted actions between competing market players:

- fixing or maintaining prices/tariffs, discounts, bonus payments or surcharges;
- increasing, reducing or maintaining prices during auctions;
- dividing markets by:
  - territory;
  - volume of sales or purchases;
  - assortment of goods/works/services sold; or
  - range of sellers or purchasers/customers;
- refusing to enter into contracts with certain sellers or buyers; and
- reducing or terminating the production of goods/works/services.

Vertical agreements

If the parties to an agreement are in a seller – purchaser relationship, such a 'vertical agreement' must not contain any provisions that lead to a restriction of competition in general and, specifically, must not:

- establish resale prices for goods/works/ services, except for maximum resale prices; or
- prohibit the purchaser from selling competing products.

Economic coordination

The Competition Law also prohibits any economic coordination exercised by one business entity (the "**Coordinator**") over the activities of other business entities if:

- the Coordinator does not belong to the same group as the entities it coordinates;
- the Coordinator is not active in the market where it coordinates the business of these other business entities; and
- the coordination results in any of the prohibitions outlined in the *Cartel agreements and concerted actions* or *Vertical agreements* sections above.

Restriction of competition in general

Agreements in general must not lead to a restriction of competition in the market. In particular, they must not lead to:

- different prices being set for the same product (work, service) without economic or technological justification;
- the imposition of unfavourable terms upon a contracting party;
- the impediment of other business entities' access to or withdrawal from a certain market; and
- the establishment of membership conditions in professional or other associations, if these conditions lead to or may lead to a restriction of competition.

As a general rule, the restrictions outlined in the *Cartel agreements and concerted actions*, *Vertical agreements, Economic coordination* and *Restriction of competition in general* sections above do not apply to agreements or actions between business entities that are part of one group of companies if these entities are controlled by the same company/individual.

Unfair competition

Unfair competition is not permitted under Russian competition legislation. In particular, unfair competition includes:

- the distribution of false or incorrect information which may cause damage to a business entity, or impair its reputation;
- providing misleading information in respect of a commodity's (i) nature; (ii) manner and place of production; (iii) consumer properties; (iv) quality and quantity; or (v) manufacturers;
- an incorrect comparison of the commodities produced by a business entity with those produced or sold by other business entities;
- the sale, exchange or other placement into circulation of a commodity in breach of third-party intellectual property rights; and
- the unlawful receipt, use and disclosure of commercial secrets, official secrets or other information protected by law.

The above restrictions are closely linked to further restrictions introduced by Federal Law No. 38-FZ "On Advertising" dated 13 March 2006 (the "**Advertising Law**").

The FAS is also entrusted with monitoring compliance with the Advertising Law and may hold business entities liable for violating it.

Transaction clearance

Transactions subject to clearance

The following transactions may require pre-transaction approval from the FAS:

- the establishment of a Russian company if (i) its charter capital is paid up by shares and/or tangible or intangible assets of another company; and (ii) the new company, as a result, acquires:
  - more than 25% of voting shares in a Russian joint-stock company;
  - more than 1/3 of the participatory interests in the charter capital of a

Russian limited liability company; or
  - more than 20% of the balance sheet value of the main production and intangible assets of the company which owns the assets (and whose assets are located in Russia);
- reorganisation (in the form of a merger or accession);
- the acquisition of more than 25%, 50% or 75% of the voting shares in a Russian joint-stock company;
- the acquisition of more than 1/3, 50% or 2/3 of the participatory interests in the charter capital of a Russian limited liability company;
- the acquisition of control over a Russian company;
- the acquisition of more than 50% of the shares/participatory interests or control over a foreign "legal entity engaged in business activities in Russia"; and
- the acquisition of the right to own, use or possess the main production and intangible assets of a company if the book value of the acquired assets located in Russia exceeds the following percentages of the total book value of the seller's main production and intangible assets:
  - 20% for companies operating on commodity markets; or
  - 10% for companies operating on financial markets.

Intragroup transactions

If an intragroup transaction qualifies as being made between legal entities/individuals that belong to the same "group of persons" under article 9(1)(1) of the Competition Law (i.e. a company and an individual/legal entity holding more than 50% of the voting shares or the participatory interests in that company), then it is expressly exempt from the merger control requirements of the Competition Law.

Regarding intragroup transactions which (i) are made between parties that are not under direct control arrangements and (ii) exceed the thresholds stated below, there is uncertainty as to whether the exemption applies. Therefore applicants may consider relying on article 31 of the Competition Law, which provides for a specific clearance procedure for intragroup transactions that would normally require pre-transaction approval. This procedure allows applicants to make a prior disclosure of the group structure to the FAS and then further notify the FAS of the transaction once completed (rather than going through pre-transaction clearance).

Thresholds

The thresholds set out below only apply to companies operating on the commodity markets. For those operating on financial markets, the requirements are different (please see the *Banking sector* chapter on page 69 for information on thresholds for banks (credit organisations)).

Pre-transaction clearance thresholds*				
Aggregate worldwide value of assets of the acquirer's group and the target's group of companies	> RUB 7 billion (EUR 149 million)	and	Aggregate worldwide value of assets of the target's group of companies	> RUB 250 million (EUR 5.3 million)
OR				
Aggregate worldwide revenue of the acquirer's group and the target's group of companies from the sale of goods, works and services during the last calendar year	> RUB 10 billion (EUR 212.8 million)	and	Aggregate worldwide asset value of the target's group of companies	> RUB 250 million (EUR 5.3 million)
OR				
The acquirer, the target or any company in their group is included in the FAS Register of Business Entities with a Market Share Exceeding 35% (mostly applicable to Russian companies)				

* To assess the assets of the target's group, the assets of the seller and its group are not taken into account when, as a result of the transaction in question, the seller and its group will no longer have any rights over the target.

Liability

General remarks

Individuals and legal entities may be subject to administrative and criminal liability for non-compliance with anti-monopoly legislation.

Liability may include:

— mandatory directions issued by the FAS to cease a violation and/or transfer to the state budget of all revenue received as a result of the violation of anti-monopoly legislation (under the Competition Law);
— fixed fines/fines calculated on the basis of revenue (up to 15% of the revenue gained over the period of the violation of anti-monopoly legislation) and/or disqualification of company officials (under the Code on Administrative Offences); and
— fines and/or disqualification of company officials and, for the more serious anti-monopoly violations, up to seven years' imprisonment for company officials (under the Criminal Code).

Specific remarks

Prohibited agreements and leniency

As mentioned above, cartels and concerted actions which violate anti-monopoly regulations are strictly prohibited and may lead to severe sanctions being imposed.

However, the Code on Administrative Offences provides for a limited opportunity for companies that have participated in illegal cartels or actions to avoid penalties – the "Leniency Programme".

To obtain total immunity under the Leniency Programme, a cartel participant

must: (i) be the first to inform the FAS of the cartel's existence; (ii) submit sufficient information and/or documents to the FAS to allow an administrative violation to be identified; (iii) fully cooperate with the FAS throughout its investigation; and (iv) cease any involvement in the cartel or other infringement immediately. It is only possible to benefit from the Leniency Programme if the FAS is not aware of the reported infringement.

Collective applications for the Leniency Programme are not accepted.

Tax system

General approach

Trends

The Russian tax system is relatively new and is still experiencing a period of rapid change.

The key trend underlying Russian tax law developments in the period from 2013 to spring 2014 is the so-called 'de-offshorisation' of the economy. Many initiatives aimed at strengthening the legal framework to combat tax evasion through tax havens have been launched at the request of President Putin. The most important initiatives in this respect are:

— implementing tax residency criteria for legal entities;
— developing the concept of beneficial ownership; and
— enacting rules on controlled foreign companies.

Moreover, Russian authorities continue to tighten their control over taxpayers. Examples of this include:

— A challenge to any act of the tax authorities must now follow a

mandatory pre-trial dispute resolution procedure. This being said, timelines for certain pre-trial dispute resolution procedures have also been extended.

— Russian courts extending the scope of thin capitalisation rules to foreign sister companies.

— Russian depositories are now required to withhold tax at the maximum 30% rate on dividends accruing on certain types of securities when they are paid to a foreign company that is deemed to be acting in the interest of non-disclosed third parties.

Tax legislation is also developing on a technical level, including, for example, the extension of the compulsory requirement to file value-added tax ("**VAT**") returns electronically to all VAT taxpayers.

Core legal framework

Part I of the Tax Code dated 31 July 1998 has been in force since 1 January 1999; and Part II of the Tax Code dated 5 August 2000 has been in force since 1 January 2001 (together, the "**Tax Code**"). The Tax Code sets out general tax principles and applicable taxes, as well as the rights and obligations of taxpayers and the state tax authorities.

According to the Tax Code, taxes in Russia may be **categorised** as follows:

— **Federal taxes** applied throughout Russia at uniform rates, such as VAT. Certain taxes have a federal and a regional component (e.g. corporate profits tax) and may have their regional component reduced at the discretion of the relevant regional authority.

— **Regional taxes and local taxes** determined by the Tax Code and the local or regional government authorities, which are collected locally or regionally. Lower-tier authorities may not grant concessions for taxes governed by a higher authority.

Federal taxes	Corporate profits tax
	VAT
	Excise duties
	Payroll-related levies
	Taxes on natural resources
	State duties
	Personal income tax
Regional taxes	Corporate property tax
	Transport tax
	Gambling tax
Local taxes	Land tax
	Individual property tax

This tax structure can result in tax burdens in different locations and may require tax filings to be made at both federal and regional levels. Several tax payments may need to be made when a company has separate subdivisions in more than one Russian region.

In this chapter we provide an outline of the following aspects:

— corporate taxation;
— taxation of individuals;
— special tax regimes;
— tax incentives; and
— double taxation treaties.

Corporate taxation

Corporate profits tax

Taxpayers

Taxpayers are defined as:

— Russian companies that pay tax on their worldwide income; and
— foreign companies that conduct business in Russia through a permanent establishment and/or are in receipt of income from a Russian source.

Permanent establishments

The Tax Code defines a "permanent establishment" as a representative office, branch, division or any other separate fixed place of activity through which a foreign company regularly engages in certain business activities (as specified in the Tax Code) in Russia.

If a foreign company does not have a permanent establishment, it is not subject to Russian profits tax. Any Russian-sourced income (interest, dividends, royalties, etc.) will subsequently be subject to withholding tax.

If a foreign company conducts any of the activities specified in the Tax Code through a dependent agent who represents the company and acts on its behalf, it may also be considered as having a permanent establishment in Russia.

As a general rule, a foreign company has the right to allocate income and expenses to its Russian permanent establishment if:

— there is a double taxation treaty between Russia and the respective country; and
— the possibility of this allocation is provided for in that treaty.

If there is no double taxation treaty, then the costs of a foreign company may be allocated to its Russian permanent establishment, provided that such costs were incurred for the purpose of that permanent establishment.

Tax base

The tax base is the total income received by the taxpayer less income exempted from taxation and expenses, as defined by the Tax Code.

The types of income that are exempt from profits tax include, by way of example:

— income in the form of property received by the Russian company from a parent company, a subsidiary or an individual, if the ownership of the recipient or the transferor in the capital of the other party is more than 50%, and the property received (excluding money) is not disposed of within one year from the date of receipt;
— income in the form of property as well as non-property rights transferred to the Russian company by its parent company for the purpose of an increase in the net assets of the taxpayer;
— income gained from revaluation of fixed assets and securities; and
— income in the form of property received as a contribution to a company's charter capital.

Deductibility of expenses

Expenses are generally recognised on an accrual basis. They are deductible for profits tax purposes if they are related to the taxpayer's income and if they are economically justified and evidenced by the requisite documentation. The tax authorities are stringent in their application of these criteria.

The law specifies certain **non-deductible expenses**, such as:

— the cost of assets transferred free-of-charge;
— any penalty payments made to the budget; and
— any employee remuneration not provided for in the relevant labour contracts, etc.

Some types of expenses are subject to **limitations on tax deductibility**:

— representative expenses: up to 4% of payroll;
— pension and life insurance for employees: 12% of payroll;
— medical insurance for employees: 6% of payroll; and
— interest on loans and other borrowings charged at a rate that is more than 20% above the average rate charged for comparable loans made in the same quarter. In the absence of comparable data, or at the taxpayer's choice, the maximum rate fixed until 31 December 2014 is:
  - for rouble loans, the refinancing rate of the Central Bank of Russia at the date the interest is being deducted (8.25% – from 14 September 2012), multiplied by 1.8; and
  - for foreign currency loans, the refinancing rate of the Central Bank of Russia at the date the interest is being deducted, multiplied by 0.8.

However, starting from 2015, (i) the procedure for calculating limits based on a company's own comparable tax liabilities and (ii) the link between foreign currency liabilities and the Central Bank of Russia's refinancing rate will no longer apply. This will allow the tax authorities to control the level of interest expenses only for controlled transactions and in accordance with transfer pricing rules.

Interest is also subject to thin capitalisation rules, with the applicable debt-to-equity ratio being equal to 3:1 (12.5:1 for banks and leasing companies).

Depreciation

Taxpayers are required to maintain separate accounts for profits tax purposes. The method applied should be clearly explained in the taxpayer's accounting policy. Once chosen, the accounting method may not be modified during the financial year (1 January to 31 December).

Two depreciation methods are available for profits tax purposes:

— the straight-line method; and
— the reducing balance method.

Depreciable property includes fixed and intangible assets with a useful life of at least one year and an initial value exceeding RUB 40,000 (EUR 851[1]).

[1] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience throughout this guide.

The useful life of depreciable fixed assets is determined, within certain limits, based on a classification adopted by the government. For intangible assets, the useful life is the utilisation period defined by any agreement (with a default provision of ten years). The tax base for a fixed asset includes all costs incurred in order to place the asset in service for production. Accelerated depreciation is permitted in cases stipulated by the Tax Code, e.g. for leased property under financial lease.

Certain assets (such as works of art) are not subject to depreciation.

Losses

Losses can be carried forward and offset against future taxable profits for a period of ten years (carrying back is not permitted). Losses from the sale of fixed assets are recognised evenly over the remaining useful life of the assets.

Transfer pricing

As of 1 January 2012, the Tax Code has been supplemented with a new section dedicated to transfer pricing principles, the tax supervision of transactions between related parties and advance pricing agreements.

Controlled transactions

The list of controlled transactions under the Russian transfer pricing rules includes, among other things, all cross-border (and certain domestic) related-party transactions. Transactions between the members of a Russian consolidated group of taxpayers are excluded from the list.

The list of related parties is relatively extensive. In general, related parties are identified when "the specifics of relations between them may affect the conditions and/or results of the transactions entered into by such parties, and/or the financial results of their activities or the activities of parties that they represent".

Specifically, the list of related parties includes:

- two companies, where one holds more than 25% of the shares in the other, directly or indirectly;
- a company and an individual holding more than 25% of its shares, directly or indirectly;
- two companies with the same parent company that holds more than a 25% share in each company;
- a company and its general director, or companies with the same general director; and
- groups of individuals/companies with more than a 50% share or participatory interest.

Methods

In terms of transfer pricing, the new regulations have retained the three previous transfer pricing methods, with "comparable uncontrolled price" (CUP) having priority, in addition to "resale minus" and "cost plus". Two additional methods ("comparable profitability" and "profit split") have been introduced.

These methods are in line with the transfer pricing practices of European countries and, in particular, the OECD Transfer Pricing Guidelines.

Each taxpayer can select the method it wishes to apply (and may even choose to use a combination of methods, or another method not expressly provided for by the Tax Code), provided it documents the reasons for this choice.

Reporting and documentation requirements

The new transfer pricing rules have introduced an overall responsibility on taxpayers to prepare documentation justifying the prices applied in all transactions specified as controlled. Upon request from the tax authorities (which may be submitted from 1 June of the year following the year of the controlled transaction), taxpayers must submit the requested documentation.

In addition, companies are obliged on a yearly basis (before 20 May) to notify their local tax inspectorates of all controlled transactions concluded between the same related parties during the previous calendar year. The notifications should contain general information on (i) the subject-matter of the controlled transactions, (ii) the parties involved, (iii) the transfer pricing methods applied in the definition of prices; and (iv) the amount of profits received and expenses incurred as a result of these transactions.

Special transitional rules are applicable to the reporting and documentation of controlled transactions entered into in the course of 2012-2013.

Tax consolidation

Since 1 January 2012, Russian companies can elect to form a consolidated tax group, provided they satisfy certain thresholds (in terms of the group's total tax liabilities, statutory accounting revenue and assets) and other criteria. In this case a single tax base is calculated for the consolidated tax group, as opposed to the calculation of multiple tax bases for the individual members. This allows the losses of certain members to be offset against the profits of others.

In practice, the impact of the new regime is limited for:

- Russian companies in general, as the thresholds are currently so high as to allow only a handful of major corporate groups to be eligible; and
- foreign investors, as:
  - foreign companies cannot become a member of a Russian consolidated tax group; and
  - group members are jointly liable for the group's tax liabilities.

Tax rate

The general profits tax rate is 20%, with 2% of the tax being payable to the federal budget, and the remaining 18% being payable to the budget of the region where the company is incorporated.

In some cases, reduced tax rates apply. By way of example, a 0% profits tax rate applies to companies (domestic and foreign) transferring participatory interests or non-listed shares in Russian companies acquired after 1 January 2011, provided the equity interest was held for at least five years.

Taxation of dividends

Dividends received by Russian companies

Dividends received by a Russian company from another Russian company, or from a foreign company, are taxed at a flat rate of 9%. Dividends received from 'strategic investments' are exempt from Russian corporate profits tax. An investment is considered strategic when:

— the recipient of the dividends owns at least 50% of the payer's capital, or owns depository receipts entitling it to receive at least 50% of the amount paid in dividends; and
— the share or depository receipts have been owned for at least 365 days on the day dividends are declared.

Dividends from companies residing in low-tax jurisdictions may not be exempt from Russian corporate profits tax. These jurisdictions are identified in an official list which is updated by the Ministry of Finance.

Dividends paid by Russian companies

The standard 15% tax rate is applicable to dividends paid by Russian companies to foreign companies. The tax should be withheld by the Russian companies paying the dividends.

If there is an applicable double taxation treaty, then the standard tax rate may be reduced to a minimum rate of 5%.

Since 1 January 2014, Russian depositories acting as tax agents are required to apply the 30% withholding tax on dividends accruing on equity securities of Russian companies kept in the central securities depository (the National Settlement Depository) and paid to foreign companies that are deemed to be acting in the interest of non-disclosed third parties. A foreign legal entity is deemed to be acting in the interest of non-disclosed third parties if it does not provide information on the persons exercising the rights related to these securities.

VAT

Taxpayers

VAT applies in particular to companies, including those importing goods into Russia.

If the taxpayer's aggregated income for three consecutive months, excluding VAT, is below RUB 2 million (EUR 42,553), the taxpayer may be exempt if it applies for the exemption.

Tax base

The following operations are subject to VAT (even if they are supplied free of charge):

— sale of goods, works and services within Russia;
— transfer of goods, works and services within Russia for the taxpayer's own purposes, if the relevant expenses are not deducted for the purpose of corporate profits tax;
— construction and building projects for the taxpayer's own use; and
— imports into Russia.

The **taxable base** is generally defined as the market value of the goods, works

and services supplied, inclusive of excise duties but exclusive of VAT.

If the goods, works and services are supplied free of charge, an imputed price (set at the market value for identical goods, works or services, excluding VAT) is used.

Exempt supplies

Certain activities, including the following, are exempt from VAT:

- assignment of loan agreements;
- operations with securities and derivative financial instruments;
- certain banking transactions;
- transactions with medical equipment and medical services;
- certain research and development services;
- transfer of exclusive and non-exclusive rights to software, know-how, databases, inventions, and a range of other rights under a licence agreement (except trademarks);
- imports of technological equipment that does not have a Russian equivalent (as per a government approved list); and
- sale of scrap and waste ferrous metals.

Tax rates

The standard rate is 18%. A reduced rate of 10% applies to books, periodicals, medical goods, certain foods and children's clothes. A 0% rate is applicable to the following operations:

- export of goods outside Russia;
- works and services related to the transportation of goods in transit; and
- certain services and goods supplied to foreign diplomatic missions, etc.

Input VAT

The VAT payable to the tax authorities is the difference between the VAT accountable for transactions subject to VAT ("**output VAT**") and the VAT incurred on purchases subject to VAT ("**input VAT**").

Input VAT is only recoverable in certain cases. Recovery no longer depends on whether it has been paid to the supplier. VAT on imports can be recovered only after payment is made to the customs authorities.

Input VAT related to expenses or assets used for the manufacture or sale of products exempt from VAT may not be offset. In the same way, input VAT related to expenses or assets used for "non-production activities" may not be offset.

Any VAT incurred on purchases and expenses which relate to activities, both subject to and not subject to VAT, must be apportioned. Only the part which is deemed to relate to activities subject to VAT may be offset as input VAT.

Any excess of input VAT over output VAT has to be refunded to the taxpayer. As a general rule, such a refund can only be made after the tax authorities have undertaken an audit. However, an accelerated VAT recovery procedure is also possible. Under this procedure, a taxpayer may recover VAT before the tax authorities complete the tax audit and

have made a definitive decision on VAT recovery. According to these rules, companies which have existed for at least three years and paid taxes exceeding RUB 10 billion (EUR 212.8 million) over the last three years are eligible for the accelerated procedure, without having to provide a bank guarantee. Other companies can benefit from the accelerated procedure provided that they give a bank guarantee for the amount of VAT to be reimbursed.

VAT invoices serve as the basis for the offset of input VAT. They have to be issued in Russian and must contain the information specified in the Tax Code.

Reverse charge

If a foreign company which does not have a Russian tax registration supplies goods, works or services in Russia, VAT is collected through a withholding mechanism. The tax-registered buyer is required to withhold VAT from the amount payable to the foreign seller and to remit it to the authorities. The tax-registered buyer may then offset the VAT which has been withheld and paid, as input VAT.

Commissioners and agents with a Russian tax registration are considered to be tax agents in relation to goods supplied on behalf of non-registered foreign companies.

Filing and payment

VAT is payable on the earlier of the following two dates:

— the date of *shipment* or *transfer* of goods, works or services; or

— the date of *payment* (in full or in part) for a *future* shipment or transfer of goods, works or services.

Advance payments are included in the VAT base at the time payment is received.

Taxpayers must file their VAT declarations on a quarterly basis. VAT returns must be filed within 20 days after the end of the tax period.

Taxpayers also have the option to pay VAT in three instalments, in the three months following the relevant quarter.

Starting from the reporting for the first quarter of 2014, all VAT taxpayers, irrespective of the number of staff, must file VAT tax returns electronically. This obligation also applies to branches and representative offices of foreign legal entities registered in Russia.

Excise duties

Excise duties must be paid by the producers and/or importers of excisable products. Excisable products are, for example, oil products, alcohol, tobacco and cars.

Excise duties are generally levied on the value of the product (please see the *Customs regulations* chapter on page 63).

Corporate property tax

Property tax is payable in accordance with regional regulations and with the Tax Code.

Taxpayers

The following structures are taxpayers for the purpose of corporate property tax:

— Russian companies having fixed assets on their balance sheets;
— permanent establishments of foreign companies having fixed assets on their balance sheets; and
— foreign companies owning immovable assets in Russia.

The above entities are required to pay property tax to the regional budget of the region where the relevant property is located.

Religious organisations and various types of public organisations are exempt from property tax.

Tax base

Property tax is assessed on fixed assets and "profitable investments in property" (as defined by Russian accounting standards). It may also encompass leased property in certain cases.

Intangible assets, movable property accounted for as fixed assets booked after 1 January 2013, inventories, work-in-progress and financial assets (among other categories) are not subject to property tax.

The tax base for most assets is the average annual residual value of taxable property for financial reporting purposes (and not for tax purposes).

However, since 1 January 2014, the cadastral value is used to calculate the corporate property tax base for the following types of property:

— business centres, shopping centres and premises in these buildings;
— non-residential premises used as offices, shops or to provide catering services or services to consumers, or which are intended for such use;
— any property owned by a foreign company operating without a permanent establishment in Russia; and
— any property owned by a foreign company with a permanent establishment in Russia, when the property is not allocated to that permanent establishment.

Tax rate

The rate is set at regional level.

When the average annual residual value is used to calculate the tax base, the rate may not exceed 2.2%. This maximum rate is currently imposed in most regions, including Moscow and Saint Petersburg.

The tax rate in respect of property for which the tax base is calculated based on the cadastral value may not exceed 2%. In Moscow, the rate will be progressively increased from 0.9% in 2014 to reach a maximum rate in 2018, with annual increases of 0.3% between 2015 and 2017.

Payments

The tax period is a calendar year. Advance tax payments must be calculated and paid on a quarterly basis. Taxpayers must file quarterly tax returns within the 30-day period following the reporting period. Annual returns must be filed by 30 March following the reporting period.

Payroll-related levies

Taxpayers

Several kinds of payroll-related taxes must be paid by employers. This applies to Russian employers as well as to foreign companies.

Insurance contributions

Insurance contributions are paid to three separate non-budgetary funds: the Pension Fund, the Federal Social Insurance Fund and the Federal Mandatory Medical Insurance Fund. In the 2014 calendar year, a regressive scale of insurance contributions is applicable: 30% is payable on the part of an employee's annual gross remuneration below RUB 624,000 (EUR 13,276); and 10% is payable on the part of any remuneration in excess of this amount.

A general rate of 22% is applicable to the remuneration of foreign employees who have no temporary or permanent residence permit. However, payments and other compensation made to highly qualified foreign specialists (please see the *Employment/Migration* chapter on page 105), as well as to those temporarily employed in Russia under labour agreements concluded for a definite term of less than six months, are exempt from social contributions.

Other payroll contributions

Contributions to the Social Insurance Fund against industrial accidents and diseases are also payable. They vary from 0.2% to 8.5% of monthly salary and depend on the risk category of the employee.

Taxes on natural resources

Taxpayers who use land, either on the basis of ownership rights or rights of permanent use, have to pay **land tax** to the local budget. The tax base used for calculation is the relevant land's cadastral value (which, in practice, is significantly lower than its market value). The tax rate is set at a local level and may not exceed 1.5% of the cadastral value (0.3% in respect of certain types of land).

Water tax is imposed on taxpayers who use water to produce hydroelectricity. The tax rates vary depending on the specific water object.

Mineral resources extraction tax is imposed on sub-soil users. It applies to various types of minerals, including oil and gas. It is based on the value of the extracted resources, and the rate varies according to the type of mineral.

Transport tax

This is a tax payable on registered transportation vehicles by the registered owners of those vehicles. The methods of declaration and payment are established by regional authorities.

The transport tax rates are generally fixed at federal level, but the regional authorities are entitled to increase/decrease these rates by a maximum of ten times. In addition, the regions have a right to set different transport tax rates depending on the categories of vehicles, their age and/or emission class.

State duties

According to the Tax Code, a state duty is a fee charged on companies and

individuals for certain services supplied by state bodies.

By way of example, the state duties for registering a Russian company currently amount to RUB 4,000 (EUR 85) and for accrediting a foreign company's branch, RUB 120,000 (EUR 2,553).

The maximum state duties for the consideration of cases by the courts of general jurisdiction and by magistrates' courts ("*mirovye sudi*") are currently RUB 60,000 (EUR 1,276). The equivalent maximum state duties for the commercial courts now amount to RUB 200,000 (EUR 4,255).

Taxation of individuals

Income tax

Taxpayers

Taxpayers are subject to Russian income tax as either tax residents or non-residents.

Tax residents are taxed on their worldwide income. An individual is considered to be a tax resident if he/she is physically present in Russia for at least 183 calendar days during a 12-month rolling period. According to clarifications from the Ministry of Finance, however, the tax residence status of an individual should be defined by counting the days spent in Russia within the relevant calendar year.

Non-residents have tax imposed on their Russian-sourced income, irrespective of the nature of that income.

Taxable income

This is gross income less deductions and exemptions.

Gross income is defined as any economic gain, in cash or in kind, received by a taxpayer and subject to his/her discretionary disposal.

Deductions and non-taxable income

A Russian tax resident can benefit from four kinds of deductions:

- **standard deductions** are available for certain categories of taxpayers (disabled persons, war veterans, etc.);
- **social deductions** comprise of educational expenditures (per taxpayer and each of his/her children) and medical expenditures (per family), up to a combined annual maximum of RUB 120,000 (EUR 2,553);
- **property deductions** relate to the purchase and sale of property (mainly residential real estate);
- **professional deductions** are generally permitted for individual entrepreneurs and include, for example, expenditure for the creation of intellectual property rights.

Certain statutory allowances, bank interest (within limits), state pensions (and certain other pensions), and revalued shares (issued as a result of statutory revaluation, merger or reorganisation) are **exempt** from taxation.

Tax rates

Residents

- A standard flat rate of 13% applies to most types of income;
- a rate of 9% applies to dividends received from Russian or foreign companies; and
- a rate of 35% applies to certain

prizes, insurance receipts and interests from bank deposits in excess of specific limits.

Non-residents

A general rate of 30% applies to all types of Russian-sourced income except dividends (to which the rate of 15% applies). It may be possible to apply the relevant provisions of a tax treaty in order to exempt certain types of income from non-resident taxation.

In addition, a 13% personal income tax rate has applied since 1 July 2010 to remuneration received from professional activities of non-residents with a highly qualified specialist status under Russian immigration law.

Tax payments

Withholding of tax

Russian companies, individual entrepreneurs and permanent establishments of foreign companies are considered to be tax agents. They must calculate, withhold and pay income tax on the payments they make to individuals.

As a result, employees are not required to file tax returns for their salary, unless they claim property deductions or they have other income which is subject to the obligation to file a tax declaration.

An individual entrepreneur remains personally responsible for meeting his/her income tax obligations.

Tax return

Individuals must file returns and pay the appropriate income tax if:

— income was received from outside Russia (in the case of a Russian tax resident);
— tax was not properly withheld; or
— income was received from the sale of property, etc.

The tax return must be filed by 30 April in the year following the tax period.

The amount of tax due must be paid by 15 July in the year following the relevant tax period. However, if the taxpayer leaves Russia, he/she must file a tax return at least one month before his/her departure and pay the amount of tax due within 15 days after the filing date.

Individual property tax

Taxpayers

According to law No. 2003-1 "On Individual Property Taxes" dated 9 December 1991, the owners of houses, flats, rooms, cottages, garages, other buildings or constructions are liable to pay individual property tax.

Tax rates

The total inventory cost of the property, which is substantially lower than the market value, is used to compute the tax rate, although this is expected to change. The Russian Ministry of Finance is developing a proposal to base the calculation on the cadastral value of the relevant property, which is much closer to the market value.

As individual property tax is a local tax, the local government authorities are entitled to set the tax rate within prescribed statutory limits.

Special tax regimes

The Tax Code provides for the following special tax regimes according to which a corporate taxpayer is entitled to pay one special tax instead of a number of separate taxes:

— simplified tax system;
— tax on imputed income;
— unified agricultural tax; and
— production sharing.

Special regimes may be applicable if the necessary requirements are met, as outlined below.

Simplified tax system

Taxpayers

Companies are eligible for the simplified tax system if they meet the following criteria:

— their annual turnover does not exceed RUB 45 million (EUR 957,447);
— the combined net book value of their fixed and intangible assets does not exceed RUB 100 million (EUR 2.1 million); and
— they employ less than 100 persons.

The Tax Code includes a list of organisations that may not use the simplified tax regime. This includes: (i) foreign companies; (ii) Russian companies with local branches and/or representative offices; (iii) companies in which more than 25% of the capital is owned by other companies; (iv) banks; (v) insurance companies; (vi) pension funds; and (vii) investment funds.

Tax rates

The rate for this tax regime is as follows:

— 6% – if all income (without deductions) is considered to be the tax base; or
— 15% – if income (less deductible expenses) is considered to be the tax base.

The simplified tax system is used as a single substitute for profits tax, property tax and VAT (subject to several exceptions). The use of this system does not exempt employers from making obligatory pension insurance contributions or from withholding income tax from their employees' compensation. Also, from 1 January 2015, the property tax exemption will no longer apply to property whose tax base is calculated on the basis of its cadastral value (such as business and shopping centres, offices)

Tax on imputed income

Regional authorities have the right to impose this tax on certain categories of taxpayers (e.g. small companies).

The tax rate is 15% on "imputed" monthly revenue and is adjusted by special coefficients which are based on the type of land used, the range of goods being produced, the level of income received each month and seasonal factors. When this tax is applied, the taxpayer becomes exempt from most, but not all, taxes and contributions (for example, obligatory pension insurance contributions remain due).

Unified agricultural tax

This tax system is aimed at reducing the obligatory tax burden on taxpayers involved in agricultural production.

Taxpayers

Taxpayers producing, processing (including industrial processing) and selling agricultural products are entitled to use this tax system, provided that the share of income they receive from the sale of agricultural products is at least 70% of their overall sales income.

Tax rate

The tax rate is set at 6% of revenue less certain deductible expenses that are listed in the Tax Code and include, in particular, the following:

— expenses relating to the acquisition, construction and manufacturing of fixed assets (being allocated during the useful life term of the relevant assets);
— lease payments;
— wages costs;
— expenses connected with certain types of insurance payments (both obligatory and voluntary); and
— the cost of material.

The unified agricultural tax substitutes profits tax, VAT (except for import VAT) and property tax.

Production sharing

Taxpayers

This simplified tax system may be used by companies (investors) entering into production sharing agreements ("**PSAs**") under which they are granted an exclusive right to carry out mineral exploration and mining operations on a particular subsoil area.

PSAs provide for the sharing of profitable production between the Russian state and an investor. A part of "compensational production" is granted to the investor to compensate them for the expenses connected with the project. In general, this does not exceed 70% of the whole amount of production or 90% when the project is implemented on the Russian continental shelf.

The production sharing tax system may be used if the relevant PSA (i) is concluded as a result of an auction and (ii) provides that, if the project's return on investment exceeds originally agreed expectations, the Russian state's share in the profitable production will increase.

General PSA regime

If a general PSA regime is used, the main characteristics of the production sharing tax system are as follows:

— Certain expenses incurred by the investor for the purposes of performing the PSA are subject to reimbursement by "compensational production".
— VAT, taxes on natural resources, state duties, land tax and excise duties paid in connection with performing the PSA are subject to reimbursement by the state.
— Goods imported to and exported from Russia are exempt from the payment of customs duties.
— Property tax is not payable on fixed assets used solely for performing the PSA.

— Transport tax is not payable on vehicles used solely for performing the PSA.
— The relevant local or regional authority may exempt the investor from paying any regional or local taxes.

Special PSA regime

Additional tax privileges may apply if (i) the PSA is concluded under a procedure which differs from the general procedure described above and (ii) the share in the production taken by the Russian state is at least 32%.

Incentives

Regional incentives

Taxpayers implementing major investment projects may, in many Russian regions, benefit from tax and economic incentives fixed at regional level.

To receive beneficial status, the relevant project must meet specific criteria (for example, as a priority investment project or project of particular importance). This presupposes injecting substantial financial resources into the economy of the region and creating jobs at new production facilities.

These incentives may include:

— corporate profits tax rate reduced to a minimum of 15.5%;
— exemption from property, land and transport taxes;
— exemption from customs duties and import VAT; and
— subsidies compensating taxes paid to the regional budgets and/or interest paid to Russian banks on loans and credits.

Special economic zones

Taxpayers can benefit from incentives granted to special economic zones ("**SEZs**") which have been created in Russia by Federal Law No. 116-FZ "On Special Economic Zones in the Russian Federation" dated 22 July 2005 in order to promote economic growth in specific areas and regions of Russia.

The general aim of SEZs is to attract foreign investment: as SEZs are exempt from customs duties, they are an effective means of promoting import and export business. The tax advantages provided for the residents of these zones are as follows:

— reduced corporate profits tax;
— exemption from property tax and land tax; and
— exemption from customs duty and VAT (in several cases).

Types of SEZ

There are four types of SEZ:

— technical research and implementation zones (Saint Petersburg, Dubna, Tomsk, Zelenograd);
— industrial production zones (Lipetsk, Tatarstan);
— recreation and tourism zones (Altai, Buryat Republic, Kaliningrad); and
— port zones.

A company registered in Russia is entitled to obtain the status of a SEZ resident after entering into a special agreement with the local agency in charge of the relevant zone.

Skolkovo innovation centre

In 2010, a territorially isolated complex in the Moscow Region named the "Skolkovo innovation centre" was created for the purpose of research, development, and commercialisation of research and development activity. A special legislative regime regulating how it will operate has been established.

The participants in the Skolkovo initiative benefit in particular from the following tax, customs and accounting incentives:

- 0% corporate profits tax rate applicable to income generated as a result of research, development and commercialisation for the first ten years of a participant's registration in the Skolkovo project;
- exemption from property tax and land tax;
- reduced payroll-related taxes;
- VAT exemption;
- reimbursement of customs duties and VAT payable upon the importation of goods;
- exemption from the obligation to keep financial accounting, unless the participant's annual income exceeds RUB 1 billion (EUR 21.3 million); and
- exemption from the payment of state duties for the issuance of work permits, invitations and visas for foreign employees.

In order to obtain the required status to operate in the Skolkovo innovation centre and benefit from these incentives, investors have to set up Russian companies to conduct research there and follow a special procedure.

Double taxation treaties

Double taxation treaties exist between many countries on a bilateral basis in order to prevent double taxation, i.e. taxation which is levied twice on the same income, profit, capital gain, inheritance or other item. The treaties generally guarantee non-discriminatory tax treatment and provide for cooperation between the tax authorities of the respective signatory countries.

Tax treaties signed by Russia are usually based on the OECD Model Treaty and the United Nations Model Convention. The provisions of these treaties override Russian domestic law.

The table below contains the tax rates applicable under several double taxation treaties to which Russia is a signatory. The rates apply to withholding taxes on Russian sourced income. The numbers in brackets refer to the notes below the table.

Country	Dividends	Interest	Royalties
Austria	5 or 15% [1]	0%	0%
Belgium	10%	0 or 10% [2]	0%
Canada	10 or 15% [3]	10%	0 or 10% [4]
China	10%	10%	10%
Cyprus	5 or 10% [5]	0%	0%
France	5, 10 or 15% [6]	0%	0%
Germany	5 or 15% [7]	0%	0%
Ireland	10%	0%	0%
Italy	5 or 10% [8]	10%	0%
Japan	15%	15%	0 or 10% [9]
Korea (South)	5 or 10% [10]	0%	5%
Luxembourg	5 or 15% [11]	0%	0%
Netherlands	5 or 15% [12]	0%	0%
Spain	5, 10 or 15% [13]	0 or 5% [14]	5%
Switzerland	5 or 15% [15]	0%	0%
Ukraine	5 or 15% [16]	10%	10%
UK	10%	0%	0%
USA	5 or 10% [17]	0%	0%

Notes:

[1] 5% for shareholdings of 10% or more, provided the investment is at least USD 100,000, otherwise 15%;

[2] 0% for bank loans or loans granted (or guaranteed) by a Contracting State, otherwise 10%;

[3] 10% for shareholdings of 10% or more, otherwise 15%;

[4] 0% for (i) copyright royalties and other like payments in respect of the production or reproduction of any literary, dramatic, musical or other artistic work, (ii) royalties for the use of computer software or (iii) royalties for the use of patents where the payer and the beneficial owner of the royalties are not related persons, otherwise 10%;

[5] 5% if the initial investment is greater than EUR 100,000, otherwise 10%;

[6] 5% if the investment is not less than EUR 76,225 and if the recipient pays tax; 10% if only one of these two circumstances applies; otherwise 15%;

[7] 5% for shareholdings of 10% or more, otherwise 15%;

[8] 5% for shareholdings of 10% or more, otherwise 10%;

[9] 0% for royalties in respect of literary, artistic or scientific works including films and tapes; 10% for royalties in respect of any patent, trademark, design or model, plan, secret formula or process, or industrial, commercial or scientific equipment, or information concerning industrial, commercial or scientific experience;

[10] 5% for shareholdings of 30% or more, provided the investment is at least USD 100,000, otherwise 10%;

[11] 5% for shareholdings of 10% or more provided the investment is at least EUR 80,000, otherwise 15%;

[12] 5% for shareholdings of 25% or more, otherwise 15%;

[13] 5% for shareholdings of at least EUR 100,000 and if the dividends are exempt from tax; 10% if either condition is met; otherwise 15%;

[14] 0% if the actual recipient of interest is the government of the other contracting state, or for long-term bank loans (exceeding 7 years); otherwise 5%;

[15] 5% for shareholdings of 20% or more, if the investment is at least CHF 200,000; otherwise 15%;

[16] 5% for shareholdings of at least USD 50,000; otherwise 15%; and

[17] 5% for shareholdings of 10% or more, otherwise 10%.

Customs regulations

General approach

Russia is a member of the Eurasian Economic Community ("**EurAsEC**"), the Customs Union of Belarus, Kazakhstan and Russia (the "**Customs Union**") and the World Trade Organisation ("**WTO**").

Customs are regulated by the Customs Code of the Customs Union (the "**Customs Code**") that came into force in mid-2010, together with Federal Law No. 311 dated 27 November 2010 "On Customs Regulation in the Russian Federation", replacing the Customs Code of the Russian Federation.

The establishment of the Customs Union resulted in the creation of a single customs territory between its member states. After that achievement, Belarus, Kazakhstan and Russia continued their phased economic integration by forming the Single Economic Space ("**SES**"), which was technically established on 1 January 2012. Ultimately, the SES will result in the creation of a common market allowing the free circulation of goods, services, capital and labour between its member states. Another aim

of the SES is the adoption of unified policies with respect to competition and natural monopolies. Full integration is expected in 2015.

The borders of the Customs Union and the SES are expected to expand. The roadmap for Armenia's entry into the Customs Union and the SES was approved at the end of 2013. A similar draft document for Kyrgyzstan is also being prepared.

Customs Union
Key features of the Customs Union

- Customs control has been moved from the Russia-Belarus and Russia-Kazakhstan borders to the outside borders of the Customs Union. As a result, customs, veterinary, sanitary and border control are now all performed at the outside borders of the Customs Union.
- Joint inspection by the customs authorities of the Customs Union member states (such as transport, vehicular control on the outside border of the Customs Union, and sampling of goods for obligatory veterinary control) are made on a 'single window – one stop' clearance basis to accelerate border crossings.
- No obligatory customs-clearance procedures exist between the member states.
- Customs duties and other economic restrictions do not apply to trade between Customs Union members, with the exception of special protective, anti-dumping and compensatory measures.
- Each member of the Customs Union is obliged to use a unified nomenclature of goods and non-tariff regulatory measures for trade with non-member states.
- Import duties are payable to a special accumulation account and are allocated between the members of the Customs Union according to the following proportion: Belarus – 4.7%; Kazakhstan – 7.33%; and Russia – 87.97%.
- Customs duty rates with respect to export to third countries are indicated in the laws of the respective exporting state. Export duties are paid to the budget of the country of production and are not allocated between the Customs Union members.
- 0% value-added tax ("**VAT**") is charged on goods exported within the Customs Union territory. Goods imported within the Customs Union territory are exempted from excise duties and indirect taxation.
- Customs authorities may challenge the declared customs value for customs clearance for a period of up to three years following the goods' release. For certain types of products, this term may be extended up to five years by internal legislation.
- There is a unified register for items of intellectual property registered in the territory of the Customs Union. Authorised economic operators ("**AEOs**") are in operation. They are permitted to store goods at their

own warehouses and release them into free circulation before submitting a customs declaration.
— Statistical databases for streamlining the control and analytical functions of the customs authorities, as well as enabling the exchange of information between the Customs Union member states are in place.

Customs Union recent developments

— Due to the 'de-offshorisation' trend, special simplified procedures for AEOs importing goods from, or paying for imported goods through, territories listed as offshore territories by the Ministry of Finance were revoked.
— The customs internal risk management system was extended to cover operations with residents of offshore territories and operations potentially related to the non-repatriation of currency by Russian residents.
— Excise duties with respect to certain products (e.g. tobacco and alcohol) were increased at the beginning of 2013. However, as a result of WTO accession, the general trend is that average tariffs have decreased and will continue to do so (please see the *WTO* section below).
— All legal entities are required to submit forms declaring the goods transported across the border of the Customs Union electronically (since 1 January 2014).
— Customs Union member states are working on the unification of their currency control and anti-monopoly legislation and are working towards the adoption of principles which unify the currency control policy within the Customs Union.
— Customs Union member states are working on improving customs valuation methods. The requirement to prove the absence of interdependence between the declarant and its supplier with respect to determining the customs value of goods has been replaced by the right to do so.
— The court practice relating to the Customs Union issues continues to develop. The Supreme Commercial Court of the Russian Federation has published Ruling No. 96 of the Plenary Meeting of 25 December 2013 "On Certain Issues of the Practice of Considering Disputes Involving the Determination of the Customs Value of Goods Imported into the Customs Territory of the Customs Union". Although the Ruling has in itself no innovative provisions, its adoption is a positive development as it was necessary to regulate the customs value at the Customs Union's level. The Court had clarified, in particular, that the customs value is determined with respect to the goods subject to import sale. According to the Court, a sale is considered to be a chain of transactions involving the transfer of title to the relevant goods against payment.

WTO

After many years of negotiations, Russia finally signed the Protocol on Accession to the WTO on 16 December 2011. Accession took place in the summer of 2012 and is expected, given time, to result in significant changes to the Russian trade market, in particular due to:

— the decrease of the average weighted customs tariff rate for the import of goods to the Russian territory from 10% to 7.8% (for industrial goods from 9.4% to 6.4%); and
— the lifting of certain restrictions on foreign ownership in specific sectors such as telecoms, insurance and banking.

As various transitional periods were established with respect to certain products and industries, the above changes were not yet in force on 5 May 2014.

Furthermore, the accession to Government Procurement Agreements, which was originally envisaged, did not materialise.

As a member of the Customs Union and the SES, Russia plans to play the role of WTO agent for the other member states of the Customs Union.

Trade between Customs Union and third countries

Overall, there are 17 types of customs procedures, including the import and export procedures established by the Customs Code. Below, we give an overview of the general features of the import and export procedures.

Importing

Declaring procedures

Under the Customs Code, declaration procedures must be completed in the country where the importing company is registered. Therefore, when importing goods to Russia (or to the customs territory of the Customs Union) a Russia-based company must fulfil customs clearance formalities for imported goods at an appropriate customs office in Russia.

In addition, when imported goods cross the customs border of the Customs Union in Belarus or Kazakhstan, a border post at the relevant country must fulfil the procedure for the internal customs transit of the imported goods to the destination point within Russia, i.e. to the customs point where the imported goods will be cleared.

Customs payments (VAT, customs and excise duty)

When goods are imported into the territory of the Customs Union from third countries, customs payments are made (i) on the territory of the member state whose customs authorities release the goods; and (ii) in the currency of that member state.

The forms and the timeframes for customs payment are determined by the legislation of the respective member state. For instance, under Russian law, customs payments for goods imported

into Russia must be made on or prior to the day the customs declaration is submitted to the Russian customs authorities.

VAT, customs duties and excise duties must be paid by separate payment orders. VAT and excise duties are to be paid to the Russian budget, whilst customs duties are transferred to a special accumulation account.

Import duties

The Customs Union member states are obliged to apply the common customs tariff and unified nomenclature of goods to goods imported into the Customs Union.

Tariff privileges

Certain goods imported into the Customs Union may be subject to tariff privileges, such as exemptions from, or reductions in, import duties.

Tariff preferences

Goods originating from developing countries and the least developed countries fall within the unified system of tariff preferences of the Customs Union.

The list of such goods is fixed by the Customs Union Commission, a supranational body comprising of representatives of the member states.

Non-tariff restrictions

Before a Russian based company imports goods into the Customs Union, they are obliged to review their compliance with any existing limitations to the importation of certain goods to Russia (e.g. quotas, special protective, anti-dumping and compensatory measures) and obtain all necessary authorisations and licences.

In connection with non-tariff regulation, the basic trend has been to specify and facilitate the registration procedure, in particular for declaration and certification. The aim is to provide for one non-tariff restriction for conformity confirmation (registration, declaration or certification) for each product.

Exporting

Declaring procedures

When goods are exported from Russia to countries outside the Customs Union, the Russian based company must fulfil their customs clearance formalities for exported goods at an appropriate customs office within Russia.

Any goods being exported will need to comply with the relevant customs procedures. When the goods leave the customs territory of the Customs Union, customs authorities located on the border of the Customs Union make corresponding notes on the export customs declaration.

Export customs duties and payment

Export duties are to be paid to the country from which the goods originated.

Non-tariff restrictions

The member states are intending to unify the non-tariff regulation measures taken with regard to third countries. These include special protective, compensatory and anti-dumping measures, as well as sanitary and veterinary measures.

Some measures of non-tariff regulation may be introduced in the form of quantitative restrictions or as an exclusive right to export and/or import certain types of goods, which require a licence to be granted by the competent authorities of the member state.

Decisions on introducing, applying and cancelling measures of non-tariff regulation are taken by the Customs Union Commission.

VAT

Goods exported to third countries from Russia are subject to a 0% VAT rate and are exempt from excise duties, provided that the export of goods is properly documented.

Mutual trade between the Customs Union members

Free circulation of goods

Declaring procedures and customs duties

As the territories of the member states of the Customs Union form a common customs territory, there are no customs offices or customs declaration procedures between them.

Customs duties are not applicable to reciprocal trade between the member states.

Non-tariff restrictions

No restrictions of an economic nature are applicable to mutual trade between the member states, except for special protective, anti-dumping and compensatory measures.

Indirect taxation within the Customs Union

Exporting goods

Goods exported within the Customs Union (from a member state to another member state) are subject to a 0% VAT rate and are exempt from excise duties provided that the export of the goods is properly documented.

Importing goods

Goods imported from the territory of one member state to the territory of another member state are subject to indirect taxes (VAT and excise duty) in the importing state.

The indirect taxes paid on imported goods are subject to deductions in accordance with the legislation of the importing state.

Indirect tax rates, which are applicable to goods imported from the territory of one member state in the territory of another member state, must not exceed those applied to similar domestic goods.

Works and services

Works and services are subject to VAT in that member state, which is regarded as the place of provision of the services or performance of the works. For example:

— works/services related to immovable or movable property are subject to VAT in the state where this property is located;
— services in the spheres of culture, art, education, physical training, tourism, recreation and sports are subject to VAT in the country where the respective recreational, tourist,

sport, etc. facilities are located; and
— consulting, legal, accounting, auditor, designer, marketing, research and development and some other types of services are subject to VAT in the state, where the purchaser of these services is located.

In other cases not mentioned above, works and services are subject to VAT in the state where the provider of the services is located.

The tax base, the rates, the collection procedures and tax concessions vary from one member state to another.

Banking sector

Banking industry

The Russian banking industry is characterised by a large number of credit organisations (1,064 as of 1 May 2014[1]) and by a high level of concentration of capital.

The number of credit organisations has reduced in the last year. This is due to the Central Bank of Russia (the "**CBR**") switching their focus to the consolidation of credit organisations and the closer supervision of their activities.

Consequently, a number of banking licences were revoked.

As of 1 May 2014, 54.3% of the banking sector's total assets[2] were held by the top five Russian banks[3]. State-

[1] http://www.cbr.ru/analytics/bank_system/obs_1406.pdf

[2] As per footnote 1.

[3] As of 1 May 2014, the top five Russian banks in terms of net assets are Sberbank (RUB 17.8 trillion, i.e. EUR 378.7 billion); VTB (RUB 6.2 trillion, i.e. EUR 131.9 billion); Gazprombank (RUB 3.9 trillion, i.e. EUR 83 billion); VTB 24 (RUB 2.3 trillion, i.e. 48.9 billion); Rosselkhozbank (RUB 1.9 trillion, i.e. EUR 40.4 billion); http://www.banki.ru/banks/ratings/?PROPERTY_ID=10&REGION_ID=0&sort_param=rating&sort_order=ASC&IS_SHOW_GROUP=0&IS_SHOW_LIABILITIES=0&date1=2014-05-01&date2=2014-04-01

owned banks[4] continue to play a significant role in the stabilisation and development of the Russian banking sector.

Legislative and regulatory framework

The legislative framework regulating the Russian banking sector is provided under Federal Law No. 395-1 "On Banks and Banking Activities" dated 2 December 2002 (the "**Banking Law**") and Federal Law No. 86-FZ "On the Central Bank of the Russian Federation" dated 10 July 2002 (the "**CBR Law**"). Bank bankruptcy is regulated by Federal Law No. 40-FZ "On Insolvency (Bankruptcy) of Credit Organisations" dated 25 February 1999. These laws and related regulations:

- define what is a credit organisation[5];
- set out the list of banking operations and other transactions that may be performed by credit organisations;
- establish the framework for the registration and licensing of credit organisations; and
- determine the regime governing bankruptcy proceedings and the protection of credit organisations.

The CBR is legally and financially independent from the Russian Government. The CBR consists of a Moscow Head Office, which includes its Board of Directors, National Banking Council and central administrative departments, a number of regional branches in the constitutive subjects of the Russian Federation (which are called "National Banks" in certain republics), and its local departments.

Under the CBR Law and the Banking Law, the CBR is responsible for regulating banking activities and is authorised to adopt binding regulations concerning banking and currency operations. The CBR actively uses its powers, and has created a detailed and extensive body of regulation on key areas, including: capital requirements – Directive No. 1260-U dated 24 March 2003; mandatory economic ratios and reserves – Instruction No. 139-I, dated 3 December 2012, and Regulation 342-P dated 7 August 2009; currency control – Instruction No. 138-I dated 4 June 2012; and provision for losses – Regulation No. 254-P dated 26 March 2004.

From 1 September 2013, the functions of the now dissolved Federal Service for Financial Markets were transferred to the CBR. This resulted in the CBR becoming Russia's financial market mega-regulator.

Licensing and operations

Licensing

A credit organisation must be licensed by the CBR in order to conduct "banking activities", as defined under the Banking Law. Credit organisations may be incorporated either as joint-stock or

(all conversions based on a notional rate of RUB 47 = EUR 1, as used for convenience throughout this guide).

[4] Such as, Sberbank, VTB, Gazprombank, etc.

[5] Here and further, banks and non-banking credit organisations.

limited liability companies or companies with additional liability. The latter form is not often used in practice, as it provides for the joint liability of the company's owners for the company's obligations. For this reason, the majority of Russian banks are either joint-stock or limited liability companies.

The CBR may **deny the issuance** of a banking licence in the event of: (i) the non-compliance of application documents with Russian law requirements; (ii) the unsatisfactory financial standing of the founders; (iii) the non-compliance with the qualification requirements of the managers; or (iv) a member of the supervisory board (board of directors) of the proposed bank having an unsatisfactory business reputation. The CBR may **revoke** a banking licence, for example, in cases of capital inadequacy, breach of banking and other Russian law requirements (including breach of anti-money laundering regulations), for the carrying out of banking operations not stipulated in a banking licence, or the insolvency of a bank.

Acquisitions

Acquisitions in the banking sector are subject to specific banking and anti-monopoly rules.

Banking rules

According to the Banking Law, the CBR must:

— give its **prior consent** to any acquisition relating to (i) more than 10%, more than 25%, more than 50%, more than 75% or 100% of the voting shares; or (ii) more than 10%, more than 1/3, more than 50%, more than 2/3 or 100% of participatory interests, in a bank;
— give its **prior consent** when a company, group of companies or individual acquires direct or indirect control of a shareholder(s) of a credit organisation holding more than 10% of the voting shares or participation interests in the respective bank or credit institution; and
— be **notified** of an acquisition of more than 1% of the voting shares or participatory interests in a bank.

Anti-monopoly rules

Prior approval from the Federal Anti-monopoly Service (the "**FAS**") is required if the proposed acquisition relates to:

— more than 25%, more than 50% or more than 75% of the voting shares, or more than 1/3, more than 50% or more than 2/3 of participatory interests, in a credit organisation, or more than 10% of the assets of a credit organisation; and
— the target is a credit organisation whose assets exceed RUB 24 billion (EUR 510.6 million).

From 30 January 2014, the post transaction FAS notification procedure was abrogated and is no longer required for 'smaller' transactions related to credit organisations whose assets do not exceed the above threshold of RUB 24 billion.

Operations

Banks may provide a wide range of

banking operations and services. Non-banking credit organisations may only conduct a limited number of banking operations, such as maintaining accounts and processing payments on behalf of various entities.

The Banking Law provides that the following services qualify as "**banking operations**" and are subject to obtaining an appropriate CBR licence[6]:

- taking deposits from individuals and legal entities (both demand and fixed-term deposits);
- investing the deposited funds as a principal, and opening and maintaining bank accounts for individuals and legal entities;
- performing settlements in accordance with the instructions of individuals and legal entities, including correspondent banks, from/to their bank accounts;
- providing cash, cheque, promissory note, payment document handling services and over-the-counter services to individuals and legal entities;
- selling and purchasing foreign currency (including banknotes and coins);
- taking deposits in precious metals and investing them;
- issuing bank guarantees; and
- processing payments in accordance with the instructions of individuals without opening bank accounts (excluding payments by post).

In addition to banking operations, credit organisations are permitted to: (i) give suretyships for the obligations of third parties contemplating payment in cash; (ii) take assignments of rights to demand payment in monetary form; (iii) perform trust management of monetary funds and other assets for individuals and legal entities; (iv) engage in operations with precious metals (in accordance with Federal Law No. 41-FZ "On Precious Stones and Precious Metals" dated 26 March 1998 and related legislation); (v) lease special premises and safe deposit boxes to individuals and legal entities for document and valuables storage; (vi) effect leasing operations; (vii) engage in factoring operations; and (viii) provide consulting and information services. A credit organisation may enter into any other transaction in compliance with the relevant Russian legislation.

Under the Banking Law, a credit organisation cannot engage in manufacturing, commodities trading (excluding precious metals[7]) or insurance activities. However, these restrictions do not extend to any cash-settled commodity derivative transactions.

Deposit insurance

To protect individual depositors, Federal Law No. 177-FZ "On Insurance of Deposits of Individuals in the Banks of the Russian Federation" dated 23 December 2003 (the "**Deposit Insurance Law**")

[6] Which includes, among other things, a general banking licence, a licence to conduct operations in foreign currency or a licence to carry out operations with precious metals.

[7] On the basis of a licence to carry out operations with precious metals.

came into effect at the end of December 2003. It stipulates that a bank may only attract deposits from, or open accounts for, individuals if the bank is a member of the deposit insurance system.

The Deposit Insurance Law established the Agency for Insurance of Deposits (the "**Agency**"). The Agency has a supervisory role over the deposit insurance system. Its responsibilities include collecting insurance contributions, managing the funds held in mandatory insurance pools, establishing insurance premiums and monitoring insurance payments. Once a bank has been granted a retail banking licence, it is entered into the Agency's register and needs to apply to the CBR to become registered as a participant in the mandatory deposit insurance system.

Participation in the deposit insurance system is subject to a number of requirements:

— the CBR must be satisfied that the bank's financial accounts and reports are true and accurate;
— the bank must be in full compliance with the CBR's stringently monitored mandatory economic ratios (capital adequacy, liquidity, etc.);
— the bank must fully comply with the CBR ratios for the assessment of the quality of the bank's capital and assets, profitability and liquidity, in addition to the CBR's requirements for the transparency of its ownership structure, risk management system and internal control; and
— the CBR must not be conducting any enforcement actions in respect of the bank, nor must any grounds for these enforcement actions have arisen during the CBR's review of the bank's application.

Failure to satisfy these requirements, or indeed, choosing not to participate in the deposit insurance system, will result in the bank being unable to attract deposits from, or open accounts for, individuals.

Member banks pay a contribution into a deposit insurance fund. These contributions are calculated as a percentage of the average daily balance of individual deposits maintained with a particular bank, subject to an established cap. All individual depositors with deposits in member banks are entitled to 100% compensation for aggregate amounts up to RUB 700,000 (EUR 14,894).

The anti-money laundering law

Federal Law No. 115-FZ "On Combating Money Laundering and the Financing of Terrorism" (the "**Anti-Money Laundering Law**") came into force on 1 February 2002, and has been revised a number of times to reflect the global developments in this area. It is the primary legislative act in the Russian Federation aimed at preventing money laundering activities and the financing of terrorism, and is supported by numerous recommendations, binding instructions and regulations of the CBR and other authorities.

The Anti-Money Laundering Law applies to individuals and legal entities engaged in transactions with monies (and other assets) in Russia, as well as so-called 'regulated entities' and the state authorities responsible for monitoring money laundering activities in Russia. It provides for mandatory internal procedures and reporting requirements in the event of any suspicious or otherwise monitored transactions.

Financial institutions, such as banks and non-banking credit organisations, professional participants of the securities market, insurance and leasing companies, postal and other non-credit organisations that deal with the transmission of money (the "**Regulated Entities**"), are required, with limited exceptions, to perform due diligence by ascertaining the identity of a customer (and beneficiary) and monitoring transactions for suspicious activity. To ensure compliance, most Regulated Entities are obliged to develop and implement sophisticated internal regulations and procedures. They must also maintain a sufficient level of education and training on these matters for relevant employees.

The Regulated Entities must identify and report transactions of a suspicious nature to the Federal Financial Monitoring Service, a designated monitoring authority. These transactions, among others, include cash or non-cash transactions of at least RUB 600,000 (EUR 12,765) and immovable property transactions of at least RUB 3 million (EUR 63,830), or the equivalent of these amounts in foreign currency. If one of the parties to a transaction is suspected of being related to terrorist activity, the transaction is subject to mandatory control regardless of the amounts involved.

The Russian anti-money laundering legislation is consistent with the relevant international practice and provides for advanced identification and control procedures in respect of foreign publicly exposed persons (so-called 'PEPs').

The CBR may undertake preventative and/or enforcement measures in respect of a Regulated Entity involved in transactions which infringe the anti-money laundering legislation. These measures may include:

— informing the entity of the CBR's concern regarding its activities;
— suggesting that the entity provide the CBR with a programme for improvement; and
— establishing additional monitoring measures.

Enforcement measures may also include the imposition of a penalty and the withdrawal of the banking licence. The Russian Criminal Code provides for criminal liability for breaches of the legislation on anti-money laundering and this includes penalties and imprisonment for the bank's management.

Lending in Russia

We set out below a brief discussion of certain issues related to lending in Russia to companies, by banks and other companies, with particular focus on foreign currency and secured lending.

Lending documents and governing law

Russian principles of contractual law are generally permissive, allowing parties freedom to negotiate terms of credit agreements to suit their commercial requirements. In addition, under Russian conflicts of laws principles, parties to a credit agreement may generally choose a relevant foreign law as the governing law of the agreement. It is usual for credit agreements to be governed by a commonly used international law, for example English or the law of the lending entity.

However, each case should be carefully analysed to determine if there are particular enforceability issues which might arise. Care should also be taken in selecting the forum in which disputes may be heard, to ensure enforceability in Russia or abroad.

Jurisdiction

There are few jurisdictions with which Russia has an agreement for reciprocal enforcement of court judgments, or in relation to which a principle of reciprocity may apply. However, Russia is a party to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, and an arbitral award obtained in another signatory jurisdiction should be enforceable by a Russian court. For this reason, it is common to provide for the jurisdiction of international arbitration in credit agreements, although consideration of the jurisdiction of foreign courts may still be relevant, in particular if the Russian obligor has assets abroad.

Currency controls

As noted in the *Currency control* chapter on page 82, a "transaction passport" maintained with a Russian authorised bank is required for a foreign currency loan into Russia.

For payments received by a Russian company for the export of goods (the receivables in connection with which may have been secured), the exporter is required to repatriate 100% of the proceeds within the period specified in the export contract. In this respect, servicing debt offshore from export proceeds becomes problematic under Russian law. Certain exemptions apply, however, for loans which are in excess of two years, made by lenders in OECD or FATF countries.

The Russian Government may introduce requirements for Russian exporters to receive payments in Russian roubles from their export operations in respect of certain goods (services) or exports to certain countries.

Reform of the Russian security legislation

On 21 December 2013, Federal Law No. 367-FZ was enacted as part of the phased Civil Code reform to modernise the Russian security legislation (the "**Security Amendment Law**"). The Security Amendment Law introduces a number of significant legal developments as of 1 July 2014, including:

— the possibility of a pledge of funds credited to the pledgor's bank accounts (prior to this, a pledge of monetary funds or a pledge of bank account was not possible under Russian law); and
— changes affecting secured creditors' rights and introducing a 'security agent' concept.

Security interests

The choice of law for security documents usually depends on the location of the secured assets (e.g. intangible assets), or the governing law of the assets (e.g. contractual rights). In Russia, the principal form of security is a pledge, which normally is entered into in connection with identified assets. In the case of competing pledges, the first in time by creation generally has priority. The

Security Amendment Law introduces the possibility to change the priority of pledges by entering into an agreement between the pledgees or between the pledgees and the respective pledgor.

Under Russian law, a universal security instrument (such as an English law debenture) which might secure all assets of a company is generally not available. There is a security instrument called a mortgage of enterprise under Russian law which may secure real estate, movable property, inventory etc. However, because of practical difficulties in putting the security in place, it is rarely used in practice.

A company is required by law to record pledges that it grants in a "pledge book" which may be inspected, and pledges over particular types of assets (e.g. real estate, participatory interests, registered intellectual property rights) are recorded on specific public registers.

The Security Amendment Law provides for the new concept of register of notices of pledges over movable property. Starting from 1 July 2014, a pledgee and a pledgor may register a pledge in this register through a notary. Although registration is not obligatory for the parties, if they do so, they will be afforded with some benefits. The pledgee whose pledge is registered in the first place will enjoy enforcement priority rights. If a subsequent pledge is registered prior the initial pledge, the subsequent pledgee will have the first ranking security of the pledged asset.

A pledgor needs to have title to the secured assets and although the pledge can be "possessory" or "non-possessory", the secured party need not take possession of the secured assets. A pledge needs to be in writing and needs to accurately identify the pledged assets, the value of the pledge and the secured obligations. The following points are worth noting, in relation to certain types of assets:

Shares or participatory interests

A pledge of shares held directly in a joint-stock company must be registered in the joint-stock company's register (which must be held by an independent licensed company). If shares in a joint-stock company are held by a depository, then its involvement is required and the pledge is registered with the depository. In this case, the shares may not be transferred without the pledgee's consent.

For participatory interests in limited liability companies, pledges must be notarised and recorded on the public Unified State Register of Legal Entities.

Immovable property

Under Russian law, interests in land (e.g. freehold and leasehold interests) are considered "immovable property" and must be registered. Pledges (or "mortgages") over the interests must also be registered in the Unified State Register of Rights to Immovable Property and Transactions Therewith. A mortgage does not come into effect until it is registered by the relevant land registration authority.

Ships and aircraft are similarly immovable assets, and pledges over these also require registration in one of the shipping registers (depending on the type of the ship) or in the state register of rights to aircrafts respectively.

Contractual and intellectual property rights

Pledges over rights will require notice to be given to the relevant counterparties, and in some cases the consent of counterparties obtained. If intellectual property rights are registered, the pledge will require registration with the relevant intellectual property register.

Bank accounts

Traditionally, under Russian law, it was not generally considered possible to take effective security by way of pledge over a bank account. As an alternative, a practice developed to enter into account withdrawal (direct debit) agreements between creditor, debtor and debtor's account bank. These agreements have a number of practical limitations, and it is preferable (if appropriate) to sweep funds to offshore accounts where security may be available.

As mentioned above, the Security Amendment Law allows for the pledge of funds credited to the pledgor's bank account. For these purposes a pledgor will have to open and maintain a specific pledge bank account. All required banking regulations to this end are not in place as of writing and are being developed by the Central Bank of Russia.

Security trusts and syndication

Under secured syndicated credit agreements, it is common for security to be held by a representative (i.e. a security agent or trustee) for a syndicate. The concept of security agent was alien to Russian law up until the adoption of the Security Amendment Law.

Because of the lack of recognition of trust concepts in Russia and the accessory nature of Russian security, syndication of credit agreements has been commonly structured to minimise disruption to Russian security upon changes to the syndicate.

The following arrangements have been commonly used:

— bilateral (fronting bank) structures (syndicated through sub-participation);
— parallel debt (creating a parallel obligation to benefit a security agent or trustee); and
— joint and several creditor structures.

However, the above structures have their own deficiencies and should be carefully analysed.

The introduction of the concept of the security agent by the Security Amendment Law could change local syndication practice, but this is likely to require clarifications from the courts and the adoption of further legislation. Under the new provisions, a creditor or any third party may, under a pledge management agreement, act as a security agent in favour of all the

creditors. The security agent will enter into pledge agreements on behalf of all the creditors. To enforce their security, creditors will have to act through the security agent; they may not do so individually.

Enforcement

Enforcement was historically carried out by way of public auction through the Russian courts. Changes to the law in 2009 introduced a wider range of out-of-court enforcement options which may be included in an agreement. These measures include (i) the possibility of a direct or commission sale of the assets; (ii) or a creditor appropriating title to the secured assets (whereas previously only proceeds were available).

To allow out-of-court enforcement the relevant pledge agreement must be notarised, unless the pledged asset is to be held by the pledgee.

However, in the case of a dispute between a pledgor and a pledgee, it is likely that any provision for out-of-court enforcement would be referred to the court's jurisdiction. Proceeds from enforcement through the court would be likely to be in Russian roubles.

Bank guarantee and suretyship

Under Russian law, a "bank guarantee" refers to a particular type of commercial instrument that a bank may issue as credit support for the debtor's obligations. A "suretyship" refers to a particular type of instrument that a company (or individual) may issue as credit support for the obligations of another. A bank guarantee is the only Russian law instrument which is not "accessory" in its nature and survives the underlying obligation. Russian law bank guarantees and suretyships are commonly used in connection with financing in Russia. In addition, providing there is a sufficient foreign element to a transaction, a similar foreign law instrument may be issued by a Russian obligor (utilising appropriate jurisdiction provisions).

The Russian legislator intends to create an independent guarantee which will not be accessory to the underlying obligation, but the timing of the adoption of the required legislative changes is unclear.

Bankruptcy considerations

Upon the bankruptcy of a debtor or pledgor, a moratorium against enforcement of security will arise whilst it is determined if financial rehabilitation, external administration or bankruptcy liquidation will apply. Repayments or arrangements in preference of other creditors are likely to be subject to anti-preference provisions set out in the bankruptcy laws. For more information related to bankruptcy and insolvency in Russia generally, please see the *Corporate bankruptcy* chapter on page 84.

When a bankrupt company is being liquidated (at the bankruptcy liquidation

stage of bankruptcy proceedings), Russian law applies **mandatory priorities** under which creditors of the same class would rank equally. In brief these are: (i) "first priority claims" (personal injury); (ii) "second priority claims" (employee related, royalties); and (iii) "third priority claims" (all other claims, including tax liabilities). So-called "current claims" (e.g. insolvency costs, obligations incurred after the company was declared bankrupt by the relevant commercial court) are not included into the order of priorities and should be satisfied as they fall due.

Secured creditors fall within the category of "third priority claims"; however their claims are satisfied in accordance with a special procedure quite separate from unsecured creditors, i.e. out of the proceeds of the sale of the pledged or mortgaged assets, subject to the following statutory thresholds of recovery.

In connection with secured claims (other than under a credit agreement), a secured creditor is entitled to 70% of the proceeds from the enforcement of the relevant security, with the remaining 20% for first and second priority claims, and 10% for insolvency expenses. In connection with secured claims under a credit agreement, these percentages change to 80%, 15% and 5% respectively.

At financial rehabilitation or external administration stage, to become entitled to enforce security, a secured creditor needs to waive its rights to vote at creditors meetings. In that case, Russian law allows this secured creditor, with the approval of the relevant commercial court and provided that the assets of the debtor are insufficient for the possible restoration of its solvency, to enforce its security and retain all the proceeds of such enforcement (ahead of the general liquidation of the debtor's assets, which is usually undertaken during the last possible stage of the bankruptcy proceedings, namely bankruptcy liquidation).

Other lending related issues

Finally, the following additional aspects should also be kept in consideration when lending or borrowing in Russia.

Corporate capacity and authority

As a general rule, the general director, or any person acting under properly delegated authority (by way of a power of attorney), has the capacity to bind the company.

If the transaction value equals or exceeds 25% of the balance sheet asset value of the company (and no lower threshold is provided for in the charter), the transaction will constitute a "major transaction". If the value is between 25% and 50% of this balance sheet value, unanimous approval of the board of directors would be required, and if over 50%, approval of a 75% majority of shareholders would be required for a joint-stock company. Similar rules would generally apply to a limited liability company unless they are varied in its charter.

If the transaction constitutes an "interested party transaction" (e.g. it may involve affiliates, or cross-management) particular care needs to be exercised in order to obtain appropriate approvals from majorities of, as the case may be, disinterested directors or shareholders/participants.

Regulatory considerations on enforcement

When taking security over company shares (either directly in Russia or through an offshore holding company, under a foreign law), two key aspects must be considered:

— With regards to enforcement of the security, ownership of the Russian entity may be restricted as "strategic" under Federal Law No. 57-FZ "On the Procedure for Foreign Investments in Commercial Organisations of Strategic Importance for the National Security of the Russian Federation" dated 29 April 2008. For more details please see the *Common forms of business structures for foreign investors* chapter on page 32.
— Ownership may also need approval from the Federal Anti-monopoly Service under Federal Law No. 135-FZ "On Protection of Competition" dated 26 July 2006. For more details please see the *Anti-monopoly issues* chapter on page 38.

Currency control

General approach

Most currency restrictions in Russia were removed in January 2007, following amendments to Federal Law No. 173-FZ "On Currency Regulation and Currency Control" dated 10 December 2003 (the "**Currency Law**"), which regulates currency transactions. Consequently, most currency transactions can be conducted without limitation.

However, the Currency Law, and related regulations, still contain a number of restrictions which should be considered (i) when dealing with transactions between residents and non-residents (in particular when importing and exporting goods and capital); and (ii) when importing and exporting foreign currency in cash.

Foreign currency transactions

Foreign currency transactions between residents

The following persons are considered to be "residents":

— citizens of the Russian Federation, except those who are (or are considered to be) living abroad for a period of at least one year;
— foreign nationals and stateless individuals who live permanently in Russia on the basis of a residence permit;
— legal entities duly registered under Russian law;
— diplomatic representatives, consular offices and other official representatives of the Russian Federation; and
— the Government of the Russian Federation, regions and municipal units of the Russian Federation.

Generally, foreign currency operations between residents are prohibited, although there are some exceptions. For example residents may borrow from, and then repay to, Russian banks in foreign currency. Contracts in Russia may be concluded in foreign currencies. However, the actual payment must be made in roubles. This can lead to exchange rate differentials, which may arise between the date the transaction is entered into and the payment date.

As a result of amendments made to the Currency Law in 2013, certain transfers of foreign currency and roubles are now deemed to be currency operations, with the effect that certain limitations exist for residents when transferring funds from their accounts, whether held in Russia or abroad, to either accounts they hold abroad or to those held by third parties.

In addition, certain residents of the Russian Federation have been prohibited from opening accounts abroad, holding currency or valuables in foreign banks or entering into foreign financial instruments. This prohibition applies to individuals holding the highest state, federal, regional or municipal official positions (such as the President of the Russian Federation, members of the Government, ministers, members of the highest legislative bodies and highest courts), their spouses and minor children.

Foreign currency transactions between non-residents

The following persons are considered to be "non-residents":

— individuals who do not qualify as residents;
— citizens of the Russian Federation living abroad for a period of at least one year;
— legal entities and all other organisations that are registered under the legislation of a foreign jurisdiction and located outside the Russian Federation;
— Russia-located representative offices and branches of legal entities or other organisations registered under the legislation of a foreign jurisdiction and located outside the Russian Federation; and
— diplomatic representatives, consular offices and other official representatives of foreign countries, as well as international and intergovernmental organisations that are located in the Russian Federation.

Payments in any currency are permitted without restriction between non-residents, provided that any such payments

in Russian roubles in the territory of the Russian Federation are made to and from those non-residents' accounts opened with Russian authorised banks[1]. Settlement of the purchase and sale of securities transactions between non-residents is also permitted, although it can be subject to Russian securities market and anti-monopoly regulations.

Foreign currency transactions between residents and non-residents

Generally, foreign currency transactions between residents and non-residents are also permitted without any restrictions. However, "transaction passports", which record foreign currency flows through Russian authorised banks, are required to be filed and maintained with an authorised bank (where the resident's account is opened) for all transactions involving the import or export of goods, loans, the provision of services and intellectual property between residents and non-residents. Under the transaction passport (and as part of its regular reporting), the bank reports the receipt and repayment of the currency to the Central Bank of Russia (the "**CBR**").

In 2011 and 2012, the Currency Law and related regulations were amended to ease transaction passport requirements. In particular, the requirement of having such a passport for cross-border transactions, including cross-border loan transactions, with a value of up to USD 50,000 (or its equivalent in another currency) was dropped.

[1] Credit organisations holding a CBR licence for conducting operations in a foreign currency.

Residents must repatriate, with certain exceptions, roubles and foreign currency received from international trade and commercial activities to their bank accounts held with Russian authorised banks. Among the exceptions are payments due to a non-resident lender. These payments may be directly transferred into the lender's foreign bank account.

In May 2014, the Russian Government decided to implement a requirement that a portion of export proceeds must be received by Russian companies in roubles. The Currency Law was amended on 5 May 2014 and now provides that the Government may determine (i) the portion of the export proceeds that must be received by the residents in roubles; (ii) a list of goods and services to which such requirement applies; and (iii) a list of countries, with residents of which a Russian resident will be obliged to enter into an export operation with such mandatory rouble part payment. At the current time, there is no information indicating whether the Russian Government is intending to prepare these lists or when it expects to do so.

Import and export of foreign currency in cash

Residents and non-residents can import and export foreign currency in cash subject to the following rules:

Up to and equal to USD 10,000	No restriction
Over USD 10,000	Subject to a written customs declaration

Sanctions

Breaching the currency control rules can result in administrative and criminal sanctions.

The Russian Code on Administrative Offences provides for administrative fines for illegal currency transactions that can range from 75% to 100% of the value of the relevant transaction.

In addition, this Code prescribes fines for failing to:

— notify the tax authorities when opening or changing details of accounts held with banks located outside Russia;
— comply with the time periods and/or form of notification required when opening or changing details of accounts in banks located outside Russia;
— repatriate funds to accounts held in Russia in due time where required by law; and
— comply with rules for providing information or documents in relation to currency operations.

Breaches of these rules can result in penalties of up to RUB 5,000 (EUR 106[2]) for individuals, up to RUB 50,000 (EUR 1,064) for company officials, up to RUB 1million (EUR 21,276) for legal entities and, in certain cases, fines ranging from 75% to 100% of the value of the relevant transaction.

More serious criminal sanctions may apply under the Russian Criminal Code. In particular, it stipulates that persons failing to repatriate foreign currency over RUB 30 million (EUR 638,298) to accounts in Russia, where required by law, may face deprivation of liberty, compulsory labour or imprisonment in each case for a term of up to five years.

[2] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience throughout this guide.

Corporate bankruptcy

General approach

The discussion in this chapter focuses on the Russian bankruptcy regime applicable to companies. The most important laws governing corporate bankruptcy proceedings are (i) Part I of the Russian Civil Code; (ii) Federal Law No. 127-FZ "On Insolvency (Bankruptcy)" dated 26 October 2002, which is the principal piece of legislation on bankruptcy in Russia (the "**Insolvency Law**"); and (iii) Regulation No. 257 of the Russian Government dated 29 May 2004.

There are no specific bodies responsible for conducting or overseeing bankruptcies in Russia. Bankruptcy proceedings are generally conducted by a Russian commercial court in the region where debtor's registered office is located.

The Insolvency Law and the Russian bankruptcy legislation in general have not been significantly amended so far in connection with the current reform of the civil law. In particular, the recent amendments to the Civil Code (including those that yet have to enter into force) have not affected the insolvency (bankruptcy) of

corporate entities in Russia. At the current time, there is no information on whether the Russian legislative bodies or the Government are intending to prepare any significant amendments to the Russian bankruptcy legislation.

Insolvency test

Under the Insolvency Law, the main test which is used to determine whether a debtor is insolvent is the debtor's inability to meet creditors' claims or fulfil mandatory payment obligations within three months from the date on which they were due.

Stages of bankruptcy proceedings

Depending on the insolvent company's circumstances, five stages of bankruptcy proceedings may apply:

— supervision;
— financial rehabilitation;
— external administration;
— bankruptcy liquidation; and
— a voluntary arrangement.

Preliminary step: initiating bankruptcy proceedings

As a general rule, bankruptcy proceedings may be commenced against all types of legal entities, with the exception of certain forms of state-owned enterprises, political parties and religious organisations.

The following are permitted to file an application, in the form of a bankruptcy petition, with a court to have a debtor declared bankrupt:

— the debtor itself;
— a bankruptcy creditor; or
— a federal executive body authorised by the Russian Government[1].

A debtor must file a bankruptcy petition with a commercial court to initiate bankruptcy proceedings if one of the insolvency criteria below is met:

— if the claims of one or more creditors are fulfilled, the debtor will be unable to fulfil its payment obligations towards other creditors;
— persons who are authorised to take a decision to apply for liquidation on behalf of the debtor decide to petition the court for the commencement of bankruptcy proceedings;
— if claims against the debtor's assets are enforced, the debtor will be unable to continue, or significantly restricted in continuing, its operations;
— the debtor meets the "inability to pay" criterion (i.e. the debtor fails to perform its payment obligations when due as a result of an insufficiency of funds); and/or
— the debtor meets the "asset insufficiency" criterion (the value of the debtor's payment obligations exceed the value of its assets).

A bankruptcy creditor or an authorised government body may file a bankruptcy petition with a commercial court to initiate bankruptcy proceedings if:

— an unsatisfied aggregate debt of the debtor exceeds RUB 100,000 (EUR 2,128[2]) which is confirmed by a

[1] The Federal Tax Service of the Russian Federation.
[2] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience throughout this guide.

court decision or an arbitral award that has entered into force; and
— one of the above insolvency criteria are fulfilled (i.e. there is evidence that the debtor is insolvent).

Initiation of the bankruptcy proceedings is not automatic and the relevant applicant, being a creditor or a debtor itself, must prove to the court that the debtor is insolvent.

Supervision

Supervision is a provisional stage of bankruptcy proceedings which operates via temporary managers. They supervise the management bodies of the debtor which remain in place. Supervision aims to (i) preserve the debtor's property; (ii) analyse its financial state; (iii) complete a creditors register; and (iv) hold the first creditors meeting.

This provisional stage commences when the court rules that a bankruptcy petition is well founded, introduces supervision and approves the appointment of a temporary manager (and the amount and source of his/her remuneration). The court may also impose interim measures alongside accepting the bankruptcy petition. The court's rulings must be executed immediately. However, even though the rulings may be appealed, the appeal process will not halt the execution of the court's ruling.

Restrictions

As of the date of the court's ruling, the debtor's business will be restricted as follows:

— Creditors' claims are to be submitted only through the commercial court supervising the bankruptcy proceedings. That court decides on their inclusion in the creditors register maintained by the temporary manager (including the amount of the claim).
— The debtor is prohibited from repaying profits and dividends, as well as effecting set-offs that violate the order of priorities established in the Insolvency Law. The debtor may not alienate or purchase shares, place securities (excluding shares), reorganise its company structure or incorporate subsidiaries.
— Any property transactions with a value exceeding 5% of the debtor's balance sheet value and any credit-related transactions are only permissible with the prior written consent of the temporary manager.

The debtor is entitled to increase its registered capital through a private placement of additional ordinary shares. However, it is not permissible to perform an increase in a company's registered capital in order to cover losses. The debtor's shareholders or third parties may repay the full amount of the creditors' claims according to the creditors register.

Temporary manager

The temporary manager is nominated from members of a self-regulated organisation of insolvency practitioners. The party filing the bankruptcy petition must suggest the self-regulated organisation or nominate an individual from that organisation. Where the party

filing the bankruptcy petition does not suggest an individual, the temporary manager is nominated by the self-regulated organisation of insolvency practitioners. In both circumstances the appointment is subject to commercial court approval.

The duties of the temporary manager involve (amongst other things) (i) preserving the debtor's property; (ii) analysing its financial state; (iii) revealing the identity of all creditors; (iv) calling the first creditors meeting; and (v) notifying creditors of the introduction of supervision.

The temporary manager is entitled to, amongst other actions, seek injunctions to preserve the debtor's assets, obtain information from the debtor, obtain documents relating to the debtor's activities, claim before a court that transactions made by the debtor are invalid, request a court to remove a director and challenge any claims brought by a creditor.

Termination of supervision

Supervision is terminated on the date a court makes a ruling to that effect. Possible outcomes could be the termination of the bankruptcy proceedings if the debtor's solvency has been restored or the introduction of one of the following stages of bankruptcy proceedings: (i) financial rehabilitation; (ii) external management; (iii) bankruptcy liquidation; or (iv) voluntary arrangement (as applicable). Under the Insolvency Law supervision is to be conducted within a seven months period starting from the date of initiation of supervision and ending with the first creditors meeting deciding on the next stage of the bankruptcy proceedings (subject to confirmation by a commercial court). If the creditors are unable to make a decision, the court will make a ruling and introduce the next stage of bankruptcy proceedings (if necessary) at its own discretion.

Financial rehabilitation

This procedure aims to restore the debtor's solvency and to schedule repayment of the outstanding debts. Financial rehabilitation may last up to two years and commences immediately upon a court's ruling.

Financial rehabilitation proposal

A debtor or a third party can propose financial rehabilitation at the first creditors meeting. The proposal differs depending on the party applying, but it will include at least: a financial rehabilitation plan, a debt repayment schedule, information on the security offered for performance of the debtor's obligations under the debt repayment schedule, and, in the case of a debtor's proposal, minutes from the general meeting of shareholders/participants authorising the decision.

Administrative manager

When the court initiates financial rehabilitation on the basis of a decision of the creditors meeting, an administrative manager will also be approved by the court. The role of the administrative manager predominantly involves monitoring the existing management

bodies of the debtor which remain in place. His/her key duties include: (i) maintaining a register of creditors' claims; (ii) examining reports on the progress of the financial rehabilitation plan; (iii) monitoring the debtor's discharge of current claims; and (iv) enforcing the performance of guarantees.

The powers of the administrative manager are generally similar to those of the temporary manager.

Restrictions

The following restrictions will take effect from the date of the court's ruling to approve financial rehabilitation:

- Monetary and property claims are only to be submitted to the debtor within the bankruptcy proceedings supervised by a commercial court.
- Previously introduced interim measures will be cancelled.
- Penalties will not accumulate further (and they will relate to the last point of the indebtedness repayment schedule).
- Setting-off counter claim(s), alienating or purchasing shares or property, and allocating profits and dividends are prohibited.

The debtor must obtain the consent of a creditors meeting in order to perform the following: (i) interested party transactions; (ii) property transactions with value exceeding 5% of the debtor's balance sheet value; (iii) issuing credit and guarantees; and (iv) any decisions about its reorganisation and the incorporation of subsidiaries.

An administrative manager's consent is necessary for transactions which increase the debtor's level of indebtedness by more than 5%, any sale and purchase of the debtor's property, succession and borrowings.

External administration

This stage of bankruptcy proceedings intends to restore the debtor's solvency and may last up to 18 months (with a possible six-month extension). The combined duration of financial rehabilitation and external administration may not exceed two years. External administration commences upon a court ruling, which is based upon the decision of a creditors meeting.

External manager

The court approves the appointment of an external manager when it decides to introduce external administration.

Amongst other actions, the external manager is entitled to:

- manage the debtor's property;
- make settlements on behalf of the debtor;
- challenge the validity of the debtor's transactions and claim any resulting damages before a court;
- refuse to perform a debtor's transaction, when this transaction was not performed earlier in full or in part, if it creates a loss in comparison with other transactions;
- challenge creditors' claims; and
- comply with the external administration plan and report on compliance to the creditors meetings.

The external manager's authority is terminated on the date of the court appoints an insolvency manager (when the debtor is declared bankrupt), or the appointment of a new head of the debtor (when bankruptcy proceedings are terminated if debtor's solvency is restored).

Restrictions

When external administration is introduced, the authority of the debtor's general director is terminated and transferred to the external manager. However, the debtor's management is afforded limited powers relating to transactions concerning capital, additional share issues and entry into specified major transactions (subject to creditors meeting consent).

A wide-ranging moratorium is imposed upon satisfaction of creditors' claims (excluding current payments).

Similar to the financial rehabilitation stage, interim measures which have been introduced earlier are cancelled. Monetary and property claims (including mandatory payments) may only be submitted within bankruptcy proceedings which are supervised by a commercial court.

Termination

External administration will be terminated prematurely if the debtor discharges all creditors' claims.

Following the external manager's report, the creditors meeting will adopt one of the following decisions by making a petition before the court to:

- terminate the external administration on the ground that the debtor has been restored to solvency and to proceed with paying creditors' claims;
- terminate the external administration on the basis that all registered claims have been satisfied;
- declare the debtor bankrupt and start bankruptcy liquidation;
- consent to a voluntary arrangement; or
- extend the term of the external administration.

The court will evaluate the external manager's report. If the court considers it to be justified, it will approve it and make a ruling on the introduction of the next stage of proceedings which can only be in the form of bankruptcy liquidation.

Bankruptcy liquidation

This stage of bankruptcy proceedings is designed to satisfy creditors' claims through the sale of the debtor's assets. Bankruptcy liquidation can be instituted for up to six months (with a possible further six-month extension).

Consequences

The immediate effects of the bankruptcy liquidation include the following:

- Monetary obligations and mandatory payments of the debtor are accelerated by virtue of statute.
- Interest no longer accrues. The same applies to financial (or other) sanctions arising from a failure to fulfil monetary obligations and mandatory payments (other than current payments).

— Information on the debtor's financial state is no longer deemed to be confidential.
— Existing attachments over the debtor's property are removed and no further attachments are allowed.
— The powers of the debtor's general director and board of directors are terminated and vested in the insolvency manager.

Bankruptcy manager

The court appoints a bankruptcy manager when a ruling for bankruptcy liquidation is issued. The bankruptcy manager acts until the bankruptcy liquidation is completed.

The principal role of the bankruptcy manager is to search, return, evaluate, pool and arrange for a sale of the debtor's assets, and to make settlements with creditors. The bankruptcy manager also dismisses the debtor's employees. The bankruptcy manager assumes the powers of the debtor's general director, board of directors and meeting of shareholders/participants. The bankruptcy manager must publish notice of the debtor's bankruptcy within ten days of his/her appointment.

Bankruptcy liquidation: order of priorities

The Insolvency Law provides a specific priority order in which creditors' claims are to be satisfied. The priority order includes first, second and third priority claims.

Current claims (i.e. creditor claims made after the court's acceptance of the bankruptcy petition) are not included in the order of priorities as such and should be satisfied when they become due.

Current claims are satisfied in the following order: (i) judicial expenses and remuneration of persons involved in administering the bankruptcy proceedings; (ii) remuneration of employees as well as contractors engaged for the purposes of the bankruptcy proceedings; (iii) operational expenses; and (iv) other current claims.

First priority claims include personal injury claims and moral damage claims. **Second priority claims** include: (i) severance benefits; (ii) the wages of the debtor's employees; and (iii) copyright royalties. **Third priority claims** include all other claims (both secured and unsecured, where secured claims mean claims secured by a pledge or a mortgage). Notwithstanding that the claims of secured creditors are accounted for in the third priority, they are satisfied in accordance with a special procedure largely separate to the unsecured creditors, i.e. out of the proceeds of the sale of the pledged or mortgaged assets. The Insolvency Law has been recently amended to ensure that pledges over bank accounts, a new type of pledge provided in the Civil Code, remain enforceable during bankruptcy.

Possible transition to external administration

Where the financial rehabilitation or external administration stages have not previously been instituted, the creditors meeting may petition the court for a transition to the external administration

stage during the bankruptcy liquidation stage. To do so, grounds must exist to believe that the debtor's solvency can be restored, and these must be backed by financial data. The transition will only be permitted if the debtor has sufficient assets to pursue independent economic activity.

Liquidation (close-out) netting

In August 2011, liquidation netting after the commencement of bankruptcy proceedings was introduced in Russian law. Since then, obligations under qualifying financial agreements that are concluded on the basis of master agreements (derivative or repo), stock exchange trading rules or clearing rules are terminated in accordance with the terms of these agreements, stock exchange trading rules or clearing rules. This leads to the determination of a close-out amount which is calculated in accordance with the terms of the relevant master agreement, stock exchange trading rules or clearing rules, and whose calculation can be made using close-out netting.

If a master agreement is entered into, the Insolvency Law stipulates additional requirements. These criteria apply to domestic and cross-border transactions and agreements.

The above rules are applicable to financial agreements concluded prior to temporary administration or prior to the implementation of one of the stages of bankruptcy proceedings.

Voluntary arrangement

A voluntary arrangement can be entered into by the creditors and the debtor at any stage of the bankruptcy proceedings, in order to terminate such proceedings and give effect to an agreement between the debtor and the creditors. The debtor, creditors, third parties and authorised bodies are entitled to enter into a voluntary arrangement.

The decision to enter into a voluntary arrangement with the creditors or an authorised body must be approved at a creditors meeting. The voluntary arrangement requires subsequent approval of the relevant commercial court.

A voluntary arrangement can only be terminated by a court, and only in respect of all creditors and/or authorised bodies. An application for termination may be put forward by creditors and/or authorised bodies which hold at least a quarter of the value of creditors' claims on the date the voluntary arrangement was entered into.

The parties are entitled to file for the termination of the voluntary arrangement when the debtor defaults or significantly violates the terms of the voluntary arrangement.

Employment/Migration

General approach

The Labour Code of 30 December 2001 (the "**Labour Code**") outlines the main provisions applicable to employment arrangements in Russia, along with numerous decrees and instructions, as approved by the competent state authorities. The main law regulating migration matters in the country is Federal Law No. 115-FZ "On the Legal Status of Foreign Citizens on the Territory of the Russian Federation" dated 25 July 2002.

The main employment law developments in 2013 and first half of 2014 (all of which are reflected in the relevant sections below) were:

— amendments to the Labour Code allowing distant work, where employees may work remotely, outside the primary location of the employer or its branch/representative offices, via IT networks, including the Internet ("**Teleworkers**"). The relevant practice in respect of Teleworkers has yet to be developed;
— work councils;

— new rules on the compulsory assessment of working conditions;
— limitations to outstaffing; and
— increasing the liability of employers for violations of labour legislation.

Below is a general description of employment law provisions as they apply to all employees, as well as how they apply to foreign employees specifically.

Formalising the employment relationship

Independent contractor vs. employee

An employing company can hire an individual to perform specific work under a civil-law services contract or an employment contract. The employing company's choice directly affects the legal status of both parties.

Provisions in an employment contract are regulated by the Labour Code, whilst those in a civil-law services contract are governed by the Russian Civil Code.

When an employer hires an employee under an employment contract, the law imposes numerous duties on the employer, including the duty to provide the employee with social security guarantees.

If hired under a civil-law services contract, an individual performs work for a customer (i.e. his/her 'employer') at his/her own risk. This is one of the most significant differences between the two types of contracts.

Even if the parties have agreed to act under a civil-law services contract, the court may find, in the event of a dispute, that the civil-law services contract constitutes actual employment because of the nature of the parties' relationships. In such event, the court may determine that employment law rules apply to a civil-law services contract.

Outstaffing

In May 2014, after several years of debates, a law, which substantially limits outstaffing in Russia, was finally enacted. The law, which comes into force on 1 January 2016, provides a general prohibition on the use of outstaffed labour, subject to certain exceptions.

Outstaffed personnel can only be provided by (i) accredited private employment agencies to fill temporary vacancies; and (ii) legal entities (including foreign legal entities and their affiliates) that second their employees to an affiliate or to another company which is a party to a shareholders agreement with the seconding entity.

Employment contract

The Labour Code stipulates that employment contracts must be concluded in writing (except for Teleworkers with whom it is possible to conclude the agreement electronically, i.e. using electronic digital signatures) and contain certain mandatory terms and conditions. Such mandatory terms include the place of work, position, duties, commencement date, the duration of employment (if applicable), remuneration and a work schedule. Employment contracts may contain additional terms and conditions,

such as probationary periods and confidentiality clauses.

The parties' rights and obligations under the employment contract must comply with the minimum requirements set by law. An individual employment contract must not result in an employee's terms and conditions of employment being worse than the terms and conditions of employment stipulated under the overriding requirements of employment law; otherwise, the legislation will supersede the provisions of the respective employee's contract.

Duration

Employment contracts may be concluded for an indefinite term or for a fixed term; the duration of a fixed-term contract may not exceed five years.

The law provides for only a limited number of grounds when an employment contract may be concluded for a fixed term. These include, in particular, the following:

— an employee replacing a temporarily absent employee;
— temporary, project-related or seasonal employees;
— directors, deputy directors or chief accountants;
— employees of companies created for a specific term and purpose; and
— an employee hired as part of a training programme ("*stazhirovka*").

If a fixed-term contract is concluded in breach of the Labour Code, a court may declare the contract to be concluded for an indefinite term.

Salary

The national minimum wage (i.e. an employee's gross monthly remuneration) is set at RUB 5,554 (EUR 118[1]), as established by law and is subject to regional coefficients determined by agreements between the regional authorities and employers. For example, as of 1 January 2014, the minimum monthly salary in Moscow was increased to RUB 12,600 (EUR 268), and from 1 July 2014 it will amount to RUB 12,850 (EUR 273). A salary is to be paid in roubles and in at least two instalments per month.

If salary payments are delayed by more than 15 days, an employee has the right to suspend work upon written notification to his/her employer.

Criminal sanctions may be imposed on the employing company's officials if salaries are not paid in full for over two months. Sanctions may include a fine of up to RUB 500,000 (EUR 10,638); a ban from holding a management position for up to three years; and/or imprisonment for a period of up to three years. Partial non-payment of salaries for over three months carries similar but lighter criminal sanctions.

Probationary period

An employment contract may provide for a probationary period, which must not exceed three months. For directors, deputy directors, chief accountants, deputy chief accountants and directors of representative offices, branches or

[1] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience throughout this guide.

other divisions, a longer probationary period may be provided. This longer period must not exceed six months.

If an employee does not meet his/her employer's requirements, the employer may terminate the contract by giving three days' prior written notice and providing, in writing, a substantiated reason for terminating the contract. The employee may also terminate the contract with three days' prior notice, without reason.

Terminating a contract for failing to pass the probationary period is not permitted for pregnant women, women with children under the age of three years, women and men who are the sole providers for children under three years of age in families with three or more children under fourteen years of age, minors, graduates and certain other categories of employees.

Working hours and leaves

A normal working week is 40 hours. Overtime is permitted upon the employer's written request and, as a rule, requires the employee's consent. Overtime may not exceed a total of four hours in two consecutive days and is limited to 120 hours in total per year.

An open-ended working day regime may be established for certain categories of employees, if set out in the employer's internal regulations and relevant employment contracts. This type of working day regime entails the employee being periodically engaged in additional work upon the written request of the employer without requiring the employee's written consent. Under this regime, the overtime work does not result in additional paid remuneration but does provide the employee with at least three additional days of leave per year.

The statutory annual paid leave for all employees is 28 calendar days. In certain cases expressly stated in the Labour Code, employees are entitled to additional paid leave.

Confidentiality obligation imposed on the employee

Russian law does not contain express provisions imposing confidentiality obligations on employees. If an employer wishes its employees to be subject to this type of obligation, it must (i) incorporate a confidentiality undertaking in the employment agreement of each employee concerned; (ii) adopt a set of internal regulations specifying the procedures for processing and obtaining access to confidential information; and (iii) implement the confidentiality regime provided for by law (i.e. use of safes, stamp "secret", etc.). In the absence of these measures, it will be almost impossible to hold an employee liable in the event of disclosure.

Restrictive covenants

Generally, Russian legal practice remains critical of the use of various restrictive covenants in employment agreements. For instance, non-competition clauses, though not directly prohibited by Russian law, are deemed unenforceable by the courts, as they are seen as violating an employee's constitutional

right to work. Certain practitioners advocate the legalisation of non-competition clauses analogous to what is seen in some foreign jurisdictions; however, it cannot be said that this train of thought enjoys wide support.

Another example is the narrow scope of the application of the 'garden leave' concept (i.e. the practice by which a dismissed employee is instructed to stay away from work during his/her notice period). The Labour Code prohibits discharging an employee from further obligations under his/her employment contract at the employer's discretion, except for a limited number of instances provided in the Labour Code. These exceptions are generally treated as the discharge of an employee from performing his/her work obligations in circumstances where there is a threat to a person's health, life or property.

Liability

Liability of the employee

An employee who breaches obligations contained in his/her employment contract may be subject to disciplinary sanctions and/or bear material liability.

The Labour Code strictly regulates **disciplinary sanctions**, and consequently sanctions may not be varied by an employment contract.

An employee's **material liability** is generally restricted to compensation for the direct damage caused to the employer's property by the employee's fault or negligence. This liability is limited to an amount equivalent to the employee's monthly salary.

However, the Labour Code sets out some exceptions to the limitation of material liability rule. It provides that an employer may, under certain conditions, impose full material liability where an employee:

- fails to protect valuable items entrusted to him/her, as evidenced by documents signed by the employee;
- intentionally damages property;
- causes damage when in a state of alcoholic, drug or other intoxication;
- causes damage as a result of criminal actions for which he/she has been sentenced by a court;
- causes damage as a result of an administrative offence as determined by the relevant state body;
- divulges confidential information;
- causes damage outside of his/her work duties; and/or
- has entered into an individual or a collective agreement on full material liability with the employer.

Full material liability extends to all damage incurred by the employer as a result of the fault of the employee.

Also, in the employment contract, an employer may provide for full material liability for certain categories of employees (e.g. chief accountant, deputy general director, etc.). The general director of a legal entity is always subject to full material liability regardless of whether his/her employment contract includes such a provision.

If the employer wishes to be compensated for the damage it suffered, it

must follow a specific procedure and request from the employee a written explanation of the cause of the damage. Following this, the employer must specify the amount and cause of any damage inflicted within one month of the alleged damage having occurred. If the employer does not exercise its right within this time period, compensation may only be recovered with the voluntary consent of the employee or through legal proceedings.

Liability of the employer

The range and scope of an employer's liability is relatively wide, as the relevant legislation is designed to provide an employee, as the weaker party in the employment relationship, with a greater degree of protection.

The employer is liable for violating contractual obligations which are statutory requirements (i.e. liability for breaching contractual obligations is established by law, not by the parties). The employer's liability is two-fold: if the employer commits a single violation, it must (i) compensate the employee for all damage and loss; and (ii) bear any administrative or criminal liability.

(i) The employer must compensate for all damage sustained by the employee in full. In a certain number of cases, losses and moral damages may also be compensated for.

(ii) Depending on the seriousness of the breach, the employer or its officers (including the CEO or the person responsible for labour and/or migration compliance in the company) can be held administratively or criminally liable. The Code on Administrative Offences provides for a penalty of RUB 1,000 - 5,000 (EUR 21 - 106) to be imposed on the relevant officer(s) and a penalty of RUB 30,000 - 50,000 (EUR 638 - 1,064) to be imposed on the employer itself. In addition, a Russian court may order the administrative suspension of the company's activities for up to 90 days. In practice, the latter sanction is usually imposed when statutory work safety rules are breached and such breaches put the life and health of employees at risk of harm. Punishment under Russian criminal law is usually imposed when the violation is either gross or entailed, or could have entailed, serious bodily harm or death. As legal entities cannot be held criminally liable under Russian law, criminal liability will be imposed on the employer's officers and administrators.

Labour book

Russian employment law requires employers to keep, sign and seal a labour book *("trudovaya knizhka")* for any employee who works for more than five days with the same employer.

The labour book includes, among other things, records of the employee's employment positions and grounds for termination of the employment contracts with previous employers. Where the employee is a Teleworker, the Teleworker and the employer may expressly agree that the distant employment of the Teleworker will not be recorded in his/her labour book.

Specifics of hiring foreign nationals

If the employee is a foreign national, the employment contract and other required documents may only be signed once the steps described in the *Specifics of employing foreign nationals* section below have been completed.

In essence, employment law applies to foreign nationals to the fullest extent provided for in the Labour Code. Therefore, the employer is obliged to enter into an employment contract with any foreign national and follow all rules and procedures which flow from their employment relationship.

Managing employment relationships

Internal regulations

Any organisation whose employees work in Russia must adopt a set of internal regulations. These regulations complement the conditions set out in each employee's employment contract, and the requirements they contain are mandatory for every employee.

Internal regulations specify the respective rights and obligations of the employer and employee, working and rest time, salary, bonuses and benefits, behaviour, employee liability, business trips, etc.

HR paperwork and inspections by the Labour Inspectorate

An employer is obliged to maintain a significant amount of records and supporting documentation relating to employee holidays, sick leave, promotions, overtime, business trips, etc.

These records may be checked by the Labour Inspectorate at any time. If, in the course of an inspection, the Labour Inspectorate finds that the requirements of employment law have been violated, it may impose fines (up to RUB 50,000, i.e. EUR 1,064, per breach) on the employer.

Based on the recent practice of the Labour Inspectorate, if similar violations of labour legislation (for example, defects in a standard labour agreement) are found with respect to each employee of the employing company, this will be considered as a multiple violation. The aggregate amount of any fine imposed on the employer for such multiple violations may be calculated by multiplying the specific individual fine by the number of employees with respect to whom the violation occurred. Thus, the total amount of fine imposed for such violations may be very significant.

Health and safety at work

Since 1 January 2014, the workplaces of all employees must be assessed, with the exception of homeworkers, Teleworkers and employees working for individuals who are not registered individual entrepreneurs. Previously, office workplaces were generally exempt from the assessment requirement.

The main purpose of the assessment remains the same as under previous rules, namely to provide employees with relevant guarantees and compensation, and to set additional pension and social

insurance rates. These rates depend on workplace hazards, which are rated as either optimal, acceptable, harmful or dangerous.

The provision of the workplace assessment is a duty of the employer. It must be held at least once every five years.

Sick leave

When an employee is on sick leave, his/her employer is required to pay him/her a temporary disability allowance for the period of sickness. The employee's entitlement to the allowance is dependent on the submission of a medical certificate in the required form. The allowance is calculated on the basis of the average monthly salary over a period of two years and is capped at a specified amount.

The first three days of an employee's temporary disability period are paid by the employer out of its own funds. Any additional days are then funded at the expense of the Social Security Fund of the Russian Federation.

The same rules may apply to foreign nationals, provided that they meet certain criteria in relation to their migration status.

Maternity and parental leaves

An employee who gives birth is entitled to 70 days' maternity leave prior to and 70 days' leave after the child's birth. Longer maternity leave may be granted in case of a multiple or abnormal pregnancy. This right arises upon the presentation of a medical certificate, which may be issued starting from the 30th week of pregnancy. This provides for a period of entitlement equal to 140 days that can be used by the employee summarily (i.e. irrespective of the actual number of days used before the child's birth).

Parental leave may last up to three years and can be used by the mother or the child's relatives at any time during this period.

The employer is responsible for paying the various maternity related allowances provided for by law and then sets off the relevant amount against payroll contributions.

In general, pregnant women and women with children under the age of three years are entitled to an extensive number of benefits and privileges under Russian employment law. In particular, such women may not be dismissed on the grounds of mass redundancy, neither may men with at least three children one of whom is under the age of three years. Moreover, pregnant women may not be compelled to work a night shift, overtime, during days of rest or holidays and may not be sent on business trips. Women with children under the age of three years may only be engaged in the above types of work only upon their written consent and provided that no medical certificate prohibits a particular employee from performing these types of work. Moreover, they are entitled to a reduced working week.

Work councils

An employer may choose to organise internal work councils. These are usually

composed of employees who have made certain achievements at work.

Work councils are consultative bodies. Their main function is to develop and address proposals to the employer with the aim of improving work processes, work efficiency, etc. They cannot substitute trade unions or other bodies which represent employees' rights.

Trade Unions

Trade unions are bodies created to represent employees and protect their social and labour rights. Any individual of at least 14 years old may join a trade union.

In the situations specified by the Labour Code (such as mass redundancy or termination of an employment contract with a trade union member) or in collective agreements (if any), the trade union's motivated opinion is required. Should this occur, the employer must provide the trade union with draft documents explaining the relevant situation. The trade union has to reply within five working days, failing which the employer is free to ignore the union's opinion. If the opinion was duly submitted, but the employer decides to act contrary to it, the trade union has the right to appeal against the employer's decision to the Labour Inspectorate or a competent court.

Trade union leaders enjoy additional protection in certain cases where their employment is terminated at the instigation of their employer on certain grounds. They may not be dismissed without the consent of the upper-level trade union in cases of mass redundancy, repeated breaches of their work obligations, or where their dismissal was based on poor performance evaluation results.

In practice, trade unions in Russia are usually only present in large companies (in particular those operating production plants or factories).

Disciplinary sanctions

Non-compliance with work discipline (i.e. the non-fulfilment or inadequate fulfilment by an employee of his/her duties) may result in the following disciplinary sanctions being applied: a warning, an official reprimand or dismissal on corresponding grounds established by law.

Disciplinary sanctions may be imposed no later than one month after the time the employer had, or should have had, knowledge of the breach and, in any event, no later than six months after the breach was committed.

The Labour Code regulates the procedure for imposing disciplinary sanctions. Failure to comply with it renders the sanction invalid.

Terminating an employment contract

Cases and grounds for termination

An employment contract may be terminated:

— at any time by the mutual agreement of the parties;

— unilaterally by an employee providing two weeks' written notice or at the initiative of the employer (as discussed below);
— because of circumstances beyond the reasonable control of the parties;
— when the term of the employment contract expires;
— if an employee refuses to continue working because of a change in the ownership of the company (employer) or its reorganisation (this only applies in relation to certain top executive positions); or
— if an employee refuses to continue working because he/she (together with the employer) is relocated.

The employer may terminate the employment contract only on the limited number of grounds expressly set out in the Labour Code, such as:

— When there is **mass redundancy** or the employer is being **liquidated**. The employer must notify each employee in writing at least two months in advance. If there is a mass redundancy, the employer must offer employees all available vacancies which are equivalent to or below their current qualifications.
— When an employee is **unsuitable** for an employment position. Unsuitability must be confirmed by an attestation committee review. However, this ground for termination should be used with caution, as employees have a good chance of successfully challenging this type of dismissal in court.
— When an employee **systematically fails to fulfil his/her employment duties without reason** or commits a **single gross dereliction** of his/her duties.
— When an employee is found to have presented **false documents during the hiring process.**

In respect of specific categories of employees (e.g. the general director, Teleworkers), additional termination grounds may be provided for in the employment agreement.

The Labour Code requires that severance pay be made under certain circumstances.

Court practice with regard to dismissals varies substantially, and may differ from region to region. However, the general tendency is to protect the interests of employees, thus placing a greater onus on the employer.

Specifics of employing foreign nationals

The rules on the stay, registration and employment of foreign nationals in Russia have been amended over the last few years. These amendments are part of a broad reform officially intended to **simplify** (for example by introducing a simplified work regime for highly qualified specialists in July 2010) and **regularise** the status of foreign nationals working in Russia.

Recent positive developments include (i) the introduction of five-year business visas; (ii) the exemption from work

permit requirements for foreigners holding a temporary residency permit; and (iii) the forthcoming extension of the highly qualified specialist regime to accredited representative offices of foreign companies in Russia (from 1 January 2015).

That said, the various amendments also show a deterioration in the status of foreigners with more stringent sanctions for those breaching the law (in particular, increased fines for employers and the strict enforcement of entry bans for foreigners who have been held administratively liable more than twice) and the extension of language and civilisation command requirements to those who wish to work or reside in Russia.

Visas for foreign employees

Foreign nationals must apply for a visa. Citizens from the following countries of the Commonwealth of Independent States are exempt from Russian visa requirements: Armenia, Azerbaijan, Belarus, Kazakhstan, Kyrgyzstan, Moldova, Tajikistan and Uzbekistan. For stays not exceeding 90 days, Ukrainian citizens are also visa-exempt.

Types of visas

There are five categories of visas: ordinary, official, transit, diplomatic and temporary residence. There are seven subcategories of an ordinary visa: business, tourist, work, student, private, asylum and humanitarian. The most important types of visa for legal entities are considered below.

Business visas

Business visas are intended for foreign nationals who wish to conduct short-term and temporary business activities in Russia. Examples of these activities include business trips, negotiations, market studies and preparations to set up a company or any other type of establishment in Russia. Foreign nationals with multi-entry business visas are permitted to stay in Russia for up to 90 days within a period of 180 days.

Since 11 January 2013, five-year business visas can be applied for in respect of employees or representatives of (i) large foreign companies investing in Russia which satisfy certain criteria established by the Russian Government; or (ii) companies taking part in Government projects such as Skolkovo or the International Financial Centre.

Foreign nationals who obtain Russian business visas are not allowed to undertake any type of work activities in Russia. This requires a work visa.

Work visas

Work visas are required for foreign nationals who intend to conduct professional activities in Russia.

A foreign national who has been issued an official invitation from an employer must first obtain a single-entry visa. The visa is valid for up to three months and may be exchanged for a one-year multi-entry work visa once the individual is in Russia, although this is not applicable to highly qualified specialists (please see the *Highly qualified specialists* section below). The family members of a work-visa holder may obtain visas of the same category marked "accompanying

person". This visa allows family members to stay in Russia, but does not entitle them to work in Russia. It expires on the same date as the principal holder's visa.

Work visas are issued only after the employer has received general authorisation to recruit foreign nationals and a quota of foreign persons they may employ. Each foreign employee must also be granted a work permit (please see the *Individual work permits* section below).

The employer must be registered with the Federal Migration Service (the "**FMS**") to be permitted to issue invitations to foreign employees.

The process of obtaining a work visa usually takes from eight to twelve weeks.

Procedures relevant to an employer

An employer who recruits foreign employees to work in Russia has to comply with the following procedures:

Quotas

All legal entities wishing to employ foreign nationals must apply by 1 May each year for a quota of foreign employees whom they may employ. Certain professions and some categories of foreign employees (e.g. highly qualified specialists, foreign nationals who are exempt from the requirement to hold a work permit) are quota-exempt.

The quota allocated to each legal entity depends on the general quota set each year for all foreign employees. This quota differs between regions, different categories of employees, as well as different professions, countries of origin and other economic and social criteria.

General authorisation for the recruitment of foreign nationals

The general rule is that any employer intending to recruit one or more foreign nationals must obtain a prior general authorisation from the FMS to recruit foreign employees within its allocated quota. By way of exception, no such authorisation is required for highly qualified specialists and for foreigners from non-visa countries (Armenia, Azerbaijan, Kyrgyzstan, Moldova, Tajikistan, Uzbekistan and Ukraine).

In its application for this authorisation, the employer must justify the use of foreign employees.

Individual work permits

General remarks

Once the general authorisation for the employment of foreign employees has been obtained, the employer must apply for a work permit for each employee.

A work permit is required for any foreign national who wishes to perform any "work activity" in Russia, including unpaid and temporary work.

However, the following categories of foreign citizens are exempt from the work permit requirement:

— citizens of Belarus and Kazakhstan; and
— those holding a permanent residence permit and, since 11 January 2013, those holding a temporary residence permit.

These categories of permit-exempt foreign citizens are not taken into account in their employers' quotas and general authorisations to recruit foreign employees.

Language command requirements
Currently, foreign employees are not required by law to pass any Russian language tests unless they apply for employment in the housing and utilities or trades and services sectors.

From 1 January 2015, applications for work permits for non-visa foreigners will need to include a dedicated certificate proving their command of the Russian language, Russian history and fundamentals of Russian law (the "**Russian Language and Civilisation**"), unless they hold a relevant Soviet or Russian certificate of education.

Distinct rules will apply to foreigners subject to a visa regime. They will be given more time to prove they meet the Russian Language and Civilisation requirements. Proof must be submitted to the authorities within 30 days from the issuance of the relevant permit (rather than upon application). If they fail to do so, their permits will be cancelled.

All foreigners who obtained their residence or work permits before 1 January 2015 will only be required to prove they meet the Russian Language and Civilisation requirements when applying to renew these permits.

Certain categories of foreigners are exempt from the Russian Language and Civilisation requirements, such as highly qualified specialists and their relatives, and full-time foreign students with accredited educational institutions in Russia.

Personal accreditation of foreign employees of representative offices and branches

If the employer is a representative office or branch of a foreign company in Russia, its accreditation certificate states how many foreign employee it may employ. Within that quota, the employer must apply to the accrediting body for the personal accreditation of each foreign employee (and his/her family members).

Personal accreditation means that the competent authorities have approved the employee to work in Russia. However, this does not relieve the employer from having to obtain a general authorisation for the recruitment of foreign nationals, a work permit and a work visa for its foreign employees.

Notification

There is a notification procedure which foreign nationals and their employers must follow. This procedure also applies to highly qualified specialists.

It is based on the following principles:

— The FMS must be notified of arrivals and of any travel within Russia.
— A highly qualified specialist and the members of his/her family are allowed a period of 90 days from the date of entry into Russia, during which they are not required to register with the migration authori-

ties. Once the foreign specialist has been in Russia for 90 days, he/she must be registered at his/her place of residence.
— Belarusian and Kazakh employees and the members of their family have to register within 30 days.
— For all other foreign nationals, the registration procedure with the FMS must be completed within seven working days.
— Foreign nationals staying in Russia or travelling to another Russian region for less than seven working days, who are not staying in a hotel or in "a hotel-like residence", are exempt from the notification procedure.
— Heads of State, heads of diplomatic missions, members of parliamentary or governmental delegations, heads of international organisations (and family members of these persons) are exempt from the notification procedure. Ship, train or aircraft crew members are exempt from the procedure under certain conditions.

Business trips within Russia

A foreign employee is permitted to go on business trips outside the Russian region(s) in which his/her work permit is valid only if he/she occupies a position which is included in the list of occupations approved by the Ministry of Health and Social Development.

In addition, the duration of foreign employees' business trips is regulated as follows:

— a total of ten days during the validity of a general work permit; and
— 30 consecutive days during the validity of a highly qualified specialist work permit.

Different rules apply to foreign nationals who hold temporary or permanent residence permits.

Highly qualified specialists

On 1 July 2010, a new category of foreign employees was introduced, entitled "highly qualified specialist". This applies to a foreign employee with professional skills, knowledge and the proper qualifications in a specific area.

The annual remuneration paid to a highly qualified specialist must be at least RUB 2 million gross (EUR 3,546 per month), unless a lower amount is set in international agreements for certain nationals.

Currently, the highly qualified specialist regime is only available to Russian commercial legal entities and Russian based duly accredited branches of foreign legal entities. From 1 January 2015 however, representative offices of foreign legal entities duly accredited in Russia will also be eligible for this regime.

When the above criteria are met, a simplified procedure applies for obtaining a highly qualified specialist work permit and work visa. Accordingly, a work permit may be obtained within 14 working days and the employer is exempt from fulfilling a significant number of formalities (obtaining a quota, general authorisation to recruit foreign employees, etc.).

In addition, opting for a highly qualified

specialist regime provides employers and highly qualified specialist with increased flexibility, such as:

— A work permit is valid for up to three years, whereas an ordinary one is valid for only one year.
— A work permit is valid for multiple Russian regions rather than just the region where the employer is based.
— There are less restrictions on business trips (as mentioned above).

Bilateral and multilateral international agreements

Three international agreements regulating foreign workforce issues have, fairly recently, come into force. They affect in particular French, South Korean, Belarusian and Kazakh citizens.

In addition to these, on 30 December 2012, an Agreement between the Russian and Japanese Governments on the simplification of the visa issuance procedure for their respective citizens was ratified by Russia. This Agreement is not yet in force though.

Arrangements applying to French employees in Russia

On 1 March 2011, the Agreement "On the Temporary Employment of Citizens of One Country on the Territory of the Other", as signed on 27 November 2009 between the Russian Federation and France, came into force.

Special filing procedures and review processes for obtaining authorising documents for employment have been established, with the goal of simplifying the temporary employment of the citizens of the two signatory countries. In particular, documents allowing French citizens to enter and work in the Russian Federation have to be processed within one month.

Arrangements applying to Korean employees in Russia

An Agreement has been in force since 1 January 2012 between the Governments of the Russian Federation and the Republic of Korea (South Korea) on the temporary work activity of their respective citizens.

This Agreement simplifies the rules and procedures applicable to the stay and employment of (i) Korean employees of representative offices of legal entities in Russia; (ii) Korean employees working at or for Russian organisations belonging to a Korean group of companies; (iii) Korean top executives managing Russian enterprises; and (iv) some family members.

In particular, quotas limiting work activities do not apply to these persons.

Arrangements applying to Belarusian and Kazakh employees in Russia

As of 1 January 2012, Federal Law No. 186-FZ "On Ratifying the Agreement 'On the Legal Status of Employed Migrants and Members of Their Families'" applies to Belarusian and Kazakh employees in Russia.

The Agreement introduces reciprocal preferences, thereby simplifying significantly the conditions of stay and employment of the countries' respective

nationals.

Quota, general recruitment authorisation and work permit requirements no longer apply to Belarusian and Kazakh employees in Russia. These migrant employees and family members are allowed to stay in Russia for the duration of a migrant employee's employment contract (rather than the one year maximum previously applicable). The timeframe for notification of entering Russia is 30 days from the entry date (rather than seven working days).

Sanctions for violating migration legislation

If an employer fails to comply fully or in part with the relevant migration procedures, it risks a fine (calculated per breach) of up to RUB 800,000 (EUR 17,021) or, if it is active in the trade sector – RUB 800,000 - 1.5 million (EUR 17,021 - 31,915), and/or the suspension of its activities for up to 90 days. The employer's officers may be liable to fines of up to RUB 50,000 (EUR 1,064) or, if the employer is active in the trade sector – RUB 50,000 - 55,000 (EUR 1,064 - 1,170). A foreign employee may also be fined up to RUB 5,000 (EUR 106), and may be deported from or banned from entering Russia. An entry ban can be imposed on a foreign citizen who has been held administratively liable more than twice, including for violations of legislation other than in the field of migration (such as, for instance, road traffic regulations). Foreign citizens are therefore strongly advised to be as compliant as possible in view of the continuing trend of strict enforcement of entry bans.

Since 9 August 2013, stricter sanctions apply to the violation of migration law requirements in Moscow, St. Petersburg, the Moscow Region and the Leningrad Region, namely: individuals will pay fines of RUB 5,000 - 7,000 (EUR 106 - 149), officials – RUB 50,000 - 75,000 (EUR 1,064 - 1,596) and companies – RUB 800,000 - 1.5 million (EUR 17,021 - 31,915) and/or have their operations suspended for 14 to 90 days.

Real estate and construction

General approach

This section relates to real estate and construction matters in Russia, which are governed by a complex body of laws and regulations. Key legislation in this respect includes:

- the Civil Code of the Russian Federation: Part I dated 30 November 1994; Part II dated 26 January 1996; Part III dated 26 November 2001 and Part IV dated 18 December 2006 (the "**Civil Code**");
- the Land Code dated 25 October 2001 (the "**Land Code**");
- the Town Planning Code dated 29 December 2004 (the "**Town Planning Code**");
- the Forest Code dated 4 December 2006;
- the Water Code dated 3 June 2006;
- Federal Law No. 102-FZ "On Mortgage (Pledge of Immovable Property)" dated 16 July 1998 (the "**Law on Mortgage**"); and
- Federal Law No. 122-FZ "On the State Registration of Rights to Immovable Property and Transac-

tions" dated 21 July 1997 (the "**Law on State Registration**").

In 2013, amendments to the Civil Code affecting basic principles of state registration of property rights came into force to enhance the reliability of the registration system and ultimately the protection of good faith purchasers. At the beginning of 2014, amendments to the participation of notaries in real estate sale and purchase transactions came into effect to ensure a quicker registration of rights when the parties opt for the notarisation of transactions. More change is on the immediate horizon as the Law on Mortgages only applies to mortgages granted after 1 July 2014 to the extent it corresponds with the new pledge requirements introduced to the Civil Code by Federal Law No. 367-FZ dated 21 December 2013.

Rights to real estate

Russian law provides for two basic types of rights to immovable property:

— the ownership right (freehold); and
— the right to lease (leasehold).

Public and private ownership rights

Real estate (including land plots) in the Russian Federation may be owned publicly or privately. In relation to land, we would like to outline a number of local specificities.

Public land ownership

Publicly owned land means that the land is owned by the State (i.e. the Russian Federation or a region) or a municipality. Substantial areas of land in Russia (particularly in the City of Moscow, which has regional rather than municipal status) have always been state-owned.

Until 2001 (when the Land Code was adopted), the delineation of state-owned and municipal land plots was regulated by several legal acts. The process of delineation was complicated and, at times, confusing. It has been clarified by the Land Code and further clarification is on-going. Pending completion of this, and to ensure that it is still marketable, public land may be disposed of by municipal authorities. They are authorised to act as landlords in lease agreements, allocate land plots for construction and act as sellers during the privatisation of public land.

Public land plots may be privatised, subject to a number of statutory restrictions. For example, land plots falling within specially protected areas (such as national parks) or areas required for defence (such as military airports) may only be state-owned.

Private land ownership

Any legal entity or individual may own private land in the Russian Federation, subject to certain restrictions which regulate the legal status of the land plot.

Generally speaking, foreign nationals and legal entities enjoy the same rights to land plots as Russian individuals and legal entities. However, in respect of the ownership of land, foreign investors may not:

— own land in certain border territories or other territories specifically designated in the Land Code or federal laws (such as, for instance, land located within the boundaries of sea ports); or
— own agricultural land. This rule also applies to Russian companies with a foreign participation of 50% or more in their charter capital. Foreign investors (as widely defined above) may only lease agricultural land, which will complicate their Greenfield projects on this type of land.

Other rights to or affecting land plots

Russian land legislation that pre-dated the Land Code also provided for other types of land rights, such as (among others) the right of permanent perpetual use of the land plot and the right of inheritable use. The right of permanent perpetual use of a land plot could only be granted to state, municipal or other public enterprises or to municipal authorities. Legal entities were required to convert any pre-existing rights of permanent perpetual use into leasehold or freehold rights by 1 July 2012. Legal entities which failed to convert these rights before 1 July 2012 may be held administratively liable and have to pay an administrative fine of RUB 20,000 - 100,000 (EUR 425 - 2,128[1]).

As in other countries, an easement (or servitude) may be established over a land plot which is owned by a third party. This grants the land user a variety of rights (including the right to build structures such as cable lines and pole lines). The easement may be public or private and the distinction depends on the persons who are interested in it. If the easement is required by a particular person or legal entity, then only a private easement may be established in respect of the relevant land; if the general public is interested in the easement, then a public easement may be established.

[1] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience throughout this guide.

Real estate transactions

Sale and purchase transaction

Cadastral and state registration

A publicly or privately owned land plot may be bought and sold provided that (i) it has undergone all cadastral registration formalities; and (ii) the title to the land plot has undergone state registration.

Both procedures require the submission of certain documents to the state registration authority (i.e. the Federal Service for State Registration, Cadastre and Cartography) or its regional/local departments ("*Rosreestr*")(the "**Registrar**").

Failure to comply with these requirements may lead to any real estate transaction connected with the land plot being declared null and void.

Rights to buildings and structures located in Russia are subject to state registration. Rights to a building are not effective until they are registered in the Unified State Register of Rights to Immovable Property and Transactions Therewith (the "**State Register**"). In other words, a building/structure/

premises legally exists only from the moment of their state registration. Moreover, state registration (as evidenced by an ownership certificate) is the only confirmation of the existence of the ownership right. Only a court decision may overrule state registration.

Buildings on land plots

A general principle of Russian law is the unity of rights to land plots and buildings. The Land Code prohibits the transfer of land without the buildings and structures standing on it. Ownership rights to a building may only be transferred together with the rights to the land plot beneath this building. In exceptional cases, title to parts of a building may be transferred separately from the land if it is impossible to separate the respective part of the land plot, or if there is a restriction on the acquisition of this land plot.

Owners of buildings located on a land plot other than their own generally enjoy a pre-emptive right to purchase the land plot, or a preferential right to lease it. If a land plot is under state or municipal ownership, the owners of buildings generally have exclusive rights to privatise the land plot.

Privatisation

Since 30 October 2001, it has no longer been possible to privatise buildings, structures or industrial facilities without simultaneously privatising the underlying land.

A building owner has exclusive rights to obtain freehold or leasehold rights to a publicly owned land plot on which the owner's building stands. The building owner is free to choose whether to acquire leasehold or freehold rights to the land plot.

Up until 1 July 2012, the owners of buildings located on municipal and state land had the right to buy out the plots at a preferential price which depended on the cadastral valuation of the land plot. This price was between three and thirty times the amount of annual land tax payments and depended largely on the location of the land plot. Since 1 July 2012 publicly-owned land can still be bought out by the relevant building owners. However, the above preferential price formula no longer applies. The buyout price is determined by the federal, region or municipal authorities and depends on the identity of the owner of the land plot.

Sale and purchase contract

General

Certain conditions of a real estate sale-purchase transaction are deemed material and must be clearly determined in the sale and purchase agreement, such as the subject-matter (i.e. the land plot or building/structure/premises) and the price. In addition, the parties to the agreement are entitled to set out their own list of supplemental contractual provisions that they consider to be material to the transaction.

If the sale and purchase agreement does not fulfil the above requirements, it is deemed not to have been concluded. This means that (i) the purchaser does not acquire the ownership right to the

land plot or real property and (ii) the land plot or real property must be vacated and returned to its owner in its original state and the sale price returned to the purchaser. These consequences arise only if a competent court declares the sale and purchase agreement as not having been concluded.

Purchase of future property

The sale and purchase of future property was until fairly recently not recognised by Russian courts. Prior to the Plenum of the Supreme Commercial Court of the Russian Federation published Ruling No. 54 dated 11 July 2011, contracts relating to a building under construction were held to be invalid for breaching the material requirements of a sale and purchase agreement.

As a result, investors and developers had to enter into a preliminary sale and purchase agreement which was then followed by the conclusion of a main agreement or an investment contract (whose legal nature was not clear since it is not regulated as a distinct type of contract in the Civil Code).

As a result of the adoption of Ruling No. 54:

— sale and purchase agreements in relation to future property are valid (hence there is no need to enter into a preliminary agreement), but the buyer's title to the property only arises after its commissioning and the subsequent registration of the seller's title; and
— the majority of investment contracts are recognised as sale and purchase agreements in relation to future property.

In practice, this means that, when a project is structured around an investment contract, the investor is denied ownership rights if the property is under construction or it is actually completed but the developer has not registered ownership. The reason for this is that legally the real estate does not exist until it is registered. Although according to the current Supreme Commercial Court practice there is no risk that an investment agreement will be considered as unconcluded, an investor (buyer) can only compel the seller (developer) to transfer the property once the developer has registered its own initial ownership to the property. Thus the investor is not able to register its ownership right immediately after commissioning. Until such registration, the only option provided to the investor is to terminate the agreement and/or claim damages for loss. This solution is far from desirable for investors. There are options for investors which can be tailored for each project and require expert contract drafting. These can include securing obligations via pledges, penalties and/or bank guarantees and, for substantial real estate finance projects, using corporate mechanisms to take control over the developer.

Purchase of land for construction

To purchase publicly owned land for construction purposes, a specific procedure generally applies and requires a tender to be organised (please see the *Construction* section below).

Registration of transfer of title

The transfer of ownership rights to real estate must be registered in the State Register, whereas the sale and purchase contract itself does not have to be registered. The registration does however require the filing of the sale and purchase contract and other related documents with the Registrar, as evidence of the transfer of ownership rights.

Title is evidenced by an ownership certificate issued by the Registrar. A certificate of ownership of a land plot is believed to be true and overrules any other evidence until a court decision resolves otherwise. However, rights to property which arose before the Law on State Registration came into force (in January 1998) are deemed valid even if they are not registered.

As of 1 March 2013 the following principles of state registration of property rights have been introduced as part of the Civil Code reform: (i) the principle that the legality of grounds for registration has been checked by the Registrar and (ii) the principle of publicity and reliability of the information entered into the State Register. The principle of publicity and reliability means that any person acting in good faith may rely on any record made in the State Register. Thus a person who incurs losses as a result of illegal or incorrect data having been entered into the State Register due to a fault of the Registrar will be able to claim compensation from the federal budget.

If the parties to a sale and purchase contract choose to conclude it before a notary (they are not obliged to do so), the notary will check the validity of the transaction and undertake the registration formalities with the Registrar. In this case, the time period for the state registration of the real estate rights will be reduced from 18 calendar days to five working days and the notary will be responsible for the validity of the transaction. This new option, which has been in effect since 1 February 2014, aims to increase the reliability of transactions and the protection of the parties' interests. As it was introduced mainly with unsophisticated parties (private individuals) in mind, it remains to be seen if businesses will make use of this new opportunity.

Since 1 March 2013, it has been possible to enter into the State Register a notation of objection or a notation of court dispute over the rights to an immovable property:

— The right to apply for a notation of objection is only available to a previously registered titleholder. If the State Register contains a notation of objection, any subsequent titleholder will be prevented from alleging his/her good faith in the event of a claim asserted against him/her for the recovery of the property.
— A dispute notation may be entered into the State Register upon the application of any person challenging the validity of the registered right.

Any member of the public may request general information about real estate (such as the owner or registered encumbrances) in the form of an extract from the State Register. Since 1 January 2013 this information can be requested electronically[2]. However, certain information relating to a chain of transactions on the transfer of rights, as well as information about the number of plots and/or properties owned by a certain person or legal entity, may be requested only by the owner of the relevant plot or property.

Certain types of encumbrance (buffer zones of hazardous facilities, protective zones of cable lines and gas transmission lines, etc.) are not always recorded in the State Register. For this reason, it is highly advisable to conduct onsite investigations and legal due diligence of the land plot and any properties located on it, as well as review the documents kept by the Registrar (e.g. cadastral passports of the property).

Leases

Land leases

The following persons may (subject to certain restrictions) lease a land plot: (i) Russian and foreign nationals; and (ii) Russian and foreign legal entities.

If the lease relates to public land, the land lease agreement will contain the general provisions dictated by the landlord, as they come from legal acts adopted by the relevant municipal or state body. In practice, they may not be changed. The conclusion of the lease will also generally presuppose a tender process (subject to certain exceptions). A lease agreement in respect of a privately owned land plot may include any provisions provided they do not contradict any mandatory Russian law requirements.

Material lease conditions, such as the subject-matter (i.e. the land plot itself) and amount of the rent, must be clearly determined in the lease agreement. In addition, the parties may set out their own list of supplemental contractual provisions that are material to the transaction.

If a lease agreement does not meet the above requirements, it is deemed not to have been concluded. If this occurs, the land plot must be vacated and returned to its owner, and any rents already paid to the landlord must be returned to the tenant.

Term

Russian legislation places no general limit on the term of a lease of a land plot. However, certain limits exist on leases of specific types of land. For example, the maximum permitted term for a lease of agricultural land or forest land is 49 years. The maximum permitted term for a lease of coastal land is 20 years. Russian legislation may also specify a minimum term for a lease of a particular type of land. In some cases, this term may be at least ten years. If this is the case, the impact of the lease term should be assessed before any material investments are made.

[2] https://rosreestr.ru/wps/portal/p/cc_ib_state_services/cc_ib_data_on_real_estate/cc_ib_electronic_state_services_GRP

Any lease agreement concluded for a term of at least one year is subject to registration in the State Register. If the lease agreement does not meet these requirements, then it is deemed not to have been concluded. The legal effect of this is that the lease is treated as if it was not concluded at all. In such cases the land plot must be vacated and returned to its owner.

The Civil Code provides that, where a lease agreement does not specify a term, then it is deemed to have been concluded for an indefinite term. In such cases, a lease may be terminated simply by either party serving a termination notice on the other party at least three months in advance of the intended date of termination.

Upon expiry of the lease, a tenant has a preferential right to conclude a lease of the same land plot for a new term. The lease agreement can expressly exclude this preferential right.

If the tenant continues to use the land plot after the expiry of the lease term and the landlord does not object, the lease will be considered to be renewed on the same conditions for an indefinite term and may be terminated at any time by either party serving a termination notice three months in advance. The Russian courts usually consider this provision of the Civil Code as a mandatory one. Therefore the courts are likely to strike down clauses providing for the automatic renewal of a lease. In order to avoid this uncertainty, the lease should contain an undertaking by the parties to enter into a new lease for the same term and on the same conditions.

Assignment

It is generally permitted (subject to certain restrictions) to sublet, assign, mortgage or contribute leasehold rights to a land plot to the charter capital of a company. Unless otherwise provided for in the lease agreement, sublease, assignment and mortgage agreements may be entered into without the consent of the landlord (but subject to a subsequent notification by the tenant). In any event, there are a number of circumstances when the tenant's right to sublease or mortgage the plot, or assign lease rights, may not be waived or restricted (such as in the case of leases of public land for more than five years).

Termination

The Civil Code grants both a landlord and a tenant the right to terminate the lease unilaterally, either in the limited number of circumstances stipulated by the Civil Code (via court procedure) or as expressly agreed in the lease agreement itself. In the latter case, both in-court and out-of-court procedures may be used.

The Land Code stipulates additional circumstances in which a landlord may terminate a lease. These include, among others, use of the land in a way that is inconsistent with its land category and permitted use, and appropriation by the state.

In relation to state or municipal land, the Land Code also grants a landlord a specific ground for the early termination of a lease which has been concluded for

a term of more than five years. If a tenant commits a material breach of the terms and conditions of such a lease agreement, the landlord may apply for a court order enabling it to unilaterally terminate the lease early.

Commercial leases of buildings, structures and premises

Commercial lease sector

Commercial leases have been developing rapidly over the past few years. The market is generally dominated by the private sector of the economy, which means that the legal relationships are heavily influenced by commercial needs, the return on investment and the level of yield.

The commercial lease sector (especially in Moscow, the Moscow Region, St. Petersburg and other large Russian cities) is also affected by international practice in respect of rent and methods of rent calculation: so-called 'net', 'double net' and 'triple net' leases. A 'triple net lease' (the most common type) is a lease where the tenant is obliged, in addition to the payment of the base rent, to compensate the landlord for all expenses associated with the leased property (including multitenant buildings) such as property taxes, insurance, utilities, and maintenance and operation costs. Triple net leases are usually used for long term lease relations for large malls, business centres and warehouses due to their alleged positive impact on taxes, cash flow and other factors.

Structuring lease arrangements in respect of existing buildings, structures or premises

Long-term lease (the "LTL")

An LTL is a lease agreement which lasts for at least one year. An LTL is only valid upon state registration in the State Register. During the registration procedure the Registrar will examine the validity of the LTL. The material conditions of any lease should, therefore, be clearly determined, including the subject-matter of the LTL (i.e. building, premises or structure) and the amount of rent or the rent calculation method.

Short-term lease (the "STL")

In order for the tenant to legally occupy the building whilst an LTL is being registered, an STL is usually entered into between the parties. Both agreements should be simultaneously executed. An STL is a lease agreement executed for a period of less than one year (usually 11 months or 360 days). As the term of an STL is less than one year, it does not require state registration. It, therefore, requires only the signatures of the parties in order to be binding.

Structuring lease arrangements in respect of buildings, structures or premises under construction

As until recently it was absolutely impossible to lease future property under Russian law, market players have been using the following two or three-tiered legal structure:

— Preliminary Lease Agreement (the "**PLA**");

— STL; and
— LTL.

This lease structure is also favourable for investment acquisitions since it becomes much easier to calculate the sale value of the property in accordance with international valuation standards.

PLA

When a building, or any other property, is under construction, and a potential tenant wishes to 'mark out' the building, as well as particular premises within the building, and 'fix' the amount of rent, it enters into a PLA with the prospective owner to regulate their pre-registration relationship.

Prior to registration of an owner's title to the building, as well as the building itself, in the State Register, no LTL may be entered into in respect of buildings or premises within buildings. The PLA, therefore, contains various obligations (such as the time period for construction, the tenant's requirements for works and fit-out of the building and/or premises).

In order to be legally valid, the PLA must clearly determine its subject-matter, sufficiently describe the property to which it relates, and establish all the material terms and conditions of the main lease agreement to be entered into (the "**Main Agreement**").

The parties to a PLA should determine a time period within which the parties must enter into the Main Agreement. If no time period is specified, the parties should enter into the Main Agreement within one year from the date of execution of the PLA. If the parties fail to enter into the Main Agreement within this time period, the PLA will terminate. However, if the failure to enter into the Main Agreement was caused by one of the contractual parties, the courts may force the defaulting party to enter into the Main Agreement.

Main Agreement – STL and LTL

The STL and the LTL are executed after the initial state registration of the ownership title to the building in the State Register.

Alternative arrangement

In its Ruling No. 13 dated 25 January 2013, the Plenum of the Supreme Commercial Court of the Russian Federation considered the issue of whether it is legally possible to conclude a lease of future property.

This Ruling seems to make the conclusion of a PLA redundant. However, it remains preferable to use the original three-tiered legal structure (including signing a PLA). Once the property is registered, the parties enter into an LTL to avoid the risk of the state registration being rejected on formal grounds (i.e. because the landlord is unable to prove that it is the owner of the property before obtaining the certificate of the state registration of ownership of the property).

Real estate transactions and anti-monopoly control

As a general rule, real estate acquisitions and leases (land and/or buildings) are not subject to anti-monopoly control.

However, pre-transaction anti-monopoly control will apply to the acquisition and

lease of production assets such as industrial-purpose structures, facilities of communal infrastructure if:

— their net value exceeds 20% of the net value of the assets of the seller or the landlord; and
— certain worldwide asset value or revenue thresholds of the relevant groups of companies are exceeded (please see the *Anti-monopoly issues* chapter on page 40).

Furthermore, under Federal Law No. 381-FZ "On State Regulation of Trade Activities in the Russian Federation" dated 28 December 2009, food retailers with a market share in a given locality exceeding 25% are prohibited from acquiring or leasing additional outlets in that locality.

Mortgages

Creating a mortgage

Both freehold and leasehold rights to land and buildings may be mortgaged; there are no restrictions against this in either the Land Code or the Civil Code. Rights to buildings and parts of buildings, including residential buildings and flats, may also be mortgaged.

The terms and conditions of mortgages are governed by the Law on Mortgage, which requires mortgages over the completed buildings and the underlying land plot be granted simultaneously.

A security interest over a land plot or other property is generally created by the parties entering into an express mortgage agreement. However, a mortgage may arise by operation of law (for example, a bank giving a loan to buy a property will become a mortgagee until the sale price is repaid in full).

A mortgage agreement must be drafted as a single contract, signed by both parties (who may choose to do so before a notary), and then registered with the Registrar. Mortgage agreements concluded before 1 July 2014 only come into effect upon registration in the State Register, failing which they are null and void. Mortgage agreements concluded from 1 July 2014 will no longer need to be state registered. They will therefore come into effect upon signing. However, mortgages as encumbrances over real estate will still need to be state registered.

The parties have two registration options:

— submit a joint application and a set of necessary documents to the Registrar; or
— appoint a notary to submit a notarised application (this option was introduced in 2011 and is available if the mortgage agreement is notarised).

The Law on Mortgage sets out the time period within which the Registrar must complete the registration formalities. For a mortgage of (i) residential property; or (ii) a land plot and non-residential property under a notarised agreement, the time period is five working days. For mortgages of land plots and non-residential property under a simple agreement, the time period is 15 working days.

Enforcing a mortgage

If a significant breach of a secured obligation occurs, the mortgagee may

enforce the mortgage. There are two methods of enforcement: (i) through the courts, resulting in the secured property being sold at a public auction; or (ii) through an out-of-court enforcement procedure (provided that the possibility of the out-of-court procedure is prescribed for in the mortgage agreement or a separate agreement between the mortgagee and the mortgagor).

The Law on Mortgage provides for the following options when the mortgagee is using the out-of-court enforcement procedure:

— retention of the mortgaged property by the mortgagee; or
— sale at an auction.

In a number of cases, the use of the out-of-court enforcement procedure is prohibited (for instance: if the first and second ranking mortgages provide for different types of enforcement procedures; if the subject-matter of a mortgage is residential property owned by an individual; or if the mortgage secures different obligations in favour of co-mortgagees).

The Law on Mortgage also sets out a procedure for the distribution of the proceeds received as a result of the enforcement of the mortgage. For example, for both the out-of-court and court enforcement procedures, the sale proceeds are distributed subject to the priority of claims between (i) all mortgagees that filed their claims; (ii) other creditors; and (iii) the mortgagor. Such priority would have to be determined on the basis of the entries in the State Register.

If enforcement of the mortgage by the mortgagee in respect of a residential property is by way of retention of the property and the proceeds do not fully cover all of the mortgagee's claims, then the outstanding payment obligation will be deemed to be fully satisfied.

Resolution of real estate disputes

In Russia commercial disputes between legal entities may be referred to the competent state courts or, if the parties so elect, to arbitration tribunals. However, until 26 May 2011, all disputes related to the execution of contracts subject to state registration, or rights and obligations arising from contracts subject to state registration (for example: LTLs, sale-purchase agreements for a plot or property, mortgage agreements) were required to be heard and resolved in state courts. This was the official position of the Supreme Commercial Court of the Russian Federation.

On 26 May 2011, the Constitutional Court of the Russian Federation held that (i) the Supreme Commercial Court's practice contradicts the law; and (ii) any dispute related to a transaction subject to state registration may be heard and resolved in arbitration tribunals established in accordance with Russian legislation. One of these tribunals is the International Commercial Arbitration Court of the Chamber of Commerce and Industry of the Russian Federation. At that time, the Constitutional Court's decision was seen as a positive step for

the development of Russian justice and for the improvement of the investment climate. However, very often this decision of the Constitutional Court is ignored by the state courts. Therefore submission of any dispute for resolution at an arbitration tribunal should be considered carefully.

Planning and construction issues

Land plots are assigned to a land category and a permitted use in order to optimise utilisation of different plots of land.

Land categories

Under the Land Code, land in Russia is divided into seven land categories (each with a designated prescribed use):

- agricultural land;
- land of settlement;
- industrial land (for the purposes of industry, energy production, transport, communication, television, radio translation, cosmic activities, defence and other special purposes);
- land containing specially protected areas and objects (e.g. nature parks);
- forest land;
- land near water; and
- reserved land.

Specific provisions may apply, depending on the land category. For example, when agricultural land is being sold, Russian regions enjoy pre-emptive rights of purchase, as do municipal authorities, in the situations provided for by the relevant regional legislation. As mentioned above, foreign investors (including companies and individuals) may not own agricultural land, but may only obtain lease rights. Agricultural land that is not used in accordance with its designated prescribed use may be taken from its owner under a court decision.

Essentially, the most suitable categories for development and commercial construction are industrial land and land of settlement. It is possible to build warehouses, commercial buildings and production facilities on land plots within these categories provided that the type of permitted use allows it.

Permitted use of land

Along with a designated prescribed use and zoning, land plots in the Russian Federation are assigned a "type of permitted use". The type of permitted use characterises a land plot in accordance with territorial zoning and establishes the specific use of a certain land plot. Each land category has different conditions for the use of land, and the Land Code requires that each plot be used only in accordance with the applicable category and established type of permitted use.

Change of land category and permitted use

Land category

It is possible to change the category of a particular land plot. For example, the regional authorities may change a plot's land category from "agricultural" to "industrial" (e.g. for the allocation of a warehouse complex) subject to a

number of obligatory procedures. A land plot may be assigned to the category of land of settlement only when it is annexed to the territory of the settlement (included in the borders of settlement). Again, this is done at a regional level if no town planning documentation has been adopted. As soon as the general plan of a settlement is adopted, the relevant change procedure requires the general plan of the settlement to be amended. This is done at municipal level.

Changing the category of forest land or land near water is more complicated (as it involves federal authorities) and is strictly regulated. Legislation provides an exhaustive list of circumstances in which there may be a change of category in these cases.

Permitted use

The owner of a land plot may change the type of permitted use at its own discretion according to the adopted town planning documentation (general plan of the settlement and the rules of land use and development). Where town planning documentation is not adopted, a strict procedure must be followed in order to change the type of permitted use, which involves public hearings.

Town planning framework

The current federal Town Planning Code, adopted in 2004 (and revised a number of times since then), stipulates that each urban settlement must adopt city planning documents, including: (i) regional and municipal territory planning documents that establish the boundaries of various development zones in large territories; (ii) city general plans that set out the boundaries of various functional development zones within individual urban settlements; and (iii) rules for land use and development that establish territorial zoning and describe in detail what may be done in each territorial zone of each urban settlement. The town planning documents establish territorial and functional zoning of the settlement territories and indicate existing town planning limitations, such as "red lines" and protection zones. Construction planned for any new development must comply with the prescribed town planning limitations and zoning. For example, the construction of a large shopping mall in a recreational zone would not be permitted.

Rules on land use and development must be adopted in line with various deadlines depending on the zoning categories (for settlements, by 31 December 2013; for rural settlements, by 1 June 2014; for the city of Moscow and the Moscow Region, 31 December 2014). After these dates, no new development will be allowed in these settlements. However, the time limit has already been prolonged several times; therefore, there are grounds to suggest that it may be prolonged again.

Another important document in respect of a particular land plot is the land plot development plan ("*GPZU*"). The land plot development plan contains all information regarding the land plot necessary for construction: the type of permitted use, boundaries, minimum

offsets from the boundaries, technical conditions for connection to engineering communications, etc. The land plot development plan is one of the mandatory documents that must be submitted in order to obtain the construction permit.

Construction

Various entities are involved in the construction process in Russia:

- a client ("*zastroyshchik*") – the entity who wants to build a property for itself or for its subsequent sale or lease;
- a technical customer ("*tekhnicheskiy zakazchik*") – a special professional company engaged by the client in order to supervise and manage the construction of the property;
- a general designer ("*generalnyi proektirovshchik*") who develops the design documentation;
- a contractor ("*podryadshchik*") or general contractor ("*generalnyi podryadshchik*") who performs the construction works for the client, either by itself or through subcontractors; and
- various specialised engineering entities who carry out surveys required for the construction.

The client must have rights to the land plot (freehold or leasehold) where construction is envisaged.

Since the majority of land in Russia is still state-owned, before commencing any construction project in Russia, it is important to assess the issues of how to acquire land in Russia and who is responsible for obtaining, from various state authorities, the authorisations and permits required for construction.

Acquisition of public land for construction

The Land Code stipulates a specific procedure for making publicly owned land available to individuals and legal entities for construction purposes.

Both Russian and foreign nationals or legal entities interested in obtaining land for construction may apply to the relevant authority for the allocation of a land plot. Any refusal to allocate land may be appealed against in court (subject to certain restrictions).

Land for construction may be obtained from the state or from the municipal authorities under either of the following two procedures:

- First, a relevant state authority carries out preparatory work (i.e. it determines the boundaries of the land plot and registers the land plot if necessary). Subsequently, it sells the land plot or the right to lease the land through an auction. This is likely to be the more common scenario.
- Alternatively, an interested party applies to the appropriate state authority for a land plot, together with authorisation for a construction site. The state authority decides whether or not to issue preliminary authorisation for a construction site (its decision is valid for three years). If preliminary authorisation is given, the applicant must carry out all

preparatory work on the land. Once the preparatory work is completed, the state authorities issue permanent authorisation for a construction site. Then a lease agreement of the land plot may be concluded between the applicant and the state authority.

The second procedure may only be applied when: (i) the land plot has not been subject to cadastral registration; and (ii) there are no rules on land use and development ("*pravila zemlepol'zovaniya i zastroyki*"), land survey plan ("*proekt mezhevaniya territorii*") and land use plan ("*proekt planirovki territorii*") in respect of the land plot (please see the *Town planning framework* section above on page 121).

As part of the further plans to reform the Civil Code, the introduction of a right of development ("*pravo zastroyki*") to allow a person to build on land owned by a third party without that person having leasehold rights to that land has been discussed. The right of development would arise under an agreement between the land owner and the individual or privately owned company (client). In parallel, they would sign an agreement granting a right of permanent possession and use of the land to the latter. If the right of development is introduced, it will replace the lease of land plots used for construction purposes.

Apart from the above schemes, land plots may also be provided to a client by the state or municipal authorities through investment schemes or public private partnership ("**PPP**") schemes (please see the *Infrastructure and public private partnerships* chapter on page 126). In these cases, the title to the land plot is provided to the successful bidder within the time period set out in the respective agreement.

Since 1 April 2012, the state authorities are entitled to terminate unilaterally lease agreements of land plots located in the cities of Moscow and St. Petersburg[3] by giving one month's prior termination notice in the following cases:

— failure to complete construction in accordance with the terms specified in the lease agreement, or, if such terms are not specified, within the construction terms set out in the construction permit if the property under construction is less than 40% complete;
— if the construction permit has not been obtained within five years of the date of execution of the land lease; or
— if the law has changed and no construction activity may be performed on a land plot or the land plot is subject to encumbrances or third party rights preventing construction.

If the land lease agreement is terminated due to the reasons above, the client may only claim documented expenses. Loss of profit will not be recovered.

Construction permits

Any construction activity may only be performed on the basis of authorisations

[3] This applies to leases concluded before 1 January 2011.

and permits issued by state authorities. In Russia the list of such permits and authorisations may differ depending on the type of property to be constructed.

A construction permit must be obtained prior to the commencement of any construction works. This is a formal document that confirms that the design documentation meets the compulsory requirements of the law.

Construction permits will be issued only in the following cases: (i) the applicant has all entitling documents to the land plot; (ii) a positive (state or non-state) expert opinion has been received by the applicant on the design documentation; and (iii) there are no contradictions between the entitling documents, design documentation and the land plot development plan.

The Town Planning Code requires the applicant for a construction permit to have rights (freehold or leasehold) to the land plot. If someone constructs a building on a land plot over which it has no rights, the building may be declared to be an "unauthorised structure" by the courts, and demolished at the expense of the person who developed the "unauthorised structure".

A construction permit may be obtained by a client or by a technical customer acting as the client's agent.

A construction permit contains a number of essential elements such as the time period for the construction works, the area of the constructed property and the name of the client. A valid construction permit is one of the documents required to commission the constructed property.

Commissioning

Property commissioning is the second most critical milestone in the construction process. Commissioning may be divided into two stages:

— commissioning of the works performed by the contractor/subcontractors for the client; and
— commissioning of the constructed property by the state authorities.

The first stage is critical in respect of the contractual relationship with the contractor or general contractor since commissioning of the works performed is treated as their acceptance by the client. This means that a contractor or general contractor is entitled to claim for payment for the works performed (the payment mechanism is usually determined in the construction agreement) and the warranty period begins to run from the date of acceptance.

The second stage is critical for state registration of the property. During this stage the state construction supervisory authority examines the compliance of the constructed property with the construction permit, the design documentation and the land plot development plan. If certain parameters (such as the total area, total structural volume, etc.) differ, the commissioning permit will not be issued and it will be impossible to register the property in the State Register.

Licences and admission certificates

In Russia, the state has historically regulated construction activities. Until January 2010, technical customers, contractors, general designers and specialised engineering entities had to obtain special licences in order to carry out construction works, engineering surveys or to prepare project and design documentation. No construction activities (including the activities mentioned above) were permitted without the requisite licence. Failure to comply with this requirement could result in criminal or administrative liability.

Since 1 January 2010, membership of self-regulated organisations ("**SROs**") (which authorise their members to carry out certain activities by issuing admission certificates) has fully replaced licensing for the following construction and design activities:

— designing buildings and structures;
— constructing buildings and structures; and
— engineering and surveying for the purposes of erecting buildings and structures.

The list of activities subject to the SRO membership requirement is set by the Ministry for Regional Development of the Russian Federation. It currently contains many activities. Activities that are not listed in the Ministry's decrees are generally exempt from the admission certificate requirement. However, some construction-related activities are still subject to licensing requirements. Examples of these activities include the installation of a fire fighting system or the operation of an industrial facility classed as posing fire or explosion hazards.

Construction and design activities, as well as the construction supervising activities in respect of any commercial property, that require SRO membership may only be carried out by a company holding a valid admission certificate. This also applies to subcontractors since Russian law does not recognise the 'umbrella principle' in respect of admission certificates.

Both Russian and foreign legal entities may obtain admission certificates. SRO membership fees depend on type of activity and may be substantial.

Infrastructure and public private partnerships

General approach

Over the last few years, infrastructure and public private partnership ("**PPP**") projects remained of great interest to both the public sector and private investors, but the unstable economic conjuncture globally, and in Russia in particular, remained a hindrance when dealing with the financing of most infrastructure and PPP projects.

On the one hand, projects like the Western High-Speed Diameter (one of the largest PPP projects in Europe), the M4 Toll Road (Section 2), the Pulkovo Airport, the M-1 Odintsovo By-Pass and the Moscow-St. Petersburg Toll Road (Section 1) projects were successfully implemented over the last few years and are now 'well on the roll'.

On the other hand, many other high-profile PPP projects have been post-

poned, suspended indefinitely, converted into public procurements or even aborted (e.g. the Moscow-St. Petersburg High-Speed Rail project (VSM-1), the Moscow-Kazan High-Speed Rail project (VSM-2), the Neva Water project, the Orlovsky Tunnel, the Palace of Arts on Vassilevsky Island, the Nadex, etc.).

That said, there is still a healthy pipeline of infrastructure and PPP projects in Russia, which shows that the PPP sector is far from stagnant.

Russian federal and regional authorities are becoming increasingly engaged in the development of PPP. At the federal level, Russia's lower chamber of Parliament (the State Duma) operates a PPP council. Several federal ministries also manage PPP councils, including the Ministry of Transport, the Ministry of Culture, the Ministry of Public Health and the Ministry for Economic Development. At the regional level, more than 60 regions have now adopted their own PPP law.

The trend over the last decade shows that Russian authorities view the PPP sector as a leading area for development and for attracting foreign investment.

Key PPP legislation

Federal PPP legislation

At the federal level, PPP projects are regulated by:

- Federal Law No. 115-FZ "On Concession Agreements" dated 21 July 2005 (the "**Concession Law**");
- the Land Code dated 25 October 2001 and laws regulating land issues;
- the Town Planning Code dated 29 December 2004 and laws regulating construction activity;
- the Civil Code of the Russian Federation (the "**Civil Code**");
- the Budget Code of the Russian Federation dated 31 July 1998 (the "**Budget Code**") and associated regulations (e.g. the Governmental decree No. 134 "Rules of budgeting and use of budget funds of the Investment Fund of the Russian Federation" dated 1 March 2008, etc.); and
- laws and decrees of specific application (e.g. Federal Law No. 257-FZ "On Motorways" dated 8 November 2007).

Concession Law

The Concession Law was adopted in 2005. Since 2007, it has been repeatedly amended at least once every year.

The Concession Law applies to certain types of infrastructure such as roads and roadside utilities, pipelines, sea and river ports, airports, public utilities, railways, subways and other public transportation and public health facilities.

The Concession Law sets out the general rules for entering into concession agreements, including the tendering rules and the material terms to be set out in these agreements.

In May 2013, the legislator introduced new amendments to the Concession Law (which entered into force on 1 January 2014). These are primarily aimed at clarifying the requirements for the implementation of certain utility infrastructure

projects, such as communal heat, water supply and waste-water utilities.

In addition, pursuant to these amendments, the official website http://torgi.gov.ru/ was developed as a single platform for posting concession tenders and related information.

Despite the introduction of the above measures, many legal obstacles affecting the bankability of PPP and concession projects remain. To name but a few, these restrictions include the prohibition on the substitution of the concessionaire during the construction stage, the prohibition on the resolution of disputes outside Russia or by non-Russian institutions and the lack of guarantees in relation to the budgetary process and tariff regulation.

Discussions on a federal PPP law

The possible adoption of a new federal law on PPP remains a topic of discussion.

On 26 April 2013, the draft of this law (introduced to the State Duma by the Russian Government in March 2013) passed its first reading.

Generally, this draft law is aimed at unifying the principles regulating PPPs, defining the powers of public authorities when acting in these partnerships and specifying the forms and procedures for implementing PPP projects.

In particular, this draft includes the following provisions which help define, characterise and regulate PPPs:

- A PPP is defined as the cooperation of a public partner (the Russian Federation, a Region of the Russian Federation or a municipal authority) and a private partner (private Russian or foreign legal entities or individual entrepreneurs) on the basis of a PPP agreement entered into pursuant to a tender procedure and aimed at increasing the quality and availability of public services by attracting private investments.
- A PPP agreement is a mixed-type contract that includes elements of various civil law nominate contracts.
- A PPP may be performed in the form of a concession agreement or in any other form which is not prohibited by Russian law.
- Under a PPP agreement, the private partner must fully or partially finance and operate and/or maintain the object that is granted under the agreement. The private partner may also be required to prepare the design documentation, obtain the relevant approvals, build or reconstruct the object granted under the PPP agreement, etc.
- A PPP agreement may provide for the transfer of ownership title to the object of a PPP agreement from one party to other.
- Should the applicable federal, regional and/or local laws and regulations be amended during the effective term of a PPP agreement in a way that adversely affects the private partner, then the parties must review the provisions of the agreement so as to restore the economic balance initially intended by the parties, as well as the

property and financial interests of the private partner.
— Other subordinate legislation (mainly, Governmental decrees) should regulate such matters as the preparation of the PPP agreement, the content of the tender documentation, the tender procedures, control over the implementation of PPP projects, etc.

At first reading, some recommendations were made in order to complete this draft law. The second reading was initially scheduled for November 2013, but in December 2013 it was indefinitely postponed to allow for closer consideration of the comments made by the various authorities that were involved in the review process.

In particular, these recommendations included: (i) specifying the material terms and provisions of a PPP agreement; (ii) harmonising the provisions of the draft law with those of the Concession Law and the privatisation legislation (especially with respect to the transfer of ownership title to the object of a PPP agreement from a public entity to the private partner); and (iii) listing the types of PPP agreement and distinguishing "municipal private partnerships" (based on the fact that local authorities are public entities, but are not considered as state authorities).

If this bill is passed into law, it would unify the terminology and stipulate a common approach to PPP, giving greater clarity and stability both at the federal and regional levels. Indeed, experts have been debating over the validity of regional PPP laws and PPP agreements (other than the concession model). Some argue that these conflict with federal laws (based on the principle of primacy of federal law).

However, others believe that this law may cause legislative array. Some provisions of the draft law remain vague and conflict with existing legislation. As with any new law, the first version is likely to show some imperfections. Rectifying these would take time and the response of the parties involved in PPP projects would have a direct effect on how quickly this law would be changed to make it appropriate and workable.

Certain existing regional laws will also need to be amended in order to bring them in conformity with this draft federal PPP law.

Finally, it is not clear how this new law will co-exist and inter-relate with the Concession Law (although the draft states that the Concession Law will still apply to concession agreements).

Regional PPP legislation

Currently, there are more than 60 regional PPP laws, the most notable one being the Saint Petersburg PPP law.

A number of projects have been procured by the Saint Petersburg Government under Law No. 627-100 of Saint Petersburg "On the Involvement of Saint Petersburg in Public Private Partnerships" dated 25 December 2006.

This law addresses a number of the limitations in the Concession Law and is

considered by many to be a more progressive statute. It is also the foremost regional law in this field (i.e. it was cited as a best-practice model in the explanatory note to the draft federal PPP law). An increasing number of proposed and on-going projects in Saint Petersburg are actually based on local PPP legislation.

Saint Petersburg's location as a port city and its high level of economic development, combined with political willingness and concrete steps towards implementing PPP, generates a friendly investment climate. This, in turn, explains the large number of projects implemented in the region, such as the Western High-Speed Diameter, the waste recycling plant in Yanino (Levashovo), the Pulkovo Airport, the Pushkinsky District education facilities and the project for the renovation of "Khrushchyovka" apartment buildings.

Whilst some other Russian regions have followed Saint Petersburg's example by adopting their own PPP law, this trend in the regional PPP sector has lost some of its momentum. This is essentially due to the likely adoption of a PPP law at the federal level. In addition, many regional PPP laws serve only as broad guidelines and remain declarative. Other regions have expressly abandoned their plans to adopt their own PPP legislation (such as the City of Moscow).

Moreover, regional PPP initiatives may be considered as modest as there is still a lack of public funding, local expertise, sufficient preparation and best-practices to rely on for the actual implementation of these projects.

In the absence of a federal PPP law, the uncertainties surrounding the validity of regional PPP laws and PPP agreements (other than the concession model) also create a hindrance to the development of regional PPP.

Alternative schemes or quasi-PPP

Alternative PPP schemes have been implemented in the past on the basis of other legislation, such as the investment contracts of the Budget Code, long-term leases with investment undertakings governed by the Civil Code, public-private joint ventures based on the privatisation legislation and general civil and corporate law principles. The draft federal PPP law is meant to become an umbrella legislative act regulating all PPPs, irrespective of the form they take.

A procurement law also exists in Russia, Federal Law No. 44-FZ "On the Contractual System in the Sphere of the Procurement of Goods, Works or Services for State and Municipal Needs" dated 5 April 2013 (in force since 1 January 2014). However, this law does not extend to PPPs or concessions (as expressly stated in the abovementioned draft federal PPP law). It only regulates the more 'traditional' procurement contracts for the purchase of goods, works and services by the state or municipal authorities, which create simply a customer/contractor relationship between the public and the private sectors.

Russian PPP environment

Governmental commitments

Russian authorities have adopted several programmes aimed at modernising infrastructures, including roads, railways, airports, power generation plants, the health system, social infrastructure.

The Government provides support to private investors in order to attract foreign investment. For instance, it co-finances and/or guarantees PPP projects. It also provides tax credits and other benefits prescribed for special economic zones (please see the relevant section of the *Tax system* chapter on page 57).

Transport

The Ministry of Transport is the state body responsible for the development and investment policy in all areas of transport. Each means of transport (roads, airports, railways, etc.) is under its supervision and is managed by a specialised entity, which, in turn, reports to the Ministry of Transport.

Roads

The state company Russian Highways is responsible for, amongst other things, PPP projects in relation to federal roads. Under its activity programme for 2010-2019, as approved by the Government[1], Russian Highways will be allocated RUB 1.4 trillion (EUR 29.8 billion[2]) to (re)construct highways, develop new international routes and create a chain of multifunctional road service zones through PPP projects. Most of the PPP projects are planned as 'life cycle contracts' by way of concession agreements and operation & maintenance contracts.

Railway

OJSC Russian Railways ("**RZD**") operates a monopoly in the Russian railway sector and regularly initiates a number of investment projects, such as the Moscow-St. Petersburg and Moscow-Yekaterinburg high-speed railways.

RZD is currently implementing its RUB 1.1 trillion (EUR 23.4 billion) investment plan for 2012-2014[3]. A new long-term investment programme which aims to see between RUB 7 - 11.6 trillion (EUR 148.9 - 246.8 billion) of investment made by 2020 for the development of railways was approved in April 2013[4]. The Russian Government will provide financial support for the largest railway projects.

Common issues for transport PPP projects

There are certain recurring obstacles for any investor looking to invest in transport projects in Russia.

By way of example, some investors may disagree with the methodologies used to assess traffic. Also, some projects may not be put to tender owing to certain transport infrastructure objects being qualified as state secrets or intended for military purposes (even though they are used mostly for civilian purposes).

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[1] Order No. 2146-r of the Government of the Russian Federation dated 31 December 2009.

[2] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience used throughout this guide.

[3] http://ir.rzd.ru/news/public/ir?STRUCTURE_ID=45&layer_id=3328&id=78600

[4] http://press.rzd.ru/news/public/ru?STRUCTURE_ID=654&layer_id=4069&id=81780

Communal utilities

Utilities are a well-grown field for investment and are thought to offer a great potential for foreign investment. As an inheritance from the Soviet Union, Russia received a large number of housing and utility facilities, most of which are in poor condition, requiring urgent repair or modernisation.

Foreign investors may encounter legal hurdles when investing in utilities facilities, such as for instance:

— Many utilities facilities have yet to be registered and there may be underlying issues when determining the ownership status of the facilities.
— A security clearance licence must be obtained when a project relates to the water infrastructure of a city with a population of more than 300,000.
— Tariff policies lack predictability and are seen as inappropriate by some.

Social infrastructure

PPP projects in social infrastructure are primarily initiated in the regions, such as the reconstruction of a hospital in Vologda, the construction of retirement homes in the Moscow Region and in Buryatia, the construction of two sport facilities in the Nizhniy Novgorod Region, the construction of a college for gifted children in Omsk, the education facilities in the Pushkinsky District of St. Petersburg and the construction of 25 kindergartens in Tomsk.

The main obstacles for investors in this field are the return on investment and available guarantees, as project cash-flow is based on the availability of payments made by the relevant state authorities.

Financing

Funding market players

International financial institutions (such as the World Bank, the International Financial Corporation, the European Bank for Reconstruction and Development) have in past years shown interest in financing infrastructure projects in Russia.

The state corporation Bank for Development and Foreign Economic Affairs ("**VEB**") is the Russian financial institution responsible for developing and funding PPP projects in Russia. VEB provides financing for projects deemed to be of primary importance to the Russian Government and which are carried out on a PPP basis, including those partially financed from the Investment Fund of the Russian Federation. There are a variety of methods which allow VEB to participate in infrastructure projects, such as providing guarantees, suretyships and loans, as well as through equity finance.

In the private sector, the investment and commercial banks involved in PPP projects remain Russian for the most part, with Sberbank, VTB Capital and Gazprombank leading the way.

Legal issues

Some of the innovations that have been introduced in the framework of the Civil Code reform are likely to bring the PPP

legal environment in Russia one step closer to international best-practices in the fields of PPP and project finance. These features include concepts such as escrow accounts, nominee accounts, irrevocable powers of attorney, pledges on future receivables, pledges on bank accounts and the subordination of claims.

A topic which had been under discussion for several years was the adoption of a law "On Infrastructure Bonds". While it seems that this topic has lost some of its thrust, the so-called law "On Securitisation" (Federal Law No. 379-FZ dated 21 December 2013) could become a helpful instrument in attracting funding for PPP projects through the issuance of derivatives and other types of securities.

Despite the legal developments in 2013-2014, further amendments to the current legislation are still required in order to address the concerns of financing organisations and increase the bankability of PPP projects in Russia. The topic of the adoption of a federal PPP law remains outstanding and could address some of the concerns of investors and lenders.

Sector prospects

A number of PPP projects have already been announced or are expected for 2014-2015, including:

- the Central Ring Road ("*TsKAD*") in the Moscow Region;
- the Kutuzovsky Prospect relief-road;
- the Moscow Ring Railway;
- the Perm Eastern Bypass (section 2);
- the crossover bridge on the Lena River in Yakutsk;
- the crossover bridge on the Volga in Nizhny Novgorod;
- the construction of four recycling plants in the Leningrad Region;
- the subsequent sections of the Moscow-St. Petersburg Toll Road (especially sections 7 and 8);
- the life cycle contract for the operation and maintenance of the Moscow Metro's rolling-stock;
- medical facilities PPP projects in several Russian regions (e.g. Municipal Health Clinic No. 63 in Moscow); and
- utilities projects in several Russian regions, including in Moscow, Karelia and Yakutia.

In conclusion, the Russian federal and regional authorities seem to recognise the need to develop infrastructure projects on a PPP basis, and they are taking determined steps to create the legal framework necessary to attract both foreign and domestic investors to this type of projects. These factors will likely help support current initiatives and possibly create new opportunities in the Russian infrastructure market in 2014. However, it remains to be seen if the Russian economy will allow projects to actually materialise.

Energy efficiency

General approach

Russia offers unique opportunities for investors who want to implement projects in the energy efficiency ("**EE**") sphere and, more particularly, for representatives of countries that already possess experience of implementing EE and energy saving ("**ES**") technology.

Russian EE legislation continues to be actively developed. In April 2014 a new state programme establishing the main principles and purposes of EE and ES policies was adopted for the period up to 2020. This programme provides for a general decrease of the energy consumption per unit of Russian GDP by 13.5% by 2020. It also earmarked approximately RUB 50.3 billion (EUR 1.1 billion[1]) from the federal budget to finance the implementation of EE and ES measures.

Notwithstanding these incentives, investment in energy efficient technology in Russia remains low in comparison to developments in the rest of the world.

[1] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience throughout this guide.

This is due to regulatory constraints and a lack of public awareness as well as of understanding of EE issues.

Legal framework

The main piece of legislation for EE matters is Federal Law No. 261-FZ "On Energy Saving and Energy Efficiency Increase and Amending Certain Legislative Acts of the Russian Federation" dated 23 November 2009 (the "**Law**"). It created a legislative, economic and organisational stimulus for ES and increasing EE.

The framework nature of the Law requires the Russian Government and competent federal ministries to adopt numerous bylaws. From 2010-2012, most of these were approved.

In this chapter, we will summarise the Russian EE requirements in relation to various sectors and the main features of energy service agreements, as well as outline the energy audit mechanisms and incentives.

EE requirements

To facilitate the efficient use of energy resources and to support and encourage ES, the Law provides for several groups of EE requirements in various sectors. Below, we examine how the Law applies to (i) the circulation of goods; (ii) buildings, structures and installations; and (iii) the public sector.

EE requirements for circulation of goods

Several categories of goods produced in, and imported to, Russia must contain information on their **EE classes** in any attached technical documentation, tags or labels. This requirement concerns:

- household energy consuming devices[2] (this requirement is applicable since 1 January 2011); and
- TV sets, electrical ovens and lifts (elevators) intended for public transportation (from 1 January 2014).

Manufacturers/importers are responsible for defining EE classes for specific types of goods, and for ensuring that this information is included in any technical documentation, tags or labels attached to the goods. Failure to comply with these requirements results in **administrative liability**[3].

EE requirements for the circulation of goods also cover the introduction of **energy efficient bulbs**. As of 1 January 2011, the Law prohibits the circulation of incandescent lamps exceeding 100W in alternating current circuits for the purposes of lighting. Further restrictions on the circulation of other incandescent lamps may be

[2] These devices include refrigerators, domestic air-conditioners, electric household lamps (incandescent lamps less than 100W and luminous low-pressure lamps), etc.

[3] A 'per breach' penalty for company officials at the rate of RUB 10,000 - 15,000 (EUR 213 - 319); for individual entrepreneurs – RUB 10,000 - 15,000 (EUR 213 - 319), possibly followed by confiscation of goods; for legal entities – RUB 100,000 - 150,000 (EUR 2,128 - 3,191), with possible confiscation of goods.

introduced at a later stage.

More stringent rules have been imposed on the public sector: since 1 January 2011 no public procurement for the supply of any incandescent bulbs is permitted, with the exception of electric bulbs for premises used by large groups of people (e.g. theatre and cinema halls, lecture auditoriums and restaurants, etc.).

EE requirements for buildings, structures and installations

According to Russian EE rules, buildings, structures and installations (with only a few exceptions) must comply with the **obligatory requirements**. The Ministry of Housing and Building is responsible for setting these requirements under a special Decree adopted by the Government. The EE requirements are to be revised at least once every five years and should cover:

— the maximum energy consumption limits for buildings/structures (adoption still awaited);
— requirements relating to the architectural, functional, technological, construction, engineering and technical solutions influencing the EE of buildings/structures (adoption still awaited); and
— requirements relating to specific construction elements of buildings/structures, applicable equipment, technologies and materials (adopted in June 2010).

These EE requirements will identify the parties (developers/builders/owners) responsible for implementation. One of the most important requirements in the short term will be the posting of **EE classes** on the facades of residential buildings.

Energy meters

Every building must be fitted with an **energy meter** by specified deadlines.

As of 1 January 2011, all commercial and industrial buildings and structures are required to be equipped with water, natural gas, thermal energy and electrical energy meters. In flats and residential buildings, the water, thermal energy and electrical energy meters, both collective (for the whole building) and individual (for separate flats), must be in place as of 1 July 2012 (by 1 January 2015 for gas meters).

However, in practice, the above requirements have not yet been fully complied with.

Liability

Failure to comply with the EE requirements on design, construction, reconstruction and major repairs, as well as failure to comply with energy-meter fitting requirements, may result in administrative liability[4].

EE requirements for public sector

One of the main priorities of the Law is the public sector. For instance, **energy consumption reduction targets** are set for publicly financed institutions. Over the 2010-2014 period, they must

[4] A 'per breach' penalty for company officials at the rate of RUB 20,000 - 30,000 (EUR 425 - 638); for individual entrepreneurs – RUB 40,000 - 50,000 (EUR 851 - 1,064); for legal entities – RUB 500,000 - 600,000 (EUR 10,638 - 12,765).

reduce their consumption of water, natural gas, thermal energy, electrical energy, coal and black oil by at least 3% per year to achieve a **15% reduction (based on 2009 figures)**.

Companies with state participation and companies carrying out regulated types of activities are also obliged to adopt and implement programmes aimed at increasing EE.

Public procurements

All purchases by state or municipal clients must be made in accordance with ES and EE requirements fixed by the Ministry of Economic Development with the agreement of the Ministry of Energy, the Ministry of Industry and Trade, and the Federal Anti-monopoly Service. These requirements which concern the public procurement of certain types of goods, works and services whose performance requires considerable amounts of energy consumption include, in particular:

— limits on energy consumption; and
— technological solutions influencing the EE of goods/works/services ordered.

The federal authorities referred to above must monitor and analyse the EE of publicly procured goods, works and services on an annual basis, and they must prepare annual proposals for reviewing the EE requirements for public procurement.

Energy service agreements

Energy service agreements are entered into between a customer (private or public sector) and a contractor to provide works and services aimed at ES and greater EE.

These agreements must include the following **mandatory conditions**: (i) the volume of ES guaranteed by the contractor; (ii) the expiration date (which may not be less than the term necessary to achieve the ES set by the agreement); and (iii) other mandatory conditions required under Russian legislation.

The **discretionary terms** of an energy service agreement may include, among other things (i) a clause setting the price for the works and services, subject to the results attained or expected to be attained upon the performance of the contract (e.g. the value of ESs); and (ii) a clause stipulating the obligation of the contractor to install and commission energy meters.

Clauses containing the essential elements of an energy service agreement may be included in contracts of sale and purchase, supply and transport of energy resources (except natural gas not used as motor fuel). Model terms of these contracts have been approved by the Ministry of Economic Development.

Energy audit mechanisms

The Law provides for two main types of energy audit: **voluntary** and **obligatory**. As a general rule, energy audits are deemed voluntary, except under circumstances stipulated by the Law[5].

[5] According to art. 16 of the Law, an obligatory energy audit must be conducted, in particular, in respect of: (i) certain regulated companies; (ii) companies producing or transporting energy resources (oil, gas, etc.); (iii) companies investing in ES and EE and

Energy audits may only be conducted by companies and individual entrepreneurs who are members of self-regulated organisations. The audit should be aimed at:

— collecting objective data on the volume of energy used;
— defining EE indicators;
— defining the ES potential and increasing EE; and
— developing and evaluating a list of possible programmes which target EE increase.

The results of the energy audits must be reflected in an **energy passport** comprising of information on the presence of energy meters, the volume of energy used and the variations of such volumes, etc. Copies of energy passports are forwarded to the Ministry of Energy. This Ministry is responsible for processing, systematising and analysing the information contained in these energy passports.

Incentives

In order to encourage private investors to participate in the EE programme, the Law proposes a range of financial/tax incentives.

For example, tariff-regulated energy-transport companies may take advantage of two incentives: either by grossing up sale proceeds by the amount of expenses incurred in reducing energy loss for a period of up to five years; or retaining savings generated as a result of investments in EE and ES for a period of five years or more.

The tax and financial incentives for commercial companies include, in particular:

— investment tax credits up to 100% for companies investing in EE and ES technology;
— accelerated depreciation of assets categorised as having high EE or assets classified in the top EE class ("**Qualifying Assets**");
— three-year corporate property tax exemption on newly accounted for Qualifying Assets; and
— partial compensation of interest on loans granted by Russian banks for the purpose of investing in ES and increased EE technology.

financed by federal, regional or local budgets; and (iv) companies with a yearly energy consumption exceeding the threshold set by the Government of the Russian Federation. The above companies must conduct energy audits at least once every five years.

Anti-corruption and compliance

General approach

Over the past decade, a number of anti-corruption measures have been introduced at the legislative and executive levels in Russia. However, the issue cannot be resolved all at once and the level of corruption in Russia is widely assumed to be relatively high.

Recent developments and trends

As part of the Public Security Concept 2013-2020 approved on 20 November 2013, the President's National Anti-corruption Plan for the period 2012-2013 has been impliedly 'prolonged' for 2014. The main goals of the Government remain (i) to study the issues relating to conflicts of interest for certain categories of public officials; (ii) to organise training for federal officials involved in combatting corruption; and (iii) to consider how the Government can reduce the financial attractiveness of corruption.

Since 1 January 2013, Russian organisations have been obliged by law to develop and implement anti-corruption measures (please see the *Compliance requirements for companies* section below).

A hotly debated law prohibiting public officials and their relatives from owning bank accounts and keeping funds and valuables abroad was enacted on 7 May 2013 (Federal Law No. 79-FZ). This law also imposes an obligation on public officials and their relatives to disclose information on real estate they own abroad and liabilities they owe abroad.

In December 2013, a new Department for Counteracting Corruption was created within the Administration of the President by Presidential Decree No. 878 dated 3 December 2013. The aim of this new governmental body is to check the validity of information provided in declarations of income, property and expenses as well as to conduct conflict checks involving Russian public officials.

Legal framework

Relevant legislation

For many years, there was very little anti-corruption legislation in Russia. However, in 2008, the first National Anti-corruption Plan was announced. As part of that Plan, Federal Law No. 273-FZ "On Fighting Corruption" was enacted on 25 December 2008 (the "**Anti-corruption Law**"). This law remains the principal legislative act on bribery in Russia. However, the relevant legislation is by no means consolidated and relevant provisions are found in a number of legal acts.

Russian law in this area is also affected by international treaties.

The current legislation on corruption now includes:

- International legislation:
  - United Nations Convention against Corruption dated 2003 (ratified by Russia in 2006);
  - Criminal Law Convention on Corruption No. 173 by the Council of Europe (ratified by Russia in 2007); and
  - OECD Convention on Combating the Bribery of Foreign Public Officials in International Business Transactions dated 1997 (ratified by Russia in 2012).
- Federal legislation directly addressing corruption:
  - the Anti-corruption Law;
  - Federal Law No. 230-FZ "On Monitoring the Correlation of Expenses by State Officials with their Incomes" dated 3 December 2012;
  - Federal Law No. 79-FZ "On the Prohibition for Certain Categories of Individuals to Open and Have Accounts, Keep Moneys and Assets in Foreign Bank Accounts outside the Russian Federation, Own and/or Use Foreign Financial Instruments" dated 7 May 2013;
  - Federal Law No. 172-FZ "On Anti-corruption Examination of Regulative Acts" dated 17 July 2009;

- Law No. 2202-1 "On Public Prosecution" dated 17 January 1992;
- Federal Law No. 79-FZ "On Public Civil Service" dated 27 July 2004 (the "**Public Civil Service Law**");
- Federal Law No. 262-FZ "On Access to Information on Court Activities in the Russian Federation" dated 22 December 2008;
- the Criminal Code of the Russian Federation dated 13 June 1996 (the "**Criminal Code**"); and
- the Code on Administrative Offences of the Russian Federation dated 31 December 2001 (the "**Code on Administrative Offences**").

— Federal legislation indirectly addressing corruption, such as:
- Federal Law No. 3-FZ "On Police" dated 7 February 2011;
- tax law (please see the *Disclosure rules* section below); and
- Federal Law No. 94-FZ "On the Placement of Orders for the Procurement of Goods, Works or Services for Public or Municipal Needs" dated 21 July 2005 (the "**Public Procurement Law**") – (please see the *Example of sector-specific anti-corruption measures* section below).

— Decrees of the President, the Federal Government and other executive bodies, adopted in the period 2008-2013, specifically:
- establishing the National Anti-corruption Plan (includes a list of steps and measures to be taken with a view to fighting corruption); and
- regulating the anti-corruption examination of the acts of governmental bodies.

However, the legislation is still fragmentary and sometimes confusing.

In addition to Russian law, laws of other states may be applicable to situations in Russia. The United Kingdom Bribery Act of 2010 and the United States Foreign Corrupt Practices Act of 1977, have a wide extraterritorial reach.

State agencies

Apart from the general law enforcement authorities (the police, public prosecution, etc.), several state agencies have responsibility for enforcement of federal anti-corruption measures, such as the President's Council on Counteracting Corruption (as a supervising body) and the Ministry of Justice (responsible in particular for the anti-corruption screening of draft legal acts). The Office of the Prosecutor General also investigates instances of corruption in criminal matters. Special parliamentary committees have also been established to monitor the income and assets of the members of Parliament.

Compliance requirements for companies

Relevant amendments to the Anti-corruption Law came into force on 1 January 2013. They require Russian companies, representative offices and branches of foreign companies to

develop and implement internal measures aimed at preventing bribery. These include, amongst others, appointing compliance officers, adopting internal codes of ethics and policies for all employees, co-operating with law enforcement authorities.

In April 2013, the Russian Ministry of Labour and Social Protection issued non prescriptive guidelines on the development and implementation of anti-corruption measures.

The guidelines provide the following eight principles for bribery prevention:

— conformity of an organisation's anti-corruption policy with current legislation and generally accepted rules;
— staff involvement;
— proportionate anti-corruption measures;
— efficiency of anti-corruption measures;
— liability and inevitability of sanctions;
— business transparency; and
— constant control and regular monitoring.

To date, no sanctions are provided for failure to take anti-corruption compliance measures. However, in the event of checks by the authorities (police, public prosecutor, etc.), an order to remedy the failure can be issued against the delinquent company. In turn, failure to implement this kind of order carries administrative sanctions, namely fines and/or the disqualification of the company's general director from holding office for up to three years.

Concept of corruption in Russian law

The Anti-corruption Law defines corruption as:

— the abuse of an official rank or powers;
— giving or receiving a bribe;
— commercial bribery;
— other illegal use of official rank by an individual contrary to the lawful interests of the state and society for the purpose of any form of material benefit for oneself or others; or
— the illegal provision of a material benefit to a public official by another individual on their own behalf, or on behalf of or pursuant to the interests of a legal entity.

Material benefit includes money, valuables, other property or pecuniary services, benefits of a "property character" (*"imushestvenniy kharakter"*, e.g. travel offers), and other property rights.

Bribery is subject to the Criminal Code and consists of two interdependent elements: (i) the giving of a bribe; and (ii) the taking of a bribe. They are committed simultaneously and result in two separate crimes.

According to the Anti-corruption Law, a bribe involving money and other assets may be a property-related benefit, service or a favour, and must have a monetary value (renovation, building a house, etc.). Property-related services may include the transfer of property at

an undervalue, a reduction of lease payments or loan interest rates.

If these benefits are provided to family members or friends of the official, with the official's approval or consent, and the official has used his/her official powers to the benefit of the briber, this also constitutes bribery.

Commercial bribery is the illegal transfer of material assets to a legal entity's manager in connection with his/her position as well as the unlawful rendering of property-related services, or the granting of other property rights to him/her for taking action (or refraining from action) in the interest of the giver.

Possible targets of bribery

Even though the Anti-corruption Law contains a commercial bribery element, public officials constitute the main target of the legislation.

Definition of public officials for the purpose of anti-corruption legislation

For the purpose of Russian legislation public officials include any official or functionary executing managerial, regulatory, administrative or economic (financial) functions. Specifically, these officials hold state (i.e. federal or regional) or municipal offices established by law and discharge those functions entrusted by law, specific normative acts or on the basis of an order of a respective superior official.

Officials without executive authority may still commit breaches of the Anti-corruption Law when, in their official capacity: (i) they have the opportunity to prompt another official to act (or refrain from acting) and; (ii) they have been bribed for general patronage or connivance. Even if a briber is coerced into offering a bribe by a person presenting himself/herself as an official, the former may still be liable for a bribery offence.

Prohibitive measures for public officials

Under the Public Civil Service Law, public officials are prohibited from:

— engaging in entrepreneurial activities;
— receiving from legal entities or individuals remuneration in cash or non-cash gifts (except for gifts with a value of up to RUB 3,000 (EUR 64[1]) given during official events);
— travelling abroad at the expense of legal entities or individuals; and
— disclosing confidential or relevant information obtained during civil service in favour of legal entities or individuals after retirement.

The Public Civil Service Law also stipulates a mechanism for regulating conflicts of interest involving public officials.

Disclosure rules

Under Russian tax law, public officials and their close relatives (their spouses and minor children) must file compulsory income declarations. The tax authorities and the newly established Department for Counteracting Corruption are

[1] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience throughout this guide.

empowered to check the income of officials and demand an explanation as to the origin of their assets, if these assets do not correlate with the income level of the individual.

A new requirement for public officials and their close relatives to disclose expenses that exceed their declared income was introduced as of 1 January 2013. It applies to expenses incurred since 1 January 2012 in connection with the acquisition of immovable property, motor vehicles, securities and/or participations in legal entities.

Public officials may be dismissed for loss of confidence by their 'employer'. Their dismissal may result from a conflict of interest while in public service, or from a failure to disclose income or expenses which should have been disclosed. If it is discovered that an official is involved in entrepreneurial activities or affiliated with legal entities, he/she must be dismissed on these legal grounds.

Responsibility and penalties for corruption

Laws enacted in 2008-2012 have substantially increased the penalties for corruption in Russia. Specifically, fines for offering and accepting bribes are now calculated as multiples based on the amount of the bribes (i.e. the higher the bribe, the higher the fine).

Public officials

Apart from bribery, the Criminal Code holds public officials liable for crimes committed against the state and/or municipal authorities, such as:

— abuse of powers;
— exceeding rank and authority;
— illegal entrepreneurial activities; and
— forgery by an official.

If a public official is prosecuted for several crimes, the court will first consider each of them independently and then as a whole to determine the gravity of the offence and resulting sentence.

Under the Criminal Code, only individuals may be held liable for crimes specified in the Code (including bribery/commercial bribery); however, legal entities may be punished for corrupt activities under the Code on Administrative Offences. The liability of a legal entity does not exempt a culpable individual from liability, and vice versa.

Individuals

Individuals are subject to:

— liability to reimburse losses in full (under the Russian Civil Code);
— disciplinary actions resulting in the termination of employment (under the Russian Labour Code);
— up to 10 years' imprisonment for abuse of authority;
— up to 6 years' imprisonment for commercial bribery (for the bribe giver);
— up to 12 years' imprisonment for abuse of authority in conjunction with commercial bribery;
— up to 15 years' imprisonment for a public official who receives a bribe;
— up to 12 years' imprisonment for

bribe giving; and/or
— disqualification of a bribed public official from holding public office for up to three years.

In addition to or instead of the above-mentioned liability, those giving or receiving bribes (including commercial bribes) may be fined 10 to 100 times the amount of the bribe offered/received.

Legal entities

Legal entities may be prosecuted for:

— the illegal employment of a current or former public official, carrying a fine up to RUB 500,000 (EUR 10,638); and
— the illegal payment of a bribe on behalf of a legal entity, carrying a fine of at least RUB 1 million (EUR 21,276) plus seizure of the amount paid.

Example of sector-specific anti-corruption measures

The Public Procurement Law contains provisions which are designed to counter bribery by:

— requiring the holding of auctions or competitive tenders for the purchase of goods, works and services for federal, regional and municipal needs ("**Public Procurement**");
— regulating in detail the procedural aspects of Public Procurement (including requirements applying to tender participants);
— prohibiting tender rules that limit the number of participants; and
— requiring Public Procurement decisions to be adopted by more than one public official (i.e. shared responsibility in adopting these decisions).

Intellectual property

General approach

Over recent years Russia has demonstrated its willingness to reinforce its efforts in combating the infringements of intellectual property rights.

Negotiations aimed at Russia's accession to the World Trade Organisation led to Russia becoming a member in 2012. In the run-up to WTO accession, Russia adopted new legislation matching international standards for the protection of intellectual property rights by, in particular, increasing sanctions for and improving legal mechanisms to combat infringements of intellectual property rights. The resulting legal framework in the field of intellectual property is generally in line with international standards, allowing right owners to adequately protect their intellectual property rights.

Fresh examples of Russia's commitment to advancing the fight against copyright infringements include the adoption of:

— a law that connected administrative fines for the production of fake

goods with the number of fake goods produced in summer 2013;
— the so-called 'Anti-piracy Law'[1] which applies to the procedural issues of blocking infringing film content on the Internet (please see the *Intellectual property rights infringements* section on page 154); and
— a set of amendments to the Russian Civil Code (the "**Civil Code**") in spring 2014 expressly providing for:
  - the presumption of guilt of intellectual property rights infringers; as well as
  - the legal possibility of contacting Internet providers with a request to stop the infringement of intellectual property rights on the Internet.

International standards

Russia is a party to a number of the most important international treaties and conventions covering different intellectual property aspects, including:

— the Convention establishing the World Intellectual Property Organisation;
— the Universal Copyright Convention;
— the Berne Convention for the Protection of Literary and Artistic Works;
— the Paris Convention for the Protection of Industrial Property;
— the Madrid Agreement on the International Registration of Marks and the Madrid Protocol;
— the Singapore Treaty on the Law of Trademarks;
— the Nice Agreement on the International Classification of Goods and Services for the Purposes of Registration of Trademarks;
— the Patent Cooperation Treaty;
— the Locarno Agreement Establishing an International Classification for Industrial Designs;
— the Geneva Convention for the Protection of Producers of Phonograms against Unauthorised Duplication of their Phonograms; and
— the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).

General legal framework

Civil Code

The need to ensure consistency in the legal regulation of intellectual property has led to the adoption of Part IV of the Civil Code. This codifies the existing general legal rules concerning intellectual property rights whilst introducing some new provisions and principles.

Part IV of the Civil Code came into force on 1 January 2008 and replaced previous legislation regulating intellectual property rights, including the copyright law, the trademark law, the patent law and the software law. It was modernised as part of the Civil Code reform by the enactment on 12 March 2014 of a set of amendments concerning intellectual property rights (the "**Civil Code Amendments**") coming into force on 1 October 2014. The main changes are reflected below.

Part IV of the Civil Code includes an exhaustive list of intellectual property

[1] Federal Law No. 187-FZ dated 2 July 2013.

rights and the various legal methods for protecting these rights. It also stipulates some general requirements concerning their use and their enforcement.

Regulatory orders

In addition to Part IV of the Civil Code, certain intellectual property issues are regulated by orders of the Federal Service for Intellectual Property ("**Rospatent**").

Rospatent is subordinated to the Ministry of Education and Science and it is responsible for the registration of intellectual property rights to trademarks, patents, software, databases, as well as for the registration of, alienation of, and encumbrances over these registered rights.

Novelty in the judicial sphere

The Russian Intellectual Property Court (the "**IP Court**") was launched in 2013. As expected, this has led to an increase in professionalism and sound legal approach with regard to judgments in this field, not only from the newly established court but also across the Russian court system as a whole (please see the *IP Court* section on page 155).

Contractual aspects of intellectual property rights

Licence agreement

General

A licence agreement grants the right to use intellectual property rights within the limits set out in the agreement.

Under the Civil Code licence agreements must set out the following information:

— the licensed object;
— the duration of the licence;
— the territories for which the licence is granted;
— the manner in which the licensed object may be used; and
— the remuneration amount or how it is to be calculated.

The licence may be granted on an exclusive or on a non-exclusive basis. By granting an exclusive licence, the licensor is not only unable to issue subsequent licences to others, but is also prohibited from itself using the rights transferred under such licence, unless otherwise provided for by the parties. If the licensee is granted with the right to issue sublicences, this must be expressly provided for in the agreement.

Licences are deemed to be granted for consideration, even if the licence agreement is silent on remuneration. The agreement may fix the amount of remuneration (royalty payments), or set out a method to determine it. Remuneration may take the form of a lump-sum fixed in advance and delivered as a single payment, periodical royalties, or as a percentage of revenues.

Commercial entities are now prohibited from entering into licence agreements worldwide and for the whole term of the respective IP protection on a free-of-charge basis.

Shrink-wrap licences

The Civil Code permits the use of shrink-wrap licences for software and databases which may be granted to each user (i.e. where the conditions of the licence are provided for on the wrapping

of the CD (or other means of delivery) and the first use of the software or database by the consumer means they agree to adhere to the conditions of the licence). This type of licence agreement is considered to be royalty-free, unless otherwise provided for in the respective licence agreement.

Open licences

The Civil Code Amendments introduce the legal concept of an open licence to use works of science, literature or art. In essence, this type of licence is deemed to be a contract of adhesion and the law therefore requires the terms and conditions to be freely accessible to anyone who wishes to review them.

Licence conditions must contain the scope of the use of the work. Unless otherwise stated in the licence conditions, licences will be granted free-of-charge and be valid throughout the world for five years (if the open licence is for computer programmes and databases, this will be for the duration of the exclusive rights).

Assignment of exclusive rights

According to the Civil Code, this contract involves transferring the full and exclusive rights and title to an object of intellectual property rights for the entire period during which these rights are protected. Notably, the Civil Code Amendments expressly prohibit free-of-charge assignment agreements between commercial entities (unless otherwise regulated by the Civil Code).

Governmental registration of contracts

If a trademark, software, database, invention, utility model or design is registered with Rospatent, then any licence, assignment contracts or pledge contracts (as expressly provided for by the Civil Code) also require registration with Rospatent in order for the contract to be valid for third parties.

Rights over the results of intellectual activity

Copyright and neighbouring rights

Copyright

Copyright covers scientific, literary or artistic work that is the product of creative work regardless of the value, type or mode of expression of the work. Copyright protects both disclosed and undisclosed works. Copyright protection arises when a work is created. There are no registration requirements.

Chapter 70 of the Civil Code gives an author certain rights over his/her work. It sets out exclusive property rights over the work, as well as moral rights for the author of the work.

These exclusive rights include (among other things) the:

- right of reproduction;
- right of distribution;
- right of demonstration to the public;
- right to import or export originals; and
- right to provide access to the work by any means of telecommunication (including the Internet).

Moral rights include in particular the:

— right of authorship;
— right to the name;
— right to preserve the integrity of the work; and
— right of publication.

The exclusive rights to the works are protected for the lifetime of the author plus 70 years.

Infringement of copyright results in civil, criminal and/or administrative liability.

Neighbouring rights

Neighbouring rights cover the creation and use of performances, phonograms, broadcasting programs, cable distribution organisations, and databases.

The owner of neighbouring rights may be the performer of phonograms, the creator of databases or the broadcaster of media (which has been created by the broadcaster).

Under the Civil Code performers enjoy exclusive property rights and moral rights, whilst radio and television broadcasters enjoy only exclusive property rights.

The holding and the exercise of neighbouring rights is not subject to any mandatory registration formalities.

The rights enjoyed by owners of neighbouring rights may be granted by virtue of a licence agreement, or a contract for the exclusive assignment of rights.

Patents

Patent protection covers:
— **inventions**, which are a technical solution in any field related to a product or a process;
— **utility models**, which are the devices being results of intellectual activity in the scientific and technical spheres; and
— **industrial designs**, which are the result of intellectual activity in relation to the appearance of the product.

Chapter 72 of the Civil Code regulates the protection of inventions, utility models and industrial designs.

Patent protection is subject to conditions, which depend on the type of object being protected.

An invention can only be protected if it is:
— new;
— has an inventive step; and
— is capable of industrial application.

A utility model can only be protected if it is:
— new; and
— capable of industrial application.

An industrial design can be protected only if it is:
— new; and
— original.

The concepts of the dependent invention, dependent utility model and dependent industrial designs have been defined in the Civil Code Amendments. To use them, it will be necessary to be authorised by the patent holder of the inventions, utility models or industrial designs. Without such authorisation, the dependent objects of intellectual property cannot be used. Unlike copyright, which protects the author's work from the day of its creation, a

patent is only protected after being registered with Rospatent. The right to obtain a patent belongs to the inventor, his/her employer (in case of an employee's invention) or to their assignee(s). The patent application is filed with Rospatent for examination. Rospatent will grant the patent if the relevant criteria are met.

The maximum duration for patent protection is as follows:

— 20 years from the filing date of a patent application for an invention, with the possibility of up to a 5-year patent term extension;
— 10 years from the filing date of a utility model application, with the possibility of up to a 3-year term extension; and
— 15 years (from 1 January 2015, 5 years) from the filing date of an industrial design application, with the possibility of up to a 10-year term extension (from 1 January 2015, a 5-year term extension, which may be renewed so that the entire period of life of a design patent may be up to 25 years).

The patent licence and/or any assignment agreement needs to be registered with Rospatent. It is also possible to obtain a compulsory licence, following the decision of a court. Rospatent also registers open patent licences, which may be chosen by the owner of the patent.

According to the Civil Code Amendments, industrial design applicants will no longer need to file a list of essential features of the design by registration, which has traditionally been serving as the basis for determining the scope of protection of the design. This means that designs will be protected within the scope of the image of the design and its description. This change has narrowed the scope of protection of industrial designs.

Trade secrets and know-how

IP-related information which has actual (or potential) commercial value can be defined as a trade secret or know-how as long as the necessary criteria are met. In particular, the information must be unknown to third parties because there is no free access to it. Further, the owner of the trade secret must take active measures to protect the secret and ensure that there is no free access to it (in particular, by implementing the so-called 'trade secrecy regime').

The Law on Trade Secrets[2] (as last amended on 12 March 2014) defines the information that constitutes a trade secret and lists the measures that the right owner should take in order to ensure the protection of know-how. The law also provides for civil, administrative and criminal liability for a breach of trade secret rights.

Employees' work and employees' invention

The Civil Code regulates employees' work. This includes literary work and patented objects that are created by employees as part of their employment duties.

[2] Federal Law No. 98-FZ "On Trade Secrets" dated 29 July 2004.

As a general rule, exclusive rights to the results of an employee's intellectual activities belong to the employer.

However, if the employer fails to use, license or assign its employees' work within a prescribed period, or the employer fails to notify the employee that it has decided to keep the work secret, the exclusive rights to the work (or invention) will be transferred to its author, i.e. the employee. This does not apply to know-how.

If the employer has started to use the work, assigned the rights to it, or has decided to keep it secret, the employee is entitled to a remuneration amount as agreed between the parties. If the parties fail to agree on the sum, then a competent court may set the remuneration. As clarified by the Civil Code Amendments, the right to remuneration from the employer is not inheritable. However, the rights from the agreement concluded between the employee and the employer as well as any outstanding remuneration which the employer has not paid are transferred to the employee's heirs.

Trademarks, appellations of origin, company names and trade names

Chapter 76 of the Civil Code provides for the protection of means of individualisation, i.e. the protection of those intellectual property rights that are used to distinguish and identify companies or the goods or services they offer.

Company names

The company name is indicated in the corporate documents of the company, and it is reflected in the Unified State Register of Legal Entities. The company name is protected in Russia upon the company's registration with the tax authorities.

The exclusive right of a company over its company name may not be transferred or licensed to third parties. This exclusive right allows the owner of the company name to freely use the name, in particular, (i) on signs; (ii) on letterheads; (iii) on official documents; (iv) in advertising; (v) on products; and (vi) on packaging.

Additionally, the company name may be protected as a trademark or as a commercial name (a trade name).

Trade names/commercial names

Legal entities may use trade names separately from their company name. Unlike the company name, the trade name is not necessarily mentioned in corporate documents, or in the Unified State Register of Legal Entities. The trade name may be used to distinguish a legal entity. A legal entity can have only one trade name. A legal entity may not use a trade name which would create confusion with a third party's company name or trademark or which would mislead consumers. The right to use a trade name to individualise a Russian company is valid throughout Russia.

This exclusive right ceases to exist if the owner does not use the trade name for one year. The right to use a trade name

is protected independently, regardless of the company name or trademarks. It may be transferred by a franchise agreement, or by a contract for the lease of an enterprise.

Trademarks/service marks

A trademark is a designation which is used to distinguish the goods or services of companies. A trademark can be a word, figure or a three-dimensional designation, or a combination of all of these elements. The Civil Code provides a list of words and designations that may not be used as trademarks.

To be protected in Russia, the trademark needs to be registered with Rospatent in the Register of Trademarks. Alternatively, it may be protected in Russia under the Madrid System of the International Registration of Marks.

The maximum duration of trademark protection is ten years, which is calculated from the date of filing of the application with Rospatent. There is an option to renew this protection period, subject to the necessary petition and payment being made.

As a general rule, the exclusive rights to a trademark are transferable to third parties, unless this assignment would be misleading for consumers. The exclusive right to use a trademark may also be licensed. This may grant a third party the right to use that trademark within the framework of the licence, and in accordance with the quality requirements set out by the licensor.

Trademark protection may be terminated early if the trademark is not sufficiently used during any three consecutive years after the date of registration. Any interested person may file an application for non-use invalidation with the Chamber of Patent Disputes under Rospatent.

Information on applications for the registration of a trademark is to be published in the official gazette of Rospatent as well as in Rospatent's online database according to the Civil Code Amendments. As of 1 October 2014, any person will be able to object to a particular trademark as soon as this information has been officially published.

Appellation of origin of goods

The appellation of origin of goods is the name of the place where the goods come from. It may designate a country name, a city or any geographical area referring to the place of origin of the product.

An appellation of origin registered with Rospatent is protected throughout Russia. Any producer (or group of producers) acting within the geographical area designated by the appellation of origin may enjoy the right to use that name provided it has first obtained a certificate from Rospatent and, if the appellation of origin has not yet been registered, to register it.

The newly introduced system of official publication of trademark registration applications and right to object described above will apply to appellations of origin.

Intellectual property rights infringements

Situation in Russia

Counterfeiting and piracy are difficult to quantify in general, and this is especially true in Russia. It affects all areas of the Russian economy, including: consumer products, automotive, pharmaceuticals, etc. Counterfeit and pirated products are mainly distributed through 'open-air' markets, although they may often be found in reputable department stores.

Recognising the magnitude of the problem and its potential impact on consumers' health and well-being (especially with regard to pharmaceuticals), Russia has demonstrated a willingness to fight counterfeiting and to ensure the compliance of its laws and enforcement mechanisms with international standards.

When counterfeit or pirated goods are imported to Russia, Russian customs officers can assist right owners in stopping the infringement of their intellectual property rights. However, the competence of customs officials is limited to copyrights and trademark rights (it does not cover inventions, utility models or designs).

Notably, parallel importation is considered as a trademark infringement in Russia, although recent trends in the court practice and relevant legislative initiatives are controversial in this respect.

Liability

Russian legislation provides for civil, administrative and criminal liability for the infringement of intellectual property rights. The sanctions depend on the amount of the fake products involved and on whether the individuals or legal entities involved are repeat offenders.

Civil penalties

The civil law route entitles the trademark owner to claim in court for the:

- termination of the infringement;
- seizure/destruction of the counterfeit goods (or removal of counterfeit signs or labels); and
- payment of compensatory damages or statutory liquidated damages (in an amount of RUB 10,000 - 5 million (i.e. from EUR 213 - 106,383[3]), or double the value of the infringing goods or of the right to use the infringed trademark under regular market conditions).

Since 1 August 2013 the Anti-piracy Law provides film copyright owners with a new efficient tool of copyright enforcement, web blocking injunctions. It is expected that this law will be extended in the near future to cover music as well as other copyrighted works.

Sanctions under the Russian Code on Administrative Offences

The trademark infringer is administratively liable if the damage caused by the infringement is less than RUB 1.5 million (EUR 31,915). Various sanctions apply to various infringements.

For example, since August 2013, the levels of the applicable fines for the

[3] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience throughout this guide.

production of fake products depend upon the scope of the infringement, which will be based on the value of the fake products seized.

The most serious sanctions relate to legal entities that produce or sell infringing goods. The fine to be imposed in this case would be triple the value of the infringing products seized, and in any event will never be lower than RUB 40,000 (EUR 851). The fake products will also be confiscated.

Sanctions under the Russian Criminal Code

If the damage caused by the infringement reaches or exceeds RUB 1.5 million (EUR 31,915) or if the offender repeats the offence, he/she may become criminally liable.

The unlawful use, disclosure or appropriation of an invention or patent that has caused significant damage to the author will result in a fine of up to RUB 200,000 (EUR 4,255) or equal to the offender's income for 18 months, or imprisonment for up to two years. Similar sanctions apply to infringement of copyright and to the sale of counterfeit works.

When the offender is a company, criminal sanctions will be applied against the relevant company officials, as legal entities cannot be held criminally liable under current Russian law. This may change in the future since the introduction of corporate criminal liability is on the Russian Parliament's agenda.

IP Court

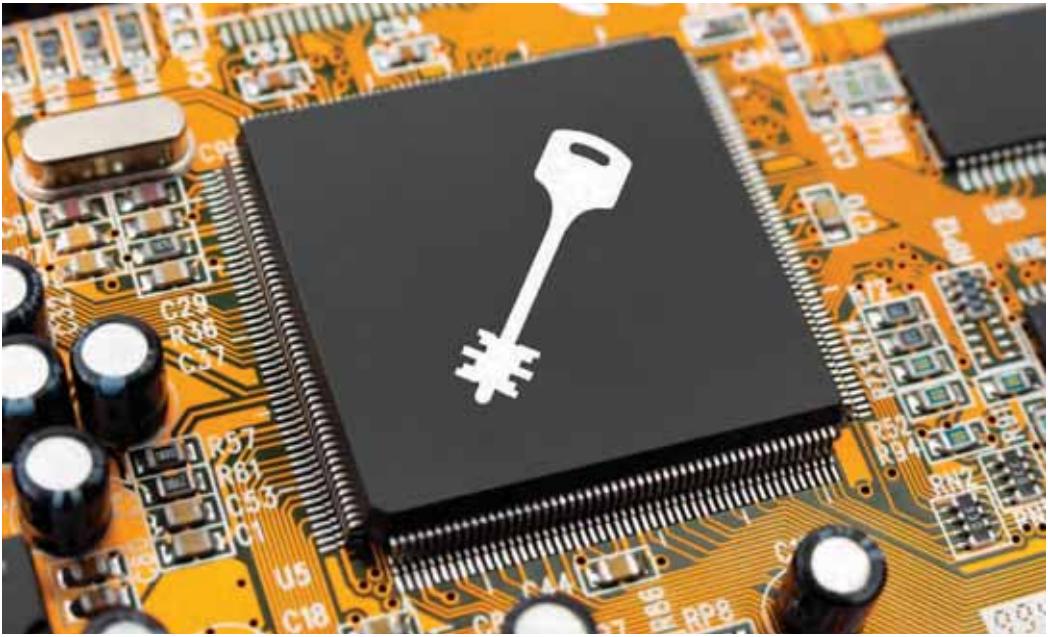
In December 2011, a law on creating the IP Court as part of the Russian commercial court system was enacted. The IP Court, which is located in central Moscow, started its operations in July 2013.

The creation of the IP Court is aimed at (i) improving the specialisation of judges and increasing their professionalism in delivering IP-related judgments and; (ii) relieving the commercial ("*arbitrazh*") courts of the great number of disputes litigated between Rospatent, on the one part, and individual entrepreneurs or legal entities, on the other part.

The IP Court reviews:

— as a court of first instance – challenges of regulatory and legal acts of Rospatent;
— as a court of first instance – claims for the invalidation of the registration of intellectual property rights and disputes over the intellectual property rights ownership; and
— as a court of third instance (i.e. a second appeal or a cassation) – intellectual property rights infringement cases between legal entities and/or individual entrepreneurs.

The cassation rulings of the IP Court can be further appealed to the Supreme Commercial Court of Russia. Other rulings are appealed against at the IP Court.



Personal data protection

General approach

In comparison to European states, data protection is an area of law that developed rather late in Russia. Russia signed the 1981 Strasbourg Convention for the Protection of Individuals with regard to Automatic Processing of Personal Data (the "**Strasbourg Convention**") on 7 November 2001. It entered into force in Russia on 1 September 2013.

Key privacy legislation

The main law regulating this issue, Federal Law No. 152-FZ "On Personal Data" (the "**Data Protection Law**"), was only adopted in July 2006. A number of provisions of the Data Protection Law are based on the Strasbourg Convention.

The Data Protection Law provides a framework that is complemented by a number of regulations of the Russian Government, as well as orders of specific ministries and authorities (some of these regulations and orders have not yet been adopted). Furthermore, some provisions of the Russian Labour Code and the

Russian Code on Administrative Offences are also applicable.

The regulation of data protection in Russia gathered momentum between 2011-2012. In 2011, the Data Protection Law was substantially amended, and new requirements for the protection of personal data processed in personal data information systems were approved by Russian Government Decree No. 1119 dated 1 November 2012.

In contrast, the period from 2013 to spring 2014 brought relatively little change. The same legal gaps remain. For example, regulation that is constantly developing at the international level, such as whistleblowing, big data, BYOD[1] and social media, requires substantial development in Russia. Also, Russian law needs to be updated in line with developing technologies. Particular attention should be paid to how the protection of personal data in relation to cloud technologies will be regulated. Cloud services are increasingly popular within a variety of different business sectors, and the lack of relevant legislation appears to be an obstacle to their development in Russia.

Trends

It is anticipated that in 2014 the legislator's efforts will primarily be directed at:

— closing some remaining loopholes in the regulation of personal data protection – one such bill (No. 416052-6) has already been submitted to the State Duma and is expected to be discussed in 2014; and
— increasing penalties for violations – the relevant bills are expected to be submitted to the Duma in the course of 2014.

However, guidance on the practical implementation of the regulations on personal data protection remains poorly developed and compliance with these regulations represents an issue for companies.

As processing the personal data of individuals represents an important part of their businesses, companies in the healthcare, insurance and banking industries, as well as those selling mass consumption goods, are at the highest risk of sanctions for violations.

Supervisory authority

The authority in charge of supervising compliance with personal data protection requirements is the Russian Federal Service for Supervision in the Sphere of Telecom, Information Technologies and Mass Communications ("**Roskomnadzor**"). Roskomnadzor is empowered to apply administrative sanctions to legal entities and individuals who fail to comply with the requirements of the Data Protection Law.

Scope of the Data Protection Law

The Data Protection Law defines, in particular, personal data and data processing. It also regulates the rights of data subjects, consent rules, cross-bor-

[1] Bring your own device.

der data transfer and the obligations of data controllers.

Personal data

Like the Strasbourg Convention, the Data Protection Law does not contain an exhaustive list of data which is deemed to be "personal data". Thus, what constitutes personal data must be assessed on a case-by-case basis. Personal data is defined as being any information referring directly or indirectly to an identified or identifiable individual. This individual is the data subject.

The Data Protection Law sets forth a special category of data: "sensitive personal data". This covers any information referring to a person's racial or ethnic origin, political opinions, religious or philosophical beliefs, personal health, sex life and criminal record. This concept corresponds with the Strasbourg Convention.

Data processing operations

The Data Protection Law applies to all personal data processing operations performed within Russia. However, in practice, Roskomnadzor has intervened to protect the rights of Russian data subjects in cases of personal data processing abroad. In 2012, Roskomnadzor successfully blocked several websites hosted or managed from abroad that contained Russian citizens' personal data and continued this policy during the period from 2013 to spring 2014[2].

Personal data operations caught by the Data Protection Law include any processing, whether performed manually or automatically. They also include data collection, storage, recording, deletion, transfer, etc. Notably, the Data Protection Law applies when data processing is performed by Russian state bodies, local authorities, legal entities and individuals.

On the other hand, the Data Protection Law does not apply to personal data processing if it is performed:

— by individuals for their private needs,
— in accordance with the Russian legislation on archives;
— in relation to data qualified as a state secret under Russian law; or
— in accordance with Russian legislation on providing information relating to the courts of Russia.

Rights of the data subjects

Under the Data Protection Law a data subject is entitled to:

— request details of the processing of his/her personal data by a data controller (what data is being processed and why, etc.);
— revoke his/her consent to the data processing at any time;
— request, in certain cases, the rectification, blocking or deletion of his/her personal data; and/or
— be compensated for damage suffered (including moral damages).

Obtaining consent from the data subjects

Personal data may be processed (i) with the prior, voluntary, express and informed consent of the individual; (ii) or in cases when the processing without

[2] http://rsoc.ru/personal-data/p581/

consent from the data subject is expressly allowed by law.

Consent can be given in any form that evidences that the consent was given (except for when qualified consent is required by law, as described in the next paragraph). In practice, consent may be given orally, in writing, electronically or by implication. In any case, the data controller must always ensure it can prove that consent was duly obtained.

Obtaining 'qualified consent'

In particular, consent must be obtained in the form of a written document ("**Qualified Consent**") in the following cases:

- the processing of sensitive personal and/or biometric personal data; and
- the cross-border transfer of personal data to countries which do not ensure an adequate level of protection of personal data (please see the *Cross-border transfer of personal data* section below).

Qualified Consent must be established in writing and contain, amongst other things, the following elements:

- name, address and passport details of the data subject;
- name and address of the personal data controller;
- purpose of the personal data processing;
- list of the personal data to be processed for which consent is given;
- list of the operations to be performed with the personal data and a general description of the methods to be used for personal data processing;
- the term during which the personal data will be processed and how consent can be withdrawn; and
- the data subject's signature (either hand written or electronic).

Cross-border transfer of personal data

The Data Protection Law distinguishes two types of cross-border data transfer:

- the transfer of data to countries with adequate protection of personal data ("**Safe Countries**"); and
- the transfer of data to countries without adequate protection of personal data ("**Unsafe Countries**").

Safe Countries comprise (i) signatories to the Strasbourg Convention and (ii) countries that are not signatories to the Strasbourg Convention, but are included in the list contained in Roskomnadzor Order No. 274 dated 15 March 2013.

The cross-border transfer of personal data to Safe Countries may be performed in accordance with the requirements of the Data Protection Law applicable to internal data transfer. As for the cross-border transfer to Unsafe Countries, this requires first obtaining the Qualified Consent of the data subject, except in cases expressly provided by the Data Protection Law.

Data controllers and data processors

The Data Protection Law defines the data controller as an entity (either a state

agency, municipal authority or a legal entity) or individual who, independently or together with others, organises the processing of and/or processes personal data, and determines the purposes and scope of personal data processing, the content of personal data which is to be processed, as well as actions performed with the personal data.

Main obligations for data controllers

The main obligations of the personal data controllers are to:

- notify Roskomnadzor of their intent to process personal data, except when an exception applies (please see the *Exceptions to the requirement to register with Roskomnadzor* section below). However, they can only start to process data after being entered on the register maintained by Roskomnadzor (see http://www.pd.rsoc.ru/operators-registry/operators-list/);
- ensure that the registration data in the register maintained by Roskomnadzor is up-to-date (and make the relevant applications in relation to any updates);
- ensure personal data security (please see the *Technical requirements* section below);
- elaborate and adopt the regulation on personal data, which should describe the procedure of personal data processing (including the list of data, the purposes of data processing, etc.);
- appoint a data protection officer who will be responsible for the organisation of data processing within the company;
- periodically perform the internal audit and assessment of the effectiveness of measures applied to protect personal data; and
- retain control over such measures and the level of protection of personal data (in particular in cases where data processing is outsourced).

Exceptions to the requirement to register with Roskomnadzor

Notification is not required, in particular, to process personal data:

- of employees, when such data is processed by their employer for the purposes of realising their employment relations – employers must however comply with other data processing requirements provided by law (in particular those provided in the Data Protection Law as well as the Russian Labour Code);
- received by the data controller to conclude an agreement with the respective data subject, provided that personal data is not disclosed to third parties and is used for the sole purpose of fulfilling the agreement;
- of members of a public union or religious organisation processed by these unions and organisations for the purposes of their activity, provided that the personal data is not disclosed to third parties;
- made public by the data subject;
- which includes only names, surnames and patronymic names of the

data subjects;
— which is necessary for the issue of a one-time pass to the data subject to enable access to the premises of the controller (or for similar purposes);
— which is included in state databases of personal data (including those created for the purposes of the protection of the security of state and public order);
— processed without the use of automatic processing methods; or
— processed in accordance with regulations on transport security.

Technical requirements

As regards security measures, the Data Protection Law has implemented the Strasbourg Convention's provisions on data security.

Personal data must be protected against unauthorised access, alteration, transfer, disclosure by transfer or deletion as well as damage and accidental destruction. In order to ensure the security of personal data, the data controller must, in particular:

— use technical devices certified by the competent Russian authorities and keep a record of the devices on which the personal data is stored;
— determine the level of damage which may be caused in case of an unauthorised processing of personal data; and
— establish rules relating to access to personal data, etc.

The Data Protection Law does not provide further details on the technical and organisational measures mentioned above, although some detailed requirements are provided in the relevant regulatory orders. The latest was adopted on 11 February 2013 regarding information that is not a state secret but is contained in the state information systems. In the absence of practical guidelines, implementing these requirements is problematic and, at times, impossible.

Outsourcing

Data controllers may outsource the processing of personal data. To do so they must enter into an agreement with a data processing service provider (a "**Technical Processor**"). The agreement must contain certain substantial conditions as set out by the Data Protection Law. Data controllers nevertheless remain responsible to data subjects for the fulfilment of their obligations.

The Technical Processor must ensure the confidentiality and protection of the personal data. In itself technical processing does not require a specific licence. However, licences are needed to provide confidential information protection services and/or to develop specific software for the protection of confidential information (including personal data).

Liability

Administrative remedies and other sanctions

If it is found that a data controller has violated the requirements of the Data Protection Law, Roskomnadzor and/or

the relevant court may:

— require the data controller to rectify the violation(s);
— issue a warning to the data controller; and/or
— impose any of the following fines:
  - RUB 300 - 500 (EUR 6 - 11[3]) on individuals;
  - RUB 500 - 1,000 (EUR 11 - 21) on officials of legal entities;
  - RUB 1,000 - 5,000 (EUR 21 - 106) on legal entities.

A draft law aimed at substantially increasing the fines is currently being discussed. If adopted, fines for legal entities would be raised to RUB 700,000 (EUR 14,894). In specific cases, fines could be as much as 1.5% - 2 % of the revenue of a legal entity for the relevant reporting period.

Judicial remedies

Data subjects can file for court action against a data controller, and in particular, to seek compensation for damage caused as a result of the illegal treatment of personal data.

Criminal law issues

In serious cases, unlawful data processing may also be deemed to amount to an illegal collection and distribution of information on the private life of a person constituting a private or family secret. Under the Russian Criminal Code, such violations are punishable with a fine, compulsory work or imprisonment.

[3] At the notional exchange rate of RUB 47 = EUR 1, as used for convenience throughout this guide.

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