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Doing Business in Russia

2009

Dear reader,

We at CMS have been welcoming investors to Russia for nearly twenty years and we appreciate the importance of good quality information to the success of business here.

To help you, we have put together this introductory guide to the Russian legal system and the principal laws and regulations that are of interest for investors in this exciting, developing market. It is of course no substitute for the expert advice tailored to your project that our specialists will be pleased to provide to you on request.

Russia is changing every day and although this guide describes the laws as at 1 September 2009, please contact us to check it remains up to date. I would also recommend that you subscribe to our free CMS news service through which you will receive our newsletters, articles and invitations to our seminars and events. You can do this by contacting myself or our Head of Marketing, Liza Jensen.

I wish you every success.

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Introduction

Political and Administrative Structure

The President

Under the Constitution of the Russian Federation, adopted on 12 December 1991, (as amended) the President is the Head of State. Currently the President is elected for a four-year term. From the elections in 2012 the President will be elected for a six-year term.

The President appoints the Prime Minister who is the head of the government, and also the Chairman of the Central Bank of Russia. Both appointments are subject to the approval of the State Duma (the lower house of the Russian Parliament).

The President determines the basic direction of Russia's domestic and foreign policy and represents the Russian State both in domestic and foreign affairs. He is commander-in-chief of the Russian armed forces.

The President has broad authority to issue decrees and directives which in practice have force of law. In certain circumstances the President has the right to dissolve the Duma. The current President, Dmitri Medvedev, took office on 7 May 2008. He succeeded Vladimir Putin, who had led the country for the previous eight years.

Executive Power

The executive is headed by the Government of the Russian Federation (Pravitelstvo). The Gov-

ernment has to enact the decisions made by the President and the Parliament.

A major reform of the executive branch was undertaken in 2004. The aim was to create a clearer and more efficient structure, and to reduce the level of bureaucracy.

Legislative Power

The legislative branch of the Russian Federation is the Federal Assembly (Federalnoye Sobraniye).

The upper chamber is called the Federation Council (Soviet Federatsii). There are 166 seats, filled by the representatives of the executive and legislative branches of each of the 83 regional federal blocks.

The lower chamber is called the State Duma (Gosudarstvennaya Duma). It has more power over legislation than the upper chamber. There are 450 representatives who are elected by proportional representation. Current members are elected for a four year term. From 2012 this term will be extended to five-years.

The legislative process consists of several stages. Bills may originate in either legislative chamber, or they may be submitted by the President, the Government, local legislatures, the Supreme Court, the Constitutional Court, or the High Arbitration Court. Bills are first considered by the State Duma and must pass three readings before being passed to the Federation Council. After adoption by a majority of the State Duma's members, 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 Duma and Federation Council. This Commission has to review and amend the bill before it is presented to the Duma again for consideration.

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

Judicial Power

The judicial system is split into three branches:

i. The courts of general jurisdiction;
ii. The '*arbitrazhniy*' or commercial courts; and
iii. The Constitutional Court.

The judicial system is also divided into a federal system and a system of local courts in each of Russia's federal states.

The courts of general jurisdiction deal with criminal, civil and administrative cases involving individuals who are not engaged in business activities. Cases are considered by the district court, unless they fall under the jurisdiction of the magistrates courts or military courts. The head of this branch is the **Supreme Court** of Russia. Decisions of the lower courts can be appealed through the intermediate courts, up to the Supreme Court.

The **commercial arbitration courts** deal with economic disputes involving individuals engaged in business activities, and disputes between legal entities and their participant members (i.e. their shareholders). The arbitration court system consists of the arbitration courts in Russia's federal regions, arbitration courts of appeal, federal arbitration courts and the **Supreme Arbitration Court** of Russia. The Supreme Arbitration Court is the highest court for the resolution of economic disputes.

The **Constitutional Court** has jurisdiction to decide whether federal (and local) legislation and regulations comply with the Constitution. This court also resolves jurisdictional disputes between the federal and local authorities, and may interpret and clarify the provisions of the Constitution.

Federal Structure

The Russian Federation consists of 83 "subjects", i.e. regional states within the federation. The Constitution grants the states a degree of autonomy over their internal economic and political affairs. The head of the executive branch of each state is appointed by the legislative body of that state on the recommendation of the President of Russia.

The Constitution sets out a general list of powers which are reserved to the federal authorities. Some powers are jointly exercisable by the federal and local authorities. The regional authorities are then allocated all other powers not contained in these two lists. 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.

Legal Environment

Foreign Investment

The Russian legal system operates under the provisions 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. Many important market-oriented reforms have been passed: For example there is a civil code governing business relations, and the tax reforms carried out in 2000-2001 have created a more favourable environment for investors. However, Russia does not yet have a stable and fully established legislative system; there are still numerous gaps and ambiguities in current legislation. Bringing the country in line with the standards of a modern market economy is a key priority for the present administration.

The constitution, federal laws and the regional laws of each state form the foundation of the Russian legal system. Presidential Decrees, Orders of the 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 so that if Russia is a signatory to an international treaty that contains provisions contradictory to the provisions of any domestic legislation, the provisions of the international treaty will prevail.

Foreign Investment

The Russian government has stated that it aims to encourage foreign investment. However the creation of a stable and attractive investment climate has proved difficult.

According to the Federal Statistics Service, net capital inflow into Russia, reached a record high of USD 82.3 billion in 2007. This was mainly due to high world oil prices. This was almost double the figure of 2006.

The main legislative acts governing foreign investments is the federal law "On Foreign Investment in the Russian Federation", of 9 July 1999 (the "Foreign Investment Law"). This law states that foreign investors and investments shall be treated no less favourably than domestic investors and investments, subject to certain wide-ranging exceptions. Exceptions may be introduced to protect the Russian constitutional system, the morality, health and rights of third parties, or in order to ensure state security and/or defence. In this regard please see the section on Strategic Industries law. Russian legislation may also introduce special regulations for the promotion of foreign investment. Foreign investment is permitted in most sectors of the Russian economy: for example 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 (which it often is, again see below). In such cases, foreign investors are entitled to receive compensation for their investment and other losses.

Restrictions on foreign investment exist in the insurance and banking sectors. The Law on Insurance of 27 November 1992 (as amended) 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.

There are also restrictions on foreign investment in the banking sector. The Central Bank has the right to use reciprocity as a criterion to specify the types of business that foreign banks may be licensed to operate in Russia. Additionally, a ceiling on the total amount of foreign bank capital, as a percentage of the total bank capital in Russia, is imposed by federal law.

Lobbying

One of the main transformations of the last fifteen years has been the redefinition of relationships between business and the State.

Given how slowly the legal culture has developed in Russia, businesses do not concentrate their lobbying efforts by attempting to influence the drafting of new laws or the actions of the draftsmen. Rather, they try to receive de facto special treatment, such as tax deferments, customs benefits, operation licences and the right to engage in certain kinds of activity.

There are few 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

Types of Structures

Russian legislation provides for several types of business structures including limited liability companies, joint stock companies, representative offices, branches, as well as limited and unlimited partnerships. A basic description of each of these is set out in Part 1 of the Civil Code of 1994 (as amended) – (the "**Civil Code**").

An individual is also entitled to conduct commercial activities in Russia provided he has the status of an individual entrepreneur. The legal framework for individual entrepreneurs is also set out in the Civil Code.

There have been significant developments in Russian corporate law during 2008-2009. Some of these have been implemented specifically as a response to the global economic crisis, whilst some are part of the ongoing development of Russian business law. Overall, the changes represent a significant improvement of the general business environment. The Russian authorities acknowledge that responding to the needs of business is essential if the country is to move forward economically.

A. Russian Legal Entities

Since the two most common types of Russian legal entity are the limited liability company and

the joint stock company (which may be either "open", meaning publicly held, or "closed", meaning privately held), we will focus on these types of company in this section.

1. Limited Liability Company

A limited liability company ("*obshchestvo s ogranichennoy otvetstvennostyu*") is designated by the acronym "OOO" before or after its name. It is the simplest form of Russian company and is often used by foreign investors who want to wholly own their businesses.

The establishment of a limited liability company is governed by the Civil Code and by the Law on Limited Liability Companies of 8 February 1998 (as amended) – (the "**LLC Law**"). Note that key legislative amendments (a number of which are discussed below) affecting limited liability companies came into force on 1 July 2009. For further information please see the CMS Russia Monthly Legal Digest for July 2009.

Capital and Contributions

The **charter capital** of a limited liability company is divided into "participations" or "interest units" ("*doli*"). Unlike the shares issued by a joint stock company, these interest units are not considered to be securities and do not therefore need to be registered with the Federal Service for Financial Markets (the "**FSFM**").

Each holder of an interest unit is referred to as a "participant".

The minimum charter capital of a limited liability company is currently RUR 10,000 (although it is expected to be increased to RUR 1 million).

Contributions to the charter capital of a limited liability company may currently be made in cash or in kind (i.e. securities, property or other tangible or intangible rights having monetary value). Legislative amendments are being considered that would limit contributions to cash only.

Exemptions from import duties and import VAT may be available for certain types of equipment that is contributed to the charter capital of a company by a foreign participant. Generally, any asset that is contributed to the charter capital must be independently valued.

Participation

A limited liability company can be wholly owned by another business entity, provided that the holding entity is not itself owned by a legal entity with only one shareholder or by one individual.

If the number of participants in the company exceeds 50, the company is obliged to either reduce the number of participants, or to re-register as an open joint stock company or production cooperative within a year.

From 1 July 2009 all limited liability companies must maintain a register of participants, which sets out the names of the participants and the number of interest units they have in the company.

As a general principle, the responsibility of participants for the company's liabilities is limited to the value of their interest units. In certain cases however, the corporate veil can be pierced (i.e. where a participant gives binding instructions to the company which lead to the insolvency of the company) resulting in participants having unlimited responsibility for the liabilities of the company.

Management Structure

The management structure of a limited liability company is relatively straightforward and is made up of the general director and the general meeting of participants. A board of directors and/or management board are not required but can be provided for by the charter.

The **general director** manages the day-to-day running of the company and deals with all other issues not falling within the authority

of the general meeting of participants and the board of directors (if there is one). The general director acts on behalf of the company, represents its interests, enters into transactions on its behalf, issues powers of attorney and appoints and dismisses employees. The general director is the only person who can represent the company without a power of attorney. Note that the general director's powers may be limited by the company's charter and his employment contract.

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

Companies are required to hold a general meeting of participants once a year. The company's charter may provide that extraordinary meetings also be held.

The general meeting of participants must be convened according to the procedure set out in the company's charter and the LLC Law.

At a general meeting of participants each participant's voting power will normally correspond to the proportion of the company's charter capital he holds. However, this principle may be varied in the company's charter.

Generally, decisions are adopted by a simple majority of the votes of all participants in the company (although different voting thresholds may be specified in a company's charter, bearing in mind however, that certain thresholds are fixed by law).

Participants can adopt decisions (with the exception of the approval of the company's annual reports and balance sheets) without holding a meeting by way of absentee vote.

A **board of directors** is an optional management body of a limited liability company. The charter defines its authority, which may include appointing/dismissing the general director or approving major transactions and interested-party transactions.

Although there are no restrictions preventing a foreign individual from being appointed as a general director, work permit regulations need to be complied with.

A limited liability company can also have a **management board**. According to Russian mandatory law provisions the general director is the chairman of the management board. Unlike the general director however, the members of the management board must obtain a power of attorney from the general director in order to conduct transactions on the company's behalf.

A charter may provide, or a resolution may be taken at a general meeting of participants, for an **audit commission** or an individual **inspector** to be appointed to audit the company's financial and business activity.

Companies with more than 15 participants are required to have either an audit commission or an inspector.

Transfer of Interest Units

Interest units or participations in a limited liability company are freely transferable to third parties, subject to a statutory right of pre-emption in favour of the other participants and the company itself (if the latter is stipulated by the charter). A charter may also specify that a transfer of interest units between participants is subject to the consent of the other participants and/or the company. The procedure for selling interest units and for determining the offer price for such interest units is set out in LLC Law and may also be addressed in a company's charter and/or participants agreement (if such an agreement has been entered into – see below). In general, a participation interest is transferred upon notarisation of the transfer agreement. Where notarisation is not required (i.e.

for the transfer of company-owned interest units to participants, for the sale of interest units from one participant to another, or the sale of company-owned interest units to third parties) title to the interest units is effective when the transfer is recorded in the Unified State Register of Legal Entities. At the date of writing it remains unclear whether a "preliminary" sale and purchase agreement (i.e. a binding agreement in which the parties agree that they will enter into a transfer agreement in respect of the interest units in the future) and other documents dealing with the disposal of interest units require notarisation. The charter may, *inter alia*, prohibit the transfer of interest units to a third party or make such transfer subject to the consent of the other participants or the company. If such consent is not granted the company itself is obliged by law to purchase these interest units.

Right to Withdraw

Following recent changes in LLC Law a participant of a limited liability company only has the right to withdraw from the company (without the consent of the other participants or the company) if such right is set out in the charter. If a participant exercises this right, his interest units will be transferred to the company on the date that the withdrawal notice is served on the company. The company is then obliged to pay the exiting participant the "actual value" of his interest units in cash. The company may however, pay the exiting participant in kind provided that the participant agrees to this. The calculation of the "actual value" and the time for payment may be set out in a company's charter.

2. Open and Closed Joint Stock Companies

The legislation governing Russian joint stock companies is found in the Civil Code and the Joint Stock Company Law of 26 December 1995 (as amended) – (the "**JSC Law**"). As mentioned above, a joint stock company can either be "open" or "closed". An open joint stock company, (*"otkrytoye aktsionernoye obshestvo"*) is designated by the letters "OAO" and a closed joint stock company (*"zakrytoye aktsionernoye obshestvo"*) by the letters "ZAO", which appear either before or after the company's name.

Capital and Contributions

The **charter capital** of a joint stock company is divided into shares (which may be split into ordinary shares and preference shares). Such shares are securities for the purposes of Russian securities legislation and must be registered with the FSFM.

For an open joint stock company the minimum charter capital is currently RUR 100,000 (although this is expected to be increased to RUR 2 million) and for a closed joint stock company it is RUR 10,000.

As with limited liability companies, **contributions** to the charter capital may currently be made in cash or in kind.

Any increase of the charter capital is made by issuing shares or increasing the nominal value of shares already issued and must be filed and registered with the FSFM.

As a general principle, the responsibility of shareholders for the company's liabilities is limited to the value of their shares. In certain cases however, the corporate veil can be pierced (i.e. where a shareholder gives binding instructions to the company which lead to the insolvency of the company) resulting in the shareholders having unlimited responsibility for the liabilities of the company.

Management Structure

The managing bodies of a joint stock company are: (i) the general meeting of shareholders; (ii)

the board of directors (which is optional for open joint stock companies with fewer than 50 shareholders); (iii) the general director; and (iv) the management board (which is optional).

A **general meeting of shareholders** must be held no earlier than two and no later than six months after the financial year end of the company. Extraordinary meetings may be called by the board of directors, the independent auditor of the company or by shareholders owning more than 10% of the voting shares in the company.

In contrast to a limited liability company, the passing of ordinary resolutions by a general meeting of shareholders only requires a majority vote of the shareholders participating in the meeting (not a majority vote of the total number of shareholders in the company). One voting share gives one vote. Voting thresholds for certain decisions may be set out in the charter subject to those thresholds that are fixed at law.

Shareholders can (subject to certain exceptions) adopt decisions without holding a meeting by way of absentee vote.

The **board of directors** is responsible for the general management of the company and has the authority to take decisions on almost any issue except those issues within the exclusive authority of the general meeting of shareholders.

Members of the board of directors are elected by the general meeting of shareholders to the board for a term that runs until the next annual shareholders meeting. They may be re-elected any number of times.

The **general director** is the only person who can represent the company without a power of attorney. In companies where a management board is also established, the general director is the chairman of that management board. A foreign national may be appointed as general director of a joint stock company subject to compliance with work permit regulations. The general director is responsible for the day-to-day running of the company. He is elected and dismissed by the general meeting of shareholders unless the charter of the company transfers this decision to the authority of the board of directors. If the latter is the case, there is a legal procedure to avoid boardroom deadlocks relating to the appointment or dismissal of the general director when, for any reason, the board of directors fails to agree on this matter.

The authority of a general director can be transferred to a management company by a decision of the general meeting of shareholders. A joint stock company can also have a **management board.** Unlike the general director however, the members of the management board must obtain a power of attorney from the general director in order to conduct transactions on the company's behalf.

Audit

Joint stock companies are required to appoint either an **audit commission** or an individual **inspector** to audit the company's financial and business activity.

An open joint stock company is subject to an annual Russian statutory audit unlike a closed joint stock company which is required to be audited annually only if it meets certain legal criteria.

Note that all joint stock companies may be audited at the initiative of the company's internal audit committee or inspector, upon a decision of the general meeting of shareholders or upon the demand of a shareholder or a group of shareholders holding 10% or more of the voting rights in the company.

Issue and Transfer of Shares

An **open joint stock company** is a "public company" and may make public offerings of

its shares. There are no statutory pre-emption rights (with some exceptions for additional share issues) or restrictions on the transferability of shares in an open joint stock company whether to other shareholders or third parties.

The shares of a joint stock company, whether open or closed, are treated as securities and, as such, are subject to the registration requirements of the Federal Law on Securities Market of 22 April 1996 (as amended). When issuing new shares all joint stock companies must prepare and file with the FSFM a copy of any decision to issue shares, a report on the results of the share issue and, in certain cases, a prospectus for the share issue.

Title to shares in a joint stock company is determined by the register of shareholders that all joint stock companies are required to maintain. Share transfers take effect when recorded in the register and the entitlement to participate in shareholders meetings is similarly determined. The register may be kept by the company itself or by an independent company duly licensed by the FSFM. If the company has 50 shareholders or more then the shareholders register must be kept by an independent registrar.

Shares of a **closed joint stock company** may not be issued to more than 50 shareholders. The transfer of shares in a closed joint stock company is subject to the pre-emption rights of other shareholders in the company (and the company itself if so provided in the charter). The procedure and terms for the exercise of pre-emption rights are set out in the company's charter and are subject to the provisions of applicable legislation.

B. Other Business Structures – Representative Office and Branch

Although foreigners can set up wholly-owned subsidiary companies and may participate in the various forms of partnership prescribed under Russian law, a representative office or a branch remain effective first-entry vehicles into the Russian market.

1. Representative Office Status

A representative office is not a separate legal entity but rather an office set up to represent the interests of its parent company. Although a representative office may, in practice, conduct business in Russia (and a lot of representative offices do so) and may be treated by the tax authorities as a separate profit centre from its parent company, the fact that as a matter of civil law a representative office does not have its own 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 its parent, including arranging marketing and advertising in Russia, negotiating the terms and conditions of agreements on behalf of the parent entity and facilitating the execution of those agreements by the parent company. It may also help 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. Foreign employees of a representative office may still however, obtain personal accreditation which confers certain practical benefits such as the right to import and export personal effects free of customs duty and VAT and which

COMPARATIVE TABLE: OAO, ZAO AND OOO

	OAO (open joint stock company)	ZAO (closed joint stock company)	OOO (limited liability company)
1	2	3	4
Activities	· any types of activities (subject to licensing requirements)		
Term	· unlimited term, unless otherwise provided in the company's charter		
Number of shareholders/ participants	unlimited	1 to 50	1 to 50
Minimum charter capital	RUR 100,000	RUR 10,000	RUR 10,000
Type of interest in charter capital	· ordinary shares · preference shares		· interest units/ participations
Issue of financial instruments	· bonds · other convertibles		· bonds
Subscription for shares	· public subscription	· closed subscription	· N/A
Contributions to the charter capital	· cash · in kind		
Payment of the charter capital	· 50 per cent within three months of the date of registration of the company · the remaining 50 per cent within one year of the date of registration of the company		· 50 per cent before the date of registration of the company · the remaining 50 per cent within one year of the date of registration of the company
Capital increase	· only after the charter capital is fully paid		
Capital decrease	· after notification of creditors and repayment of debts · mandatory decrease in certain cases		
Managing bodies	· general meeting of shareholders · board of directors (optional for an OAO with fewer than 50 shareholders); · general director · management board (optional)		· general meeting of participants · general director · board of directors (optional) · management board (optional)
Transfer of shares/ interest units between shareholders/ participants	· without restriction, 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

1	2	3	4
Transfer of shares/ interest units to third parties	· without restriction	· subject to shareholders' pre-emption rights · 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
Redemption/ Withdrawal	· shareholders may require the company to redeem their shares when they do not agree with certain decisions, including the reorganisation of the company, charter amendments which limit their rights, and the entering into major transactions · the shareholder can sell its shares		· a participant may only withdraw from the company if this is provided for in the company's charter
Expulsion of a shareholder/ participant	· a shareholder may not be expelled from the company		· participants owning at least 10% of the company's charter capital may bring a court action to expel any participant who grossly violates his obligations or whose actions /omissions prevent or materially impede the company's activities
Responsibility of the company	· company is not liable for the obligations of the shareholders/ participants		
Responsibility of shareholders/ participants	· as a general rule, liability is limited to the value of their shares/ interest units		

assists with obtaining multi-entry visas. There has been considerable debate about whether accredited employees of a representative office require work permits but in practice having a work permit should avoid difficulties with Russian state and local migration authorities. A representative office may have a number of different types of bank account including a foreign currency account and rouble 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 Central Bank regulations and other applicable legislation.

As a representative office is merely an extension of a parent non-Russian company, the non-Russian company remains responsible for the liabilities of the representative office.

Management

A representative office is managed by the head of the office, who is authorised to conduct the business of the office and to represent the foreign company by way of 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 a Russian national although an accountant who understands the intricacies of Russian tax and accounting law is a practical necessity.

2. Branch

Status

A branch is also an office set up to represent the interests of its 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 liable for the liabilities of the branch.

Management

As regards management issues they are practically the same as for representative offices. Foreign employees of a branch should also be personally accredited like the employees of a representative office and, in addition, they must obtain work permits with the Federal Migration Service of Russia in order to work in Russia.

C. Other Entities

The Civil Code provides for a range of other entities including simple partnerships (which are not legal entities) as well as full and limited partnerships and additional liability companies which are legal entities. There are also non-commercial organisational forms that may be used for charities, trade associations or other non- profit organisations.

Registration, Liquidation and Reorganisation of Businesses

Having decided on the type of business structure to use in Russia, the next step is to register the chosen vehicle with the relevant authorities. A distinction should be drawn between the registration for legal entities (limited liability companies and both open and closed joint stock companies) on the one hand, and the accreditation and registration of representative offices and branches, on the other.

Registration of a Russian Legal Entity

The Federal Law "On State Registration of Legal Entities and Individual Entrepreneurs" No. 129-FZ dated 08 August 2001 (as amended) establishes a single procedure for the registration of legal entities, regardless of their organisational and legal form and the kinds of economic activities they carry on.

Registration takes approximately two months to complete (i.e. for the company to be fully operational) but often takes longer and the process is quite unpredictable.

The application to register the company can be filed by the applicant in person or can be sent by mail (which adds significant time to the registration process and increases the risk of rejection of the application). The applicant must be the chief executive of the founding parent company or the new company's founder himself (if an individual). It is not possible to appoint an attorney to file the application which means the process of establishment takes longer where the chief executive/founder is unable to file/collect documents in person.

The tax authorities forward the required documents for the new company's registration to the Federal Service for State Statistics and the 3 social funds.

However, it should be noted that delays on the part of the Federal Tax Service are quite frequent and often the newly established company will need to intervene to speed up the process. Before documents are submitted for state registration, the new company must have identified its future premises (as the address is set out in the documents to be filed for state registration) and have a lease agreement or other letter from the owner or landlord, confirming that such premises are guaranteed to the company upon registration.

The application and supporting documents must be notarised and, if they were signed abroad, legalised (where applicable) and accompanied by a certified Russian translation.

Payment of Capital

For a limited liability company, at least 50% of the charter capital must be paid prior to state registration and the balance must be paid within one year of registration. If a founder fails to pay the total amount of its interest units within these time limits, then such non-

Table showing main differences between a Representative Office and Branch

Entity	Representative Office	Branch
Formation	Accreditation limited to three years before renewal	Accreditation limited to five years before renewal
Capacity	Technically restricted to representation but function may be 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
Staffing	May act as employer. Requires head of the representative office and chief accountant	May act as employer. Requires head of branch office and chief accountant
Maximum accreditation or renewal term	3 years	5 years

paid interest units become the property of the company.

For a joint stock company, at least 50% of the charter capital must be paid within 3 months of state registration and the balance within one year of registration.

Registration of the Initial Share Issue

Since shares in open and closed joint stock companies are treated as securities, there are certain additional registration requirements imposed by the FSFM.

Antimonopoly Control

In exceptional cases, the establishment of a company requires prior consent of the Federal Antimonopoly Service. This is the case, for example, where shares or immovable assets are contributed to the charter capital of a newly established company and certain thresholds are met.

Accreditation and Registration of a Representative Office or Branch

The procedure for opening accredited representative offices and branches in Russia is more burdensome than for incorporating a limited liability company. In Moscow and Saint Petersburg, it is divided into two main stages (which normally take up to 2-3 months to complete), whilst in other Russian regions a preliminary approval of the location of the representative office or branch must be obtained from the local authorities (which can sometimes result in long delays). For a branch, the accreditation is given by the State Registration Chamber of the Russian Ministry of Justice (SRC), and in case of a representative office, it will generally be either the Chamber of Commerce and Industry of the Russian Federation, or the SRC.

As a result of accreditation, the representative office or branch is included in the State Register of Accredited Representative Offices/ Branches of Foreign Entities.

Accreditation enables a representative office or branch to operate at federal level, irrespective of where the representative office is physically located.

In addition, representative offices or branches must be locally registered with the State Committee on Statistics, the tax authorities and the social funds.

All documents submitted to the accrediting body and registration authorities must be prepared in Russian (or translated into Russian) and legalised (where applicable).

Reorganisation of a Legal Entity

The Civil Code envisages mergers, consolidations, de-mergers, spin-offs and transformations. A reorganisation is quite a complex process and may take between 3-12 months to complete.

Liquidation of a Legal Entity

A legal entity can be liquidated: (i) voluntarily, by the decision of its shareholders/participants; and (ii) by the court in the circumstances listed in the Civil Code.

Shareholders' and Participants' Agreements

Russian corporate law has recently changed to allow participants of a limited liability company and shareholders in a joint stock company to enter into agreements regulating their respective rights in the company. Until now it has been assumed that such agreements were not permitted in relation to a Russian company and for this reason Russian joint ventures have in almost all cases been structured off-shore so that the Russian entity is a wholly owned subsidiary of a joint venture company established in a common law jurisdiction with a beneficent tax regime. The legislation is still extremely new and in parts unclear. The wording of the amendments to the JSC law is very similar but slightly different from

the wording of the amendments to the LLC law and at this time it is difficult to opine confidently whether the differences are significant – on the face of it it appears the scope of issues that may be regulated for a JSC is more limited when compared with the scope for a LLC. The new law has also left unanswered a number of related legal questions as for example the question of whether an agreement in relation to the capital of a Russian entity may be governed by non-Russian law and whether such agreements need to be notarised. Accordingly, we do not anticipate a change to direct on-shore structuring of Russian joint ventures until the answers to these questions become clearer. See the CMS Legal Alert of July 2009 – "New Russian Attitude to Shareholders Agreements – How useful is the New Law?" for further discussion of the issues.

Strategic Industries

The Foreign Investment Law and other regulations, have been amended by the law "On the Procedure for Foreign Investments in Commercial Organisations of Strategic Importance for the National Security of the Russian Federation" (the "Strategic Industries Law"), which came into force on 7 May 2008.

The Strategic Industries Law does not regulate foreign investments insofar as they are already governed by other federal laws or by international conventions ratified by Russia (such the rules governing military co-operation between Russia and foreign States).

The Strategic Industries Law provides for a list of 42 sectors of the economy that are deemed to be *strategic*, including:

- meteorological and geophysical technologies;
- military technologies, 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 Russia;
- communication services, including fixed-line telecommunications but excluding internet access services;
- television and radio broadcasting; and
- subsoil use.

Restrictions on Private Investors

The Strategic Industries Law provides that transactions which cause privately operated foreign investors (or their group of entities) to gain control over a strategic company are subject to the requirement of *prior* approval from the authorised governmental body in charge of controlling foreign investments in the Russian Federation (the "authorised body"). If the approval is obtained, the transaction must be conducted during the timeframe set out in the approval.

Foreign investors (or their group) are deemed to "gain control" over a company by disposing shares in the following situations:

- the acquisition, directly or indirectly, of more than 50% of the voting shares in a Russian company operating in a sector deemed to be of strategic importance (a "strategic company") that does not conduct geological surveys on the subsoil and/or explore and extract minerals on federal subsoil plots (called "operating on federal subsoil plots");
- the acquisition, directly or indirectly, of less than 50% of the voting shares in a strategic company that does not operate federal subsoil plots, if the acquirer gains effective control over the company;
- the acquisition, directly or indirectly, of 10% and more of the voting shares of a strategic company operating on federal subsoil plots; and

- the acquisition of control of a strategic company, which is the result of a change in the number of voting shares in that Company.

It should be noted that if the foreign investors (or their group) already own, directly or indirectly, over 50% of the strategic company's voting shares, then the transactions referred to in the preceding paragraph do not require prior approval from the authorised body. This exception does not apply to transactions involving a strategic company that operates on federal subsoil plots.

It should also be noted that a limited number of transactions only require post transaction notification, which must be made within 3 months of the change of control taking effect.

Restrictions on States and International Organisations

The Strategic Industries Law also bans foreign States, international organisations and organisations controlled by them, from acquiring control over Russian companies in sectors deemed to be of strategic importance.

In addition, it provides that foreign States, international organisations and organisations controlled by them must first obtain prior approval from the authorised body when:

- acquiring, directly or indirectly, more than 5% of the voting shares of a strategic company and operating on federal subsoil plots; and
- acquiring, directly or indirectly, more than 25% of the voting shares of a strategic company that does not operate on federal subsoil plots, or otherwise gaining the right to block decisions of that company's management bodies.

Notification

Foreign investors acquiring 5% or more of shares in a strategic company must inform the authorised body.

In addition, foreign investors (or their group) must supply the authorised body with information relating to stakes in strategic companies of 5% or more, which they acquired before the Strategic Industries Law entered into force.

Tax System

General Approach

The Russian tax system is relatively new. Some progressive tax concepts are being introduced into the legislation. The Tax Code of the Russian Federation of 31 July 1998 (as amended) contains a description of the general tax principles, the applicable taxes, the rights and obligations of the taxpayers and the state tax authorities.

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

1. Federal taxes applied throughout Russia Federation at uniform rates, such as VAT. Many taxes have a federal and regional component, and some taxes (such as corporation tax) may have their regional component reduced at the discretion of the relevant regional authority.
2. Regional taxes and local taxes are determined by the Tax Code and the local or regional government authorities. They are collected locally or regionally. Lower-tier authorities cannot grant concessions with respect to taxes governed by a higher authority.

Federal taxes	· Corporate profits tax · Value-added tax (VAT) · Excise taxes · Personal income tax · Unified Social Tax (UST) · Mineral resources extraction tax · Water tax · Payments for the use of natural resources · State duties

Regional taxes	· Company property tax · Transport tax · Tax on gambling
Local taxes	· Land tax · Individual property tax

The tax structure can result in different tax burdens in different locations. It also means that there may be a requirement for both federal and state tax filings, and for several tax payments to be made when an entity has branches in more than one Russian region.

Taxation of Corporations

Corporate Profits Tax

Taxpayers

Taxpayers are defined as:

- Russian legal entities that pay tax on their worldwide income; and
- Foreign legal entities that conduct business in Russia through a permanent establishment and/or are in receipt of income from a Russian source.

Profit tax is always levied at the level of the individual entity. There are no provisions for group relief or fiscal unity, although a draft law is currently under discussion.

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 entity does not have a permanent establishment, it is not subject to Russian profit tax. Any Russian-sourced income (interests, dividends, royalties, etc) will subsequently be subject to withholding tax.

Please note that if a foreign company conducts activities listed in the Code through an agent, it may also be considered as having a permanent establishment in Russia; The agent represents the company and acts on its behalf.

As a general rule, a foreign legal entity 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 if the possibility of such an allocation is provided for in the that treaty. If there is no double taxation treaty then the costs of a foreign legal entity may be allocated to its Russian permanent establishment, provided that they were incurred by that permanent establishment.

Tax Base

This is the total income received by the taxpayer less any income exempted from taxation and any expenses, as defined by the Tax Code.

The types of income which are exempt from profits tax are as follows:

- Income in the form of property received from a parent company, a subsidiary or an individual, if the legal person transferring the property owns at least 50% of it, and the property received (except money) is not disposed within one year from the date of receipt;
- 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 profit tax purposes if they are related to the taxpayer's income, and if they are economically justified and evidenced by the requisite documentation. The criteria are generally applied very strictly by the tax authorities.

The law specifies certain **non-deductible expenses**:

- The cost of asset's transferred free-of-charge;
- Penalty payments made into the Budget; and
- Employee remuneration which is not provided for in that employee's labour contract.

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

- Representations: up to 4% of payroll
- Pension and life insurance for employees: up to 12% of payroll;
- Medical insurance for employees: Up to 3% of payroll;
- Interest on loans and other borrowings charged at a rate which 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 is[1]:
  - For rouble loans, the refinancing rate of the Russian Central Bank at the date the loan is advanced (currently 11,5%), multiplied by 1,5;
  - For foreign currency loans, 22%.

Interest is subject to the thin capitalisation rules.

Depreciation and Amortization

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

Two depreciation methods are available for profit tax purposes:

- The straight-line method; and
- The reducing balance method

Depreciable property includes tangible and intangible assets with an initial value exceeding RUR 20,000 (c. US $ 632) and a useful life of at least one year.

The useful life of depreciable fixed assets is determined, within certain limits, based on a classification adopted by the government, as follows: For intangible assets the useful life is the utilisation period defined by any agreement, in all other cases it is ten years. The tax basis for a fixed asset includes all costs incurred in order to put it in a position where it can be used productively by the buyer. Accelerated depreciation is permitted for leased property.

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

Losses

Losses can be carried forward and be offset against future taxable profits for 10 years. Carry back is not allowed. Losses from the sale of fixed assets are recognised evenly over the remaining useful life of the assets.

Transfer Pricing Mechanisms

The Russian tax authorities are entitled to challenge the price of certain transactions, and to impose additional tax liabilities when the sales price deviates from the market level by more than 20%. This rule concerns the following transactions:

- Transactions between related parties;
- barter transactions;
- foreign trade transactions; and
- transactions in which the price fluctuated by more than 20%, within a short period of time.

The government is working on an amendment to the transfer pricing rules. One of the most important points in the draft law is the

[1] Please note that this rule is in force until 31 December 2009 and applies to relations arising from 1 September 2008. As a general rule, a maximum rate of the refinancing rate of the Central Bank multiplied by 1,1 for rouble loans and a maximum rate of 15% for foreign currency loans applies.

requirement to have documentation in place to support the level of prices according to the OECD transfer pricing guidelines.

Tax Rate

The general profit tax rate is 20% (as from 1 January 2009); 2% of the tax is payable to the Federal government and the remaining 18% to regional governments.

Taxation of Dividends

(i) Dividends received by Russian legal entities
Dividends received by a Russian company from another Russian company, or from a foreign legal entity, 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 dividends owns at least 50% of the payer of dividends' capital, or owns depository receipts entitling it to receive at least 50% of the amount of paid dividends; and / or
- the share or depository receipts have been owned for at least 365 days on the day dividends are declared; and / or
- the value of the investment is at least RUR 500,000,000 (c USD 16.1 million).

Dividends from companies residing in low-tax jurisdictions (a list of these jurisdictions has been published by the Ministry of Finance) cannot be exempted from Russian VAT.

(ii) Dividends paid by Russian legal entities
The standard 15% tax rate is applicable to dividends paid by Russian legal entities to foreign legal entities. The tax should be withheld by the Russian legal entity 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%.

Value Added Tax (VAT)

Taxpayers

VAT applies to companies, individual entrepreneurs and to any person importing items into the customs territory of the Russian Federation.

If the taxpayer's aggregated income for 3 consecutive months, excluding VAT, is below RUR 2,000,000 (approx. USD 64,516), the taxpayer may be exempt. An exemption must be applied for.

Tax Base

VAT taxable operations include the folowing (even if they are supplied free of charge):

- The realisation of goods, works and services in Russia;
- The transfer of goods, works and services in Russia for the taxpayer's own purposes, if the relevant expenses are not deducted for the purposes of corporate profit tax;
- Construction and building projects for the taxpayer's own use; and
- Imports into the customs territory of Russia.

The **taxable base** is generally defined as the market value of the goods, works and services supplied, inclusive of excise duty and VAT. If the Russian tax authorities consider that the price deviates from the market value for identical goods, works or services by more than 20%, they may charge additional VAT.

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

Exempt Supplies

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

- The assignment of loan agreements;

- Operations involving securities and derivative financial instruments;
- Certain banking transactions;
- Transactions with medical equipment and medical services;
- Certain research and development services;
- The 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 (a list is approved by the government); 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;
- Certain services and goods supplied to foreign diplomatic missions.

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.

Whether input VAT is recoverable no longer depends on whether it has been paid to the supplier. VAT on imports can be recovered only after payment to the customs authorities.

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

Any VAT incurred on purchases and expenses which relate to activities which are both subject to VAT, 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. Such a refund will only be made after the tax authorities have undertaken an inspection.

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 Russian Tax Code.

Reverse Charge

If a foreign entity 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 that tax 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 Russian tax registration are considered to be tax agents in relation to goods supplied on behalf of non-registered foreign entities (see below for more information on tax agents).

Filing and Payment

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

- The date of *shipment* or *transfer* of the goods, works or services;
- The date of *payment* (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.

Starting from Q3 2008 taxpayers have the option to pay VAT in three instalments, in the three months following the relevant quarter.

Excise Tax

Excise tax must be paid by legal entities or individual entrepreneurs that are producers and/or importers of excisable products. Excisable products are, for example, oil products, alcohol, tobacco and cars.

Excise tax is generally levied on the value of the product.

Corporate Property Tax

Property tax is payable in accordance with regulations of each state and with the Tax Code.

Taxpayers

The following entities are subject to property tax:

- Russian legal entities; and
- Foreign legal entities having a permanent establishment in Russia and/or owning immovable assets in Russia.

These entities are required to pay property tax to the regional government of the state they are located in.

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

Tax Base

Property tax is assessed on both movable and immovable property. Taxable property includes fixed assets and "profitable investments in property" (as defined by Russian accounting standards). It also comprises property which is leased. Foreign legal entities that do not have a permanent establishment in Russia are only taxed on immovable property.

Intangible assets, inventories, work-in-progress, financial assets (among other categories) are not subject to property tax.

The tax base is the average annual residual value of taxable property for financial reporting purposes (rather than for tax purposes).

Tax Rate

The rate is set at the regional level but cannot exceed 2.2%. This maximum rate is currently imposed in most regions, including Moscow and St. Petersburg.

Payments

The tax period is a calendar year. Advance tax payments must be calculated and paid on a quarterly base. Taxpayers must file quarterly tax returns within the 30-day period following the reporting period. Annual returns must be filed no later than 30 March following the reporting period.

Unified Social Tax (UST) and other Payroll Related Taxes

Taxpayers

UST, pension insurance contributions, and contributions for insurance against injury and professional illness must be paid by employers. This applies to Russian employers as well as to foreign companies.

UST

UST is assessed on the remuneration (in cash or in kind) of each employee.

It is paid to the Federal Budget, the Social Fund and the Medical Fund. Payments are made on a regressive scale and depend on an employee's annual income, as follows:

Income per year	Rate
Below RUR 280,000 (approx. USD 8,846)	26%
RUR 280,001 – RUR 600,000 (approx. USD 18,957).	RUR 72,800 (approx. USD 2,300) + 10% of sum exceeding RUR 280,000
Above RUR 600,000	RUR 104,800 (approx. USD 3,311) + 2% of sum exceeding RUR 600,000.

Special reduced UST rates are applied to companies operating in the Information Technology Sector.

The tax period is the calendar year. UST is payable on a monthly basis, no later than the 15th day of the following month.

Other Payroll Contributions

Pension insurance contributions are assessed according to the gross payroll of each employee. Payments are also made on a regressive scale.

Pension insurance contributions are deductible from UST.

Contributions to the Social Insurance Fund are additionally payable. They vary from 0.2% to 8.5%, depending on the risk category of the employee.

Taxes on Land, Water and Natural Resources

Land tax is a local tax imposed on taxpayers that use land either on the basis of ownership rights, or rights of permanent use.

Water tax is imposed on taxpayers who use water to produce hydroelectricity.

A tax is imposed on sub-soil users, based on the value of the extracted resources.

Transportation Tax

This is a tax payable on registered transportation vehicles by the registered owners of those vehicles. The methods of declaration, payment and deposit are variable

State Duties

According to the Tax Code, a state duty is a fee charged on organisations and individuals for taking certain legal actions. Examples of such legal actions alongside the corresponding state duties are shown in the table below:

Legal actions	State duties
Accreditation of a representative office or branch	RUR 60,000 (approx. USD 1,935)
Registration of a Russian legal entity	RUR 2,000 (approx. USD 65)
Licensing	From RUR 10,000 (approx. USD 323) to RUR 100,000 (approx. USD 3,226)
Accreditation of a subsidiary of a foreign entity	RUR 60,000 (approx. USD 1,935)
Registration of rights to real estate	RUR 7,500 (approx. USD 242)
Registration of rights to transportation facilities	From RUR 100 (approx. USD 3) to RUR 400 (approx. USD 13)

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. Since 1 January 2007, an individual is considered to be a tax resident if he is physically present in Russia for at least 183 calendar days during a 12-month period. According to the clarifications of the Ministry of Finance, how-

ever, 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 that they may dispose of at their discretion.

Deductions and Non-taxable Income

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

- Standard tax deductions:
  The taxpayer receives a standard monthly deduction of RUR 400 (approx. USD 13) until his total annual earnings amount to RUR 40,000 (approx. USD 1,290).
  Other standard deductions are also available for certain categories of taxpayers.
- Social tax deductions:
  Social deductions comprise educational expenditures (per taxpayer and for each of his children) and medical expenditures (per family), up to a combined annual maximum of RUR 50,000 (approx. USD 1,613).
- Property deductions:
  Property deductions relate to the purchase and sale of property (mainly residential real estate).
- Professional deductions:
  These 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;
- A rate of 35% applies to certain prizes, insurance receipts and interests from bank deposits in excess of specific limits.

Non-residents

A 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.

Tax Payments

Tax Withholding

Russian entities, individual entrepreneurs and permanent establishments of foreign entities 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 income tax obligations.

Tax Return

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

- The income was received from outside Russia (in the case of a Russian tax resident); or
- The income was paid by an individual; or

- The tax was not properly withheld; or
- The income was received from the sale of property.

The tax return must be filed no later than 30 April in the year following the tax period.

The amount of tax due must be paid no later than the 15 July following the relevant tax period. However, if the taxpayer leaves Russia, he must file a tax return at least one month before his departure and pay the amount of tax due, within 15 days, after the date the tax return is filed.

Individual Property Tax

Taxpayers

According to the law "On the individual property tax" of 9 December 1991 (as amended), the owners of houses, apartments, cottages, garages and other buildings or constructions are liable to pay individual property tax.

Tax Rates

The tax rate varies depending on the total inventory cost of the property. As individual property tax is a local tax, the local government authorities are entitled to set the tax rate within the following limits:

Property cost	Tax rate
Below RUR 300,000 (approx. USD 9,478)	Below 0,1%
RUR 300,000 to RUR 500,000 (approx. USD 15,798)	0,1% – 0,3%
Above RUR 500,000	0,3% – 2%

Special Tax Regimes

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

- A simplified tax system;
- A unified agricultural tax;
- A tax on imputed income; and
- Production sharing.

Special regimes may be applicable if the necessary requirements are met.

Simplified Tax System

Taxpayers

A legal entity is eligible for the simplified tax system if they meet the following criteria:

- Their turnover does not exceed RUR 15,000,000[2] (approx. USD 473,934); and
- the combined net book value of their fixed and intangible assets does not exceed RUR 100,000,000 (approx. USD 3.159 million); and
- there are fewer than 100 employees.
- The Tax Code includes a list of organisations that cannot use the simplified tax regime. This includes foreign companies, Russian companies with local branches and/or representative offices, companies where more than 25% of capital is owned by other organisations, banks, insurance companies, pension funds, and 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;
- 15% if income less deductible expenses is considered as the tax base.

The simplified tax system is used as a single substitute for profits tax, property tax, a portion of UST and VAT (subject to several exceptions). The use of this system does not exempt employers and individual entrepreneurs from making obligatory pension insurance contri-

[2] A draft law increasing the demanded turnover to RUR 45,000,000 (approx. USD 1.5 mln.) is currently under discussion.

butions, or withholding income tax from their employees' compensation.

Tax on Imputed Income

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

The tax rate is 15% on "imputed" revenue each month. It 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 taxes and contributions (except, for example, obligatory pension insurance contributions).

Unified Agricultural Tax

A taxpayer producing, processing and selling agricultural products is 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.

The unified agricultural tax is used as a substitute for profit tax, VAT (except import VAT), property tax and a portion of UST (payable to medical and social funds). The tax rate is imposed at 6% of revenue less certain deductible expenses that are listed in the Tax Code.

Customs Duties

Export Duties

Export duties are assessed on the export of some raw materials, such as oil and oil products, timber and metals).

Import Duties

There are numerous applicable rates, which are generally higher than those in most Western countries. The customs rates usually vary from 0% to 25%, depending on the nature of the goods imported. The rates also vary depending on the country of origin. Countries are classified into 5 groups:

- Most favoured nations: the basic customs rate applies.
- Developing countries: 75% of the basic rate applies.
- Less developed countries: Exempt from import duties.
- CIS nations: Exempt from import duties.
- Non-favoured nations: Twice the basic rate applies.

Fixed assets which are imported as contributions in-kind by a foreign participant or shareholder into the charter capital of a Russian company may be exempt from import duties. This is the case if the contribution is in the form of technological equipment.

There are now new special customs regimes and procedures. Customs clearance has become much simpler and faster, although the process can still be problematic.

Incentives – Special Economic Zones

Taxpayers can benefit from incentives granted to special economic zones (SEZ) which have been created in Russia by the Federal Law "On The Special Economic Zones" of 22 July 2005 (as amended) in order to promote economic growth in specific areas and regions of Russia

The general aim of SEZ is to attract foreign investment: as SEZ are exempted from custom duties, they are an effective means of promoting import/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

Four types of SEZ are established by the legislation:

- Technical research and implementation zones (St. Petersburg, Dubna, Tomsk, Zelenograd);
- Industrial production zones (Lipetsk, Tatarstan);
- Recreation and tourism zones (Altai, Buryatia, 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.

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 UN Model Convention.

The provisions of such treaties override Russian domestic law. However, in practice, the tax authorities often deny the benefit conferred by a treaty, even if all the relevant conditions are fulfilled.

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	5/15 (1)	0	0
Belgium	10	0/10	0
Canada	10/15 (2)	10	0/10
China	10	10	10
Cyprus	5/10 (3)	0	0
Denmark	10	0	0
Finland	5/12 (4)	0	0
France	5/10/15 (5)	0	0
Germany	5/15 (6)	0	0
Ireland	10	0	0
Italy	5/10 (7)	10	0
Japan	15/10	10	0/10 (8)
Korea (South)	5/10 (9)	0	5
Luxembourg	10/15 (10)	0	0
Netherlands	5/15 (11)	0	0
Norway	10	0/10 (12)	0
Poland	10	10	10
Portugal	10/15 (13)	10	10
Spain	5/10/15 (14)	0/5 (15)	5
Sweden	5/15 (16)	0	0
Switzerland	5/15 (17)	5/10 (18)	0
Ukraine	5/15 (19)	10	10
UK	10	0	0
USA	5/10 (20)	0	0

Notes:

(1) 5% for 10% shareholders, otherwise 15%;
(2) 10% for 10% shareholders, otherwise 15%;
(3) 5% if the initial investment is greater than US 100,000, otherwise 10%;
(4) 5% for 30% shareholders, otherwise 12%;
(5) 5% if the investment is not less than FFr 500,000 and if the recipient pays tax; 10% if either is untrue; otherwise 15%;
(6) 5% for 10% shareholders, otherwise 15%;
(7) 5% for10% shareholders, otherwise 10%;
(8) 0% for royalties in respect of literary, artistic or scientific works including films and tapes; 10% for royalties in respect of any patent, trade mark, design or model, plan, secret formula or process, or industrial, commercial or scientific equipment, or information concerning industrial, commercial or scientific experience;
(9) 5% for 30% shareholders, otherwise 10%;
(10) 10% for 30% shareholders, otherwise 15%;
(11) 5% for 25% shareholders, otherwise 15%;

(12) 0% for commercial loans in connection with a delay of payment for goods, equipment and services; otherwise 10%;
(13) 10% for 25% shareholders, otherwise 15%;
(14) 5% for participation of at least ECU 100,000 and if the dividends are exempt from tax; 10% if either condition is met; otherwise 15%;
(15) 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%;
(16) 5% for 100% participation or 30% participation in a joint venture; otherwise 15%;
(17) 5% for 20% shareholders, otherwise 15%;
(18) 5% for bank loans, otherwise 10%;
(19) 5% for participation of at least US 50,000; otherwise 15%;
(20) 5% for 10% shareholders, otherwise 10%.

Anti-monopoly Issues

Anti-monopoly issues are governed by a number of acts, including the law "On Protection of Competition" dated 26 July 2006 (the "Competition Law"), the Code on Administrative Offences and the Criminal Code. The Federal Anti-monopoly Service (FAS) is the national executive authority that has a control and enforcement role to ensure compliance with anti-monopoly legislation, and that oversees the adoption of regulatory acts.

Anti-competitive Practices

The Competition Law covers the following types of anti-competitive practices:

- Abuse of dominance
- Cartel agreements and concerted actions
- Unfair competition

Dominance is not strictly concerned with market share and may be found in certain circumstances even if the share is less than 35%.

The hard-core cartel agreements and concerted actions involve the following violations:

1. fixing or maintenance of prices (tariffs), discounts, additions (additional payments) or extra charges;
2. rise in, reduction or maintenance of prices when holding auctions;
3. market sharing on the basis of the territorial principle, volume of a commodity's sales or purchases, assortment of commodities being sold or composition of sellers or purchasers (customers);
4. refusal to make contracts with certain sellers or buyers;

5. imposing unfavourable terms upon a contractor;
6. reduction or termination of a commodity's production;
7. impeding access to a commodity market or withdrawal of other economic units from a commodity market; and
8. establishing conditions of membership (participation) in professional or other associations, if such conditions lead or may lead to restriction of competition.

Unfair competition is prohibited, and this includes (but is not limited to):

1. dissemination of false, incorrect or distorted data which may cause losses to an economic unit or breach its business reputation;
2. misleading in respect of the nature, mode and place of production, consumer properties, quality and quantity of a commodity or in respect of its producers;
3. incorrect comparison of the commodities produced by an economic unit, with commodities produced or sold by other economic units;
4. the sale, exchange or other placing into circulation of a commodity, if in so doing, this resulted in the unlawful use of intellectual property in some way; and
5. unlawful receipt, use and divulging of information constituting commercial, official or other secrets protected by law.

Mergers

The Competition Law contains a system for mandatory notification to (and prior approval of) the FAS of mergers where certain thresholds are met.

The following actions require merger clearance from the FAS, provided that the respective thresholds established by the Competition Law are met:

1. Formation of a Russian legal entity, provided that its charter capital is paid up by shares and/or tangible or intangible assets of another business entity and results in:
   - acquisition (in ownership or the right to control) of more than 25 %, 50 % or 75 % of voting shares in a Russian joint-stock company; or
   - acquisition of more than 1/3, 50 % or 2/3 of participation interest in the charter capital of a limited liability company; or
   - acquisition of the rights to own, use or possess tangible and/or intangible assets of a Russian legal entity, in circumstances where the book value of the acquired assets exceeds 20 % of the total book value of tangible and intangible assets owned by this Russian legal entity.
2. Reorganisation (in the form of merger or annexation).
3. Acquisition of more than 25 %, 50 % or 75 % of voting shares in a Russian joint-stock company.
4. Acquisition of more than 1/3, 50 % or 2/3 of participation interest in the charter capital of a Russian limited liability company.
5. Acquisition of indirect control over a Russian legal entity.
6. Acquisition of the rights to own, use or possess tangible and/or intangible assets of a Russian legal entity, in circumstances where the book value of the acquired assets exceeds 20 % of the total book value of tangible and intangible assets owned by this Russian legal entity. Please note that this calculation of assets should be applied only for legal entities operating on commodity markets. For those that operate on financial markets, the threshold is 10% of the total book value of tangible and/or intangible assets owned by the Russian

financial organization, including credit institutions.

The transactions mentioned above require merger clearance (prior and/or post transaction) with the FAS, provided that the respective thresholds established by the Competition Law are met. These are mostly asset-based thresholds. However, when the asset-based thresholds are not met, the income-based thresholds should be applied.

Prior Merger Clearance Test:

i. the book value of the acquirer's assets, the assets of the commercial entities belonging to the acquirer's group worldwide and the assets of the target and of commercial entities belonging to its group worldwide, exceeds more than RUR 7 billion, and the aggregate value of the assets of the target and of the commercial entities belonging to the target's group exceeds RUR 250 million; **or**

ii. the aggregate income of the entities listed above from the sale of commodities during the last calendar year exceeds RUR 10 billion, and the aggregate value of the assets of the target and of the commercial entities belonging to the target's group exceeds RUR 250 million; **or**

iii. enrolment of the acquirer (its group) and/or the target (or its group) in the register of commercial entities with a market share in excess of 35% maintained by FAS. Please note that this threshold should be applied separately from the above-mentioned thresholds and it is applicable only for Russian legal entities.

Post-Transaction Merger Clearance Test:

Where the thresholds for prior approval are not met, the Competition Law requires post facto notification to the FAS within 45 calendar days after the deal has been closed where:

i. the book value of the acquirer's assets, assets of commercial entities belonging to the acquirer's group worldwide and assets of the target and of the commercial entities belonging to its group worldwide exceeds more than RUR 400 million; **or** the aggregate income of the acquirer and its group worldwide plus the target and its group worldwide from the sale of commodities during the last calendar year worldwide exceeds more than RUR 400 million. This threshold should be applied when the above-mentioned threshold (i) is not met;

and

ii. the book value of assets of the target and of commercial entities belonging to its group worldwide exceeds RUR 60 million.

Please note that all thresholds listed above should be applied only for legal entities operating on commodity markets. For those that operate on financial markets, the requirements are different.

Sanctions

For non-compliance, legal and physical persons are subject to administrative and criminal liability. The Competition Law provides for a prescription and collection of revenue received under the violation as possible penalties; the Code on Administrative Violations allows imposition of turnover (up to 15%) fines and disqualification, and the Criminal Code stipulates for fines, disqualification and up to 7 years of incarceration for the most serious anti-monopoly violations.

Leniency

The Code on Administrative Violations provides a limited opportunity for companies that have participated in illegal cartels to avoid penalties. In order to obtain total immunity under

the leniency program, a company, which participated in a cartel, must be the first one to inform the FAS of it, provided that the FAS is not aware of such infringement. The company must submit information and/or documents sufficient to allow the FAS to launch an investigation, prove the cartel, fully cooperate with the FAS throughout its procedure, and put an end to the infringement immediately. Collective applications are not accepted.

Currency Control

Foreign Currency Transactions

The Foreign Exchange Control Law of 10 December 2003 ("the Currency Law") regulates currency transactions. Many currency transactions can be conducted without any limitations, although the law does define several restrictions.

Foreign Currency Transactions Between Residents

The following persons are considered to be 'residents':

- Citizens of the Russian Federation, except those who are (considered to be) living abroad on a permanent basis;
- Foreigners and individuals without Russian citizenship who live permanently in Russia on the basis of a residency permit;
- Legal entities duly registered under Russian law;
- Diplomatic representatives, consular offices and other official representatives of the Russian Federation; and
- The government of 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, 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.

Furthermore, residents must repatriate all roubles and foreign currency received from international trade and commercial activities into their Russian bank accounts. There is an exception for payments due to a non-resident lender. Such payments may be directly transferred into the lender's foreign bank account.

Foreign Currency Transactions Between Non-residents

Non-residents are:

- Individuals who are not defined as residents;
- Legal entities and all other organisations that are registered under the legislation of a foreign country, and that are located outside the Russian Federation;
- Representative offices and branches of legal entities or other organisations located in the Russian Federation and registered under the legislation of a foreign country; 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 foreign currency are permitted without restriction between non-residents. The purchase and sale of securities between non-residents are also permitted, although they can be subject to Russian securities 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 are obligatory for all currency transactions involving the import or export of goods, loans, the provision of services and intellectual property between residents and non-residents.

Import and Export of Foreign Currency

Residents and non-residents can import foreign currency into Russia without limitation. When the value exceeds USD 10,000, they have to make a written customs declaration.

Residents and non-residents can export up to USD 3,000 of foreign currency without submitting a customs declaration, and up to USD 10,000 with a declaration. Exports of over USD 10,000 are authorised up to the correlating amount stated on the customs declaration form which was used for the import of that currency.

Breach of the currency rules can result in severe sanctions.

Employment

General Approach

The Labour Code of the Russian Federation of 30 December 2001, as amended, (the "Code") is currently the main law applicable to employment arrangements.

Please note that according to Russian law employment relationships are distinguished from civil law service agreements. If a civil law service agreement includes aspects that could be construed as an employment relationship, the mandatory provisions of employment law are applicable.

Employment Contracts

According to the Labour Code, employment contracts must contain mandatory conditions such as the place of work, position, duties, a commencement date, the duration of employment (if applicable), remuneration, and a working schedule. Employment contracts may contain optional conditions, such as probation periods and confidentiality. The parties' rights and obligations under the employment contract must comply with minimum legal requirements. An individual employment contract must not result in employee's terms of employment being worse that the terms of employment stipulated under the overriding requirements of employment law, otherwise the legislation will supersede the provisions of the individual's contract.

Duration

Employment contracts may be concluded for an indefinite term, or for a finite term not exceeding 5 years.

The law provides for a limited number of situations when finite term contracts may be used, which include the following situations:

- A worker replacing a temporarily absent employee;
- Temporary, project-related, or seasonal workers;
- directors, deputy directors, or chief accountants;
- employees of companies created for a specific term and purpose; and
- training programs.

An employment contract concluded for a finite term in breach of the Code's provisions may be declared to be operative for an indefinite term by a court.

Salary

An employee's monthly remuneration shall be a minimum of RUR 4330 (app. USD 137), as established by law. It should be paid twice a month, in roubles.

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

Criminal sanctions may be imposed on the employer's executive if salaries are not paid for over 2 months. Sactions may include a fine of up to RUR 120 000 (app. USD 3791), a ban from holding a management position for a period up to five years, or imprisonment for a period of up to two years.

Probation

An employment contract may provide for a probation period, which shall not exceed 3 months. For directors, deputy directors, chief accountants, deputy chief accountants, directors of representative offices, branches or other divisions, a longer probation period may be established. This longer period may not exceed 6 months. A probation period cannot be provided for certain pregnant women, minors, graduates, and some other categories of employees.

Termination of the Contract

An employment contract can be terminated:

- at any time by the mutual agreement of the parties;
- by the employee alone with 2 weeks' prior written notice, or at the initiative of the employer (as discussed below);
- due to circumstances beyond the reasonable control of the parties;
- because of expiration of the employment contract's term;
- when an employee refuses to continue working due to a change in the owner of the employer, or the subordination of the employer, or its reorganisation;
- when an employee refuses to continue working because of the relocation of the employer.

The employer may terminate the employment contract based on a limited number of grounds specifically listed in the Code, as follows:

- When there is a staff redundancy or the employer is liquidated. The employer has to notify each employee in writing, which must be signed, at least 2 months in advance. In the case of staff redundancy, the employer must offer employees all available vacancies that correspond with their qualifications;
- When an employee is unsuitable for an employment position. Unsuitability must be confirmed by an internal committee review. This ground should be approached with caution because employees have a

high chance to successfully challenge it before a court;

- A systematic unjustified non-fulfilment of, or single gross violation of, employment duties; and
- Presentation of false documents by an employee when being hired.

The Labour Code requires dismissal pay to be made in certain circumstances.

An employer cannot terminate a pregnant women's employment contract, unless that employer goes into insolvent liquidation. There are also very few situations when it is possible to terminate the employment contract of a women with children under 3 years old, or a single women with children under 14 years old or disabled children under 16 years old.

Working Hours, Vacation, Sick Leave

A normal working week is 40 hours. Overtime is permitted upon the employer's written request; it cannot exceed four hours on two consecutive days, and is limited to 120 hours in total per year. The employer may establish irregular working hours for certain categories of employees, and fix these in its internal policies and relevant employment contracts.

Minimum annual paid vacation is 28 calendar days. In the event of irregular working hours the employee is entitled to 3 additional vacation days.

An employee is entitled to a temporary disability allowance of up to RUR 18720 per month (app. USD 585). The employer reimburses this amount by accordingly reducing its social tax.

Women are entitled to 70 days maternity leave prior to childbirth, and 70 days' leave after childbirth.

Labour Book

Russian employment law requires employers to keep, sign and stamp a Labour Book (*"trudovaya knizhka"*) for any employee working for more than five days with the same employer. The Labour Book includes, amonst other things, records of the employee's employment positions, their performance and any disciplinary action taken against them.

Social Partnership

The interests of the employer and employees are regulated by system of social partnership. This system has the following features:

- Negotiation of collective agreements;
- Consultation on labour issues;
- Employees' participation in the employer's management;
- Participation of parties in pre-court settlements of employment disputes.

Role of Trade-Unions

The Russian Federal law of 12 January 1996 defines a trade union as: a voluntary association of citizens, associated by mutual professional interests, created for the purpose of representing and protecting social labour rights and interests. It is not mandatory for trade unions to be registered.

When making decisions, the employer should consider the opinion of trade-union(s), as applicable. If an agreement cannot be reached, the employer is entitled to adopt decisions unilaterally, although such actions can be challenged in court.

Independent Contractors

An independent contractor may be engaged pursuant to the Civil Code's provisions on civil work contracts. Under a civil work contract, the contractor performs certain work at his own risk for a customer (i.e. his/her employer).

However, if there is a dispute the court may find that because of its nature the civil contract constitutes actual employment, and so uphold employment law as applicable to the civil contract.

Specifics of Hiring Foreign Nationals

Immigration law in Russia has been modified recently. Several laws entered into force in 2006 and 2007 which amend the rules concerning the stay, registration and work of foreigners in Russia. These new regulations were part of a broad reform officially intended to *simplify* and *regularise* the status of foreigners working in Russia.

As a result, Russian immigration law today is complex and at times ambiguous. The reforms have also strengthened the sanctions applicable for breach of the regulations.

Visas for Foreign Employees

Foreigners must apply for a visa. Citizens of the CIS countries (except Georgia) Armenia, Azerbaijan, Belarus, Kazakhstan, Kirghizstan, Moldova, Tadzhikistan and Ukraine are exempt from Russian visa requirements.

Types of Visas

There are five categories of visas: ordinary, official, transit, diplomatic and temporary residence. There are five further subcategories of ordinary visa: business, tourist, working, student and humanitarian. The most important of types of visa for businesses are considered below.

Business Visas

Business visas are aimed in principle at foreigners seeking to carry out short-term and temporary business activities in Russia. Examples of such activities include business trips, negotiations, market studies and preparing to establish a legal entity in Russia.

Foreigners who obtain Russian business visas are not allowed to undertake full-time work in Russia; this requires a working visa.

Working Visas

Working visas are apply to foreigners preparing to carry out a professional activity in Russia.

A foreigner must first obtain a single-entry visa. This will be valid for a maximum term of three months. It can be converted into a 1 year multiple-entry working visa once the individual is in Russia. Family members of a working visa holder can obtain visa of under the same category marked "accompanying person." This visa does not entitle the family member to work in Russia and it will expire on the same date as the principal's visa.

Working visas are issued only after the employer has received a general authorisation enabling them to recruit foreigners and a quota of foreign persons who they may recruit. Each foreign employee must also be granted a work permit (please see below).

The employer has to be registered with the Federal Migration Service in order to be able to issue invitations to foreign workers (again, please see below). The registration is valid for one year and can be renewed.

It takes from 8 to 12 weeks to obtain a working visa.

Visa Procedures Relevant to an Employer

An employer recruiting foreign employees in Russia has to comply with the following procedures:

Quotas

Companies who wish to employ foreigners must apply each year for a quota of foreign workers that they may employ. The quota allocated to each entity depends on the general quota set each year for all foreign workers. This quota differs between states, different categories of workers, different professions, countries of origin and other economic and social criteria).

General Authorisation for the Recruitment of Foreigners

Any employer intending to recruit one or several foreigners must obtain prior general authorisation to recruit foreign employees from the Federal Migration Service. For this purpose the employer must justify the use of a foreign workers.

Individual Work Permits

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

A work permit is required for any foreigner who wishes to perform a 'work activity' in Russia, including unpaid and temporary work.

Work permits are usually only valid for one region of Russia. However the holder of a work permit can work in another region as follows:

- on business trips for maximum of 10 calendar days during the work permit's term;
- by working 'on the road' for a maximum of 60 calendar days during the work permit's term.

Although it is difficult to control in practice, these maximum periods have to be taken into account by employers when they are arranging business trips for their employees.

The Ministry of Public Health and Social Development has drawn up a list of positions in which foreigners are allowed to work in the entire territory of Russia without restriction. This includes (among others): translators, car drivers, cargo carriers, economic consultants, photographers and artists.

In all other cases, work performed outside the authorised region is prohibited.

Sanctions

For a failure to comply, fully or in part, with the relevant procedures, the employer risks a fine of up to 800,000 roubles (app. USD 25,277) or the suspension of its activities for up to 90 days. The employer's executive may be liable to fines of up to RUB 50,000 (app. USD 1 579). A foreign employee can also be fined up to RUB 5,000 (app. USD 158), and may be deported.

There is a notification procedure which must be followed by foreigners (and their employers). The rules entered into force in January 2007 and are considered below.

Outline of the Regulations

- A notification must be made to the immigration authorities;
- The notification procedure applies not only to arrivals to and departures from Russia, but also to any travel within Russia;
- Foreigners staying in Russia, or travelling to another Russian federal territory for less than 3 days, and who are not staying in a hotel or in 'a hotel like residence' are exempt from the notification procedure;
- Heads of States, heads of diplomatic missions, members of parliamentary or governmental delegations, heads of international organisations (and family members of such persons) are exempt from the notification procedure. Ship, train or aircraft crew members are exempt from the procedure under certain conditions;
- For notification purposes, it is acceptable to use the employer's address as their usual place of stay on the notification form;
- The obligation to make a notification of a foreigner's arrival, departure and travel within Russia to the Federal Migration Service is incumbent upon the "receiving party;" this is the organisation or person who facilitates the foreigner's stay in Russia (i.e. the employer, the hotel or the owner of the foreigner's dwelling). The "receiving party" can be a natural person or a legal entity and is not necessarily the "inviting party".

The Operation of the Notification Procedure in Practice

Upon Arrival:

- A foreigner must fill in an immigration card and keep it with them until their departure;
- The receiving party must notify the immigration authorities of the foreigner's arrival at their place of stay within 3 working days, by filing a notification form;
- The Federal Migration Service will place a stamp on the tear-off voucher from the regisation form, and give this back to the foreigner, or the person making the registration on their behalf, on the same day;
- The tear-off voucher serves as proof that the foreigner's arrival has been duly notified. The foreigner must keep this voucher with them at all times;
- It is possible to file a notification by post (stamp duties of RUB 118 and posting fees apply). If this procedure is used, the notification form is filed in two counterparts. After reviewing the notification document, the post office will return the voucher to the registered person. The counterpart voucher is kept by the postal services for 1 year.
- The postal route is quite straight forward, but in practice it can be a haphazard process which may not result in proper registration. Further, different federal regions take different approaches to the postal route.
- If any changes are made to the to the data submitted in the notification, the receiving party must notify the Federal Migration Service of the changes within 3 working days.

Upon Departure:

- When a foreigner leaves their place of stay in Russia, either for a trip abroad or within Russia, the receiving party must return the tear-off voucher to the Federal Migration Service within two working days following the foreigner's departure. This procedure may also be performed by post (a mailing slip is delivered to the receiving party in this case);
- If the foreigner leaves Russia, they must, as before, return the immigration card to the border guard who is responsible for passport control;
- If a foreigner travels to another destination in Russia, the new "receiving party" must repeat the notification procedure at the new place of stay. A trip of less than 3 working days does not require notification.

The Special Procedure for Foreigners Staying in a Hotel:

- Foreigners staying in a hotel are subject to a different procedure. Upon their arrival at the hotel, they need to give their passport, visa and immigration card to the hotel desk staff. The hotel is responsible for filling out the notification form and filing it with the Federal Migration Service. The tear-off voucher is given to the foreigner on day of registration. Upon their departure, the foreigner must return the voucher to the hotel administration, which must notify the immigration authorities before noon the next day.
- The implementation of this procedure is not straight forward; immigration offices are not open every day of the week and generally operate for only 2 to 4 hours per day. Moreover, notification by post is only possible if a foreigner is staying several days as it can take some time. Finally, a strict application of the law would prevent a foreigner from departing on the same day he/she arrived. This is because they would not have had enough time to receive the voucher evidencing their re-

gistration, and so technically they would risk a formal warning if their documents were checked. In view of these issues, the authorities are currently considering implementing an electronic notification procedure.

- The position of a foreigner arriving at a hotel late in the night and leaving the next morning remains an uncertain. Again, if they fail to register, they risk being penalised.

Bankruptcy

General Approach

The most important legislation governing insolvency proceedings in Russia is as follows:

- The first part of the Russian Civil Code;
- The Federal Law on Insolvency (bankruptcy) of 26 October 2002 (as amended), which is the principal piece of legislation on insolvency in Russia (the "Insolvency law");
- The Regulation of the Government of Russia of 29 May 2004.

Under the Insolvency law a debtor is defined as insolvent where a commercial court ("arbitrazh court") has recognised the debtor's inability to meet creditors' claims, and/or to fulfil mandatory payment obligations within 3 months from the date they were due. A debtor can also be declared insolvent when their aggregate liabilities are more than the aggregate value of their property.

Insolvency Procedures

There are four stages of insolvency proceedings, which will apply as is relevant to the insolvent company's circumstances:

- supervision;
- financial rehabilitation;
- external management;
- insolvent liquidation; and
- a voluntary agreement.

Preliminary Step: Initiating Bankruptcy Proceedings

As a general rule, bankruptcy proceedings may be commenced against all types of legal en-

tity, other than certain forms of government-owned enterprises, political parties and religious organisations.

The following are permitted to file an application with an arbitrazh court to have a debtor declared insolvent:

i. the debtor itself;
ii. a bankruptcy creditor; and
iii. the Federal Tax Service with claims supported by a judgment at law for an amount over 100,000 RUR (app. USD 3155).

The Insolvency law compels a debtor to initiate bankruptcy proceedings if one of the tests for insolvency (as outlined above) is met.

Supervision

Supervision is a provisional procedure which operates via an interim administrator. Supervision aims to preserve the debtor's property, analyse its financial status, complete a register of creditors and hold the first creditors' meeting.

Supervision commences when the court rules that a bankruptcy petition is founded, introduces supervision, approves the appointment of an interim administrator (and amount and source of his remuneration). The court may also impose provisional measures alongside the bankruptcy petition. The court's rulings must be executed immediately, and they cannot be appealed against.

Restrictions

As of the date of the court's ruling the debtor's business is restricted as follows:

- creditors' claims are to be submitted only through the creditor's register;
- the debtor is prohibited from setting-off (by counter claim) allocations of profits and dividends. The debtor may not alienate or purchase shares, place securities (excluding shares), reorganise their company structure or found subsidiaries;
- credit-related transactions and any property transactions which exceed 5% of the debtor's balance sheet value, are only permissible with the prior written consent of the interim administrator.

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

The Interim Administrator

The interim administrator is nominated by a court from the members of a self-regulating organisation of arbitrazh insolvency practitioners. His duties involve (among other things) preserving the debtor's assets, analysing its financial state, revealing the identity of all creditors, calling the first creditors' meeting and notifying creditors about the introduction of supervision.

The interim administrator is entitled, among other things, to seek injunctions to preserve the debtor's assets, to obtain information from the debtor, to obtain documents relating to the debtor's activities, to claim before a court that transactions made by a debtor are invalid, to request a court to remove a director, and to challenge creditors' claims.

Termination of supervision

Supervision is terminated on the date a court makes a ruling to that effect, and another stage of insolvency proceedings are entered into: financial rehabilitation, external management, insolvent liquidation, or settlement (as applicable). The court will issue a ruling upon the decision of the first creditors' meeting within 7 months from the date of the bankruptcy petition. If the creditors are unable to

make a decision within the 7 month deadline, the court will make a ruling and introduce the next phase of insolvency proceedings at its own discretion.

Financial Rehabilitation

This procedure aims to restore the debtor's solvency and to schedule the repayment of 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 at least include: 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 authorising the decision.

Rehabilitation Administrator

A rehabilitation administrator is appointed by a court. The role of the rehabilitation administrator is predominantly a monitoring one. His key duties include: maintaining a register of creditor's claims, examining reports on the progress of the financial rehabilitation plan, monitoring the debtor's discharge of current claims, and, enforcing the performance of guarantees.

The powers of the rehabilitation administration are similar to those of the interim administrator.

Restrictions

The following restrictions (and consequences) will take effect from the date of the court's ruling on financial rehabilitation:

- monetary and property claims are only to be submitted under the bankruptcy procedures;
- previously introduced interim measures shall be cancelled;
- penalties will not accumulate further, (and they will relate to the last turn of the indebtedness repayment schedule);
- setting-off by counter claim(s), the alienation or purchase of shares or property, and the allocation of profits and dividends, are all prohibited.

The debtor must obtain the consent of a creditors meeting in order to perform the following: interested party transactions: property transactions exceeding 5% of the debtor's balance sheet value, the issuance of credit and guarantees, and any decisions about its reorganisation and the foundation of subsidiaries.

A rehabilitation administrator's consent is necessary for the following: 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 insolvency procedure intends to restore the debtor's solvency and may last up to eighteen months (with a possible six month extension). The combined duration financial rehabilitation and external administration shall not exceed two years. This stage of proceedings commences upon a court ruling, which is based upon the decision of a creditors' meeting.

External Administrator

The court approves the appointment of an external administrator when it makes a ruling on introducing external administration.

Amongst other things, the external administrator is entitled to:

- manage the debtor's property;
- make a settlement on behalf of the debtor;

- challenge the validity of debtor's transactions and any resulting associated damages before a court;
- refuse to perform a debtor's transaction, when such as transaction was not performed earlier in full or in part, if such a transactions creates loss in comparison with other transactions;
- challenge creditor's claims; and
- comply with the external administration plan and report on compliance before a creditor's meeting.

The external administrator's authority is terminated as of the date of the court's appointment of a liquidator (when the debtor is declared bankrupt), or the appointment of a new head of the debtor (when a settlement is made).

Restrictions

When external administration is introduced the authorities of the debtor's chief executive are terminated and transferred to the external administrator. The owner and the management bodies lose the right to (among other things): decide on the nominal value of shares, place shares, register capital increases, apply for the sale of the debtor's business, and to replace the debtor's assets.

A wide-ranging moratorium is imposed upon creditor's claims (excluding current payments).

Similar to the situation under financial rehabilitation, interim measures which were introduced earlier will be cancelled. Monetary and property claims, including mandatory payments, may only be submitted in accordance with the bankruptcy procedure.

Termination

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

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

- terminating external administration due to the restoration of the debtor's solvency;
- declaring the debtor insolvent;
- settlement; or
- the extension of external administration.

The court will evaluate the external administrator's report. If it considers it to be justified it will approve it, and make a ruling on the introduction of the next proceedings.

Insolvent liquidation

This procedure is designed to make a settlement of creditors' claims through the sale of a debtor's assets; it can be instituted for up 6 months (with a possible further 6 month extension).

Consequences of Winding-up

The immediate effects of the liquidation include the following:

- monetary obligations and mandatory payments incurred by the debtor are deemed to be due;
- interest will no longer be accumulated, and financial (or other) sanctions arising from a failure to fulfil monetary liabilities and mandatory payments (other than current payments) will be terminated;
- information on the debtor's financial state is no longer deemed to be confidential;
- previous property attachments shall be removed and no further attachments are allowed; and
- the powers of the CEO and management of the debtor will be terminated and vested in the liquidator.

The liquidator

The court appoints a liquidator when a ruling for insolvent liquidation is issued. The liquida-

tor acts until the winding-up process or court procedures are completed.

The principal role of the liquidator is to search, return, valuate, pool and arrange for a sale of the debtor's assets, and to make settlements with creditors. The liquidator also dismisses the debtor's employees. The liquidator assumes the powers of the debtor's CEO, its management bodies and its asset holders. The liquidator has to publish notice of the debtor's insolvency within 10 days of its appointment.

Insolvent liquidation: Order of Priorities

The Insolvency Law provides a specific priority order in which claims will be met. These is established as: certain 'current claims,' then first, second and third priority claims.

Current claims shall be met before first priority claims. *Current claims* include: claims made before the bankruptcy petition was accepted, any expenses related to the bankruptcy procedures (including the remuneration of employees and contractors) and operational expenses. *First priority claims* include personal injury claims. *Second priority claims* include redundancy payments, the wages of the debtor's employees and copyright loyalties. *Third priority claims* include all other claims.

Possible transition to External Administration

Where financial rehabilitation and/or external administration proceedings have not previously been instituted, the creditors' meeting may petition the court for a transition to the external administration procedure. To do so there must be grounds to believe that the debtor's solvency can be restored, and this must be backed by financial data. The transition will only be permitted if the debtor has sufficient property to pursue independent economic activity.

Voluntary Arrangement

This insolvency proceeding may be applied at any stage of an insolvency, in order to terminate proceedings and to give effect to an agreement between the debtor and creditors. The debtor, creditors, third parties and authorised bodies are all entitled to enter into a settlement or voluntary arrangement.

The creditors' meeting is responsible for approving the decision to enter into a voluntary arrangement with the creditors or an authorised body. The voluntary agreement may only be instituted on a court's approval.

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 who held at least a quarter of the value of creditor's 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.

Property

The Land Code and Other Applicable Legislation

The adoption of the Land Code in October 2001 overturned the legacy of state ownership of land and established the right of private land ownership in Russia.

The key legislation regulating the property and construction market in Russia includes:

- the Land Code of the Russian Federation No. 136-FZ dated 25 October 2001 (the "Land Code");
- the Civil Code of the Russian Federation: part I No. 51-FZ dated 30 November 1994; part II No. 14-FZ dated 26 January 1996; part III No. 146-FZ dated 26 November 2001; part IV No. 230—FZ dated 18 December 2006 (the "Civil Code");
- the Town-Planning Code No. 190-FZ dated 29 December 2004 (the "Town-Planning Code");
- the Federal Law No. 102-FZ dated 16 July 1998 "On Mortgages (Pledges of Immovable Property)" (the "Law on Mortgages");
- the Federal Law No. 101-FZ dated 24 July 2002 "On the Circulation of Agricultural Land" (the "Law on Agriculture Land");
- the Federal Law No. 122-FZ dated 21 July 1997 "On the State Registration of Rights to Immovable Property and Transactions Therewith" (the "Law on State Registration"); and
- the Federal Law No. 214-FZ dated 30 Deember 2004 "On Participatory Share

Construction for Multifamily Housing and of Other Immovable Objects and on Amending Certain Legal Acts of the Russian Federation" (the "Law on Participatory Construction").

Rights to Land

There are two basic types of rights to land plots provided by the Land Code:

- the ownership right to a land plot (freehold); and
- the right to lease the land plot (leasehold).

Russian land legislation pre-dating the Land Code also provided for other types of land rights such as, among others, the right of interim use to the land or the right of inheritable use. The right of interim use to land could only be granted to state, municipal or other public enterprises or to municipal authorities. Entities with rights of interim use will be penalised if they fail to convert to lease or freehold rights before 1 January 2010.

Sale of Land

The sale and purchase of land for construction is possible, provided that the land in question has first been allocated a cadastral registration number and has been registered as freehold with the Federal Service for registration, cadastre and cartography. Failure to comply with this requirement can lead to any land transaction connected with that plot of land being declared null and void. The Land Code provides that agreements establishing the seller's right to re-purchase the land plot at will, as well as provisions imposing restrictions on the use of the land plot by the buyer, are invalid. Similarly, any limitations on a seller's liability against third party claims will also be invalid.

One of the basic principles of the Land Code is the *unity* of rights to the buildings and the land plot. Rights to buildings can only be assigned together with the rights to the land underneath it. The law prohibits the assignment of land without the buildings and structures standing on it. In exceptional cases, buildings can be assigned separately from the land on which they are situated if it is impossible to separate the land, or if there is a restriction on the sale and purchase of the land.

Owners of buildings located on a land plot other than their own enjoy a pre-emptive right to purchase or lease that land plot. If the land plot is under state or municipal ownership, the owners of buildings have an exclusive right to privatise the land plot provided that they follow the set procedure and do so within the period stipulated by law.

In line with the principle of unity of rights to buildings and land plots, the Town-Planning Code provides that a construction permit can only be obtained by someone with rights to the land. Should someone construct a building on a land plot over which he has no rights, the building will be a "unauthorised construction".

Leases

Private individuals, legal entities, state and municipal authorities (as well as foreign individuals and foreign legal entities), may all (subject to certain restrictions) lease or own property in Russia.

Russian legislation places no general limitation on the terms of a lease. However, certain limitations exist with regard to leases for specific types of property. For example, the maximum term permissible for a lease of agricultural land is 49 years. This also applies to forest land. The maximum permissible term for the lease of coastal land is 20 years.

The Civil Code provides that where a term is not stipulated in a lease agreement, it is deemed to have been concluded for an indefinite period. Such a lease may be terminated by

either party serving notification at least three months in advance. A tenant has a priority right to any subsequent lease of the same land plot (and, on the sale of land, a priority right to purchase the same land plot).

As a general rule provided by the Land Code, leasehold rights to a land plot may themselves be sublet, assigned, mortgaged or contributed to the share capital of another entity. Unless otherwise provided for in the lease agreement, such transactions can be entered into without the consent of (but subject to the notification of) the landlord. However, the Land Code outlines an exception, under which a tenant is obliged to obtain the landlord's consent when the lease agreement is for a state or municipal land plot and is for a term of less than 5 years.

Any changes to the terms of a lease agreement require the consent of both parties.

The Civil Code provides for the rights of the landlord and tenant to unilaterally terminate an agreement in the situations stipulated by the Civil Code, or by the lease agreement. In these cases an out of court procedure is used.

The Land Code sets out an exception for a landlord's early termination of a lease agreement for state or municipal land. If the lease agreement is for a term of five or more years it can be unilaterally terminated by the landlord on the application of a court order. An application for such an order can only be made where there has been a material breach of the terms of the lease agreement by the tenant. The Land Code stipulates the circumstances in which a landlord may terminate a lease. These include, among others, the use of land in a way that is inconsistent with its designated prescribed use and appropriation by the State.

Land Privatisation

Since the Land Code came into force, it has become impossible to privatise buildings, structures or industrial objects without simultaneously privatising the land on which such structures stand. There are, however, some exceptions for land plots that are not used commercially, or have limited commercial use.

As mentioned above, a property owner has an exclusive right to obtain ownership or leasehold rights to the land plot on which any property stands, if they had obtained rights over this property before the Land Code came into force. Owners of the same buildings therefore may enjoy leasehold rights to the land, or rights of interim use. The building owner is free to choose whether to acquire freehold or leasehold rights to the land plot.

The Land Code initially contained an unclear provision stipulating that a lease agreement relating to a land plot on which a person's property is located does not prevent the owner of that property from obtaining ownership rights to the land. This provision was restrictively interpreted by the Highest Arbitration Court of Russia. It was ruled that ownership rights to the land could only be acquired in cases where the lease agreement was concluded before the Land Code came into force. These provisions were changed under legislation which came into force in the end of October 2007, according to which building owners have the right to acquire ownership rights over the land whether or not the lease agreement was entered into before the Land Code came into force.

Registration of Land Rights and Pre-existing Ownership Rights

State registration of the rights to land is currently carried out by the Federal Registration Service and its local departments. Locally registered property rights are subsequently entered

on a consolidated state property register that is open for public inspection.

Rights of ownership to land, as well as long term leasehold rights (for a period exceeding one year), are subject to state registration in accordance with Federal Law. Rights that require state registration are enforceable only after they are registered. However, rights to property that arose prior to this legislation coming into force (January 1997) are valid even if they are not registered.

Designated Prescribed use of Land

The Land Code divides land into a number of categories on the basis of its designated prescribed use. These are as follows:

- agricultural land;
- settlement land;
- industrial land (for the purposes of industry, energy, transport, communication, television, radio translation, cosmic activities, defence and other special purposes);
- specially protected areas (e.g. nature parks);
- forest land;
- coastal land; and
- reserved land.

The Land Code provides that the prescribed use of land should be stated in all title documents, agreements for the use of the land, and registration documents. Each category has different conditions for the use of land and the Land Code requires that each plot is used and exploited only in accordance with the applicable to the category. Land that is not used in accordance with its prescribed use can ultimately be withdrawn from the owner. The prescribed use of land may change depending on the permission granted by the relevant state, municipal or local authority.

Specific provisions may apply, depending on the type of designated use. For example, in the case of sale of agricultural land for private ownership, States of the Russian Federation enjoy pre-emptive rights of purchase, as do municipal authorities, in the situations provided for by the relevant regional legislation.

Mortgages

Both ownership and leasehold rights can be mortgaged. There are no restrictions in either the Land Code or the Civil Code on the grant of security over freehold or leasehold land. Rights to residential houses and apartments can also be mortgaged.

The terms and conditions of a mortgage are governed by the Law on Mortgages which provides that completed buildings and other real estate may be mortgaged, but only together with the rights that the building owner has to the land beneath the building.

Mortgages must be registered with an appropriate registration authority. The mortgage agreement only comes into force when it is registered. If a mortgage agreement is not registered it is null and void. Before the Law on State Registration came into force in January 1997, the registration of property rights was exercised by local authorities. Registration is now carried out by the Federal Registration Service.

Acquisition of Interests in Land by Foreign Investors

On the whole, foreign individuals and legal entities now enjoy the same rights to land as Russian individuals and companies. As such, they may lease or purchase land for use or construction.

However, the Land Code imposes a number of restrictions. Foreigners may not

own land in border territories, or other specially-designated territories. Furthermore, the Law on Agricultural Land provides that foreign individuals and legal entities may only acquire leasehold rights to agricultural land.

Acquisition of Land for Construction

Land for construction is allocated to a particular use. Such land can be purchased or leased.

The Land Code stipulates the procedure for making state-owned land available to individuals and companies for construction purposes.

An individual or legal entity (including foreign individuals 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 in court.

There are two possible options for obtaining land for construction from the state:

- a relevant state authority carries out preparatory work, i.e. it determines the boundaries of the land plot, registers the land plot (if necessary) and subsequently auctions the land plot or the right to lease the land; or
- an interested party applies to an 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 (such decision being valid for three years). If preliminary authorisation is given, the applicant must carry out all preparatory work on the land. Once the preparatory work has been completed, the relevant state authority decides whether or not to issue permanent authorisation for a construction site.

Housing Finance

Housing finance in Russia is governed by the Law on Participatory Construction. A developer, who must have certain rights to the land, may collect money from individuals or legal entities for the purpose of building 'multifamily' housing, or other forms of construction. Once the construction is complete, rights over the property are granted in the following ways:

- through a participatory share construction agreement;
- through participation in an "accumulative residential cooperative;"
- using housing certificates (setting out the owner's right to receive residential premises from the issuer);
- through the incorporation of a housing cooperative, with individual participation.

A participatory share construction agreement provides for the execution of a developer's obligations under the agreement. The obligations are secured by a mortgage over both the ownership to the land plot (or the leased rights to the land plot) and the respective property located on this land plot, in favour of the participants. The rights over the land plot are mortgaged from the moment that the agreement is registered with the state.

A participant can terminate an agreement unilaterally by serving written notice to the developer in the following circumstances:

- the developer fails to transfer the residential premises on time;
- the developer does not carry out repairs of construction defects following a request from a participant;
- the house is constructed in substantial breach of quality regulations;
- the developer breaches the rules of a surety agreement; or
- in other cases stipulated by federal law or by agreement between the parties.

The Federal law "On Protection of Consumers Rights" also applies to such agreements. According to this law, a consumer has the right to terminate the agreement unilaterally at any time, on the condition that the developer is paid for any actual expenses related to the performance of its obligations under the agreement. This provision explains, among other things, why developers often prefer to use other types of contracts and contractual schemes rather than participatory share construction agreements. Furthermore, legislation provides that it is only permissible to enter into a participatory share construction agreement once a construction permits has been obtained.

When there is unilateral termination of an agreement by a participant, the developer must return the funds paid to it by the participant within 20 working days.

As already explained, new legislative provisions make it clear that the person acquiring the title to residential premises also becomes entitled to the common property of that premises, including the land plot beneath it. The acquirer remains entitled to the plot even after the building is demolished or destroyed; during this period they have the right to initiate construction. If they do not exercise this right, the land plot may be withdrawn from them on the basis of a special procedure.

Licences and Permits

Currently the following activities relating to construction and design require licensing:

- the design of buildings and structures;
- the construction of buildings and structures; and
- engineering and surveying for the purpose of erecting buildings and structures.

The Licensing Commission of the Ministry for Regional Development was responsible for the licensing of these activities until 31 December 2008. According to the latest amendments to the Russian legislation the licensing of design, construction and engineering activities will be abolished from 1 January 2010. The new system requires entities who require a licence to be members of construction companies. These construction companies will be members of self-regulated organisations, who will be responsible for the issuing of licence certificates. It should be noted that the Commission from 1 January 2009 the commission will no longer issue licences. Licences issued before 1 January 2009 will be valid until 1 January 2010. During the transfer period between 1 January 2009 and 1 January 2010, both licences and the news certificates issued by the self-regulated organisations will be valid.

Land Regulation and Anti-monopoly Issues

Antimonopoly and competition issues are governed by a number of acts, including the Land Code, the Federal Law "On Privatisation of State and Municipal Property", and the Act "On Competition Protection" that came into force in 2006. The Federal Antimonopoly Service (FAS) is the national executive authority that oversees the adoption of regulatory acts. The FAS has a control and supervisory role to ensure compliance with antimonopoly legislation.

The legislation outlines a number of situations when the FAS must be notified of a proposed transaction. Notification must generally be made 45 days after the respective transaction has taken place. In a number of cases, post transaction notification is insufficient, and prior consent must be granted by the FAS

It is important to note that if the net value of the property that is the subject matter of a

real estate transaction (or a series of related transactions) exceeds 20 percent of the net value of the assets of the seller, then the following may apply:

- Pre transaction consent from the antimonopoly authority will be required if: (i) If the combined total asset value of the purchaser and the seller exceeds 10 billion roubles (approx. 240 million USD); or (ii) if their net profits from the realisation of goods over the last calendar year exceeds 8.6 billion roubles (approx. 2345 million USD) and thereby the asset value of the seller, according to the last balance sheet, exceeds 250 million roubles (approx. 6 million USD); or (iii) if one of the indicated parties is included in the register of entities that have more than a 35% share of the market;
- Post transaction notification of the antimonopoly authority will be required if (i) the total asset value of the purchaser, or net profit from the realisation of goods for the last calendar year, exceeds 400 million roubles (approx. 13.8 million USD) and thereby the net asset value of the seller exceeds 60 million roubles (approx. 2,070 thousand USD), or (ii) if one of the indicated parties is included in the register of entities that have more than a 35% share of the market;

A transaction which requires prior consent or notification from the FAS may be held to be invalid by the courts. The court must make an application to FAS, who may in turn declare the transaction to be invalid if it has, or may lead to, a restriction of competition. Thus provided such transactions are not appealed against in the court system, they are voidable, but not automatically void.

Failure to provide the information required by the FAS will incur an administrative liability.

Decisions taken by Antimonopoly Service may be subject to appeal.

Intellectual Property

General Approach

Russia has demonstrated a willingness to reinforce its attempts to combat infringement of intellectual property. Negotiations regarding Russia's accession to the WTO have stimulated Russia to adopt legislation approximating international standards for the protection of intellectual property rights, including provisions for criminal prosecution for breaches of intellectual property rights.

The need to ensure consistency in the regulation of different intellectual property issues has led to the adoption of Part IV of the Civil Code. This has codified the existing regulations concerning intellectual property rights and has introduced some new provisions and principles.Part IV of the Civil Code entered into force on 1 January 2008 and replaces the previous legislation regulating intellectual property rights, including the Copyright law, the Trademark law, the Patent law and the Software law.

In addition to part IV of the Civil Code certain IP issues are governed by orders of the Federal Service of Intellectual Property, Patents and Trademarks (Rospatent). Rospatent is subordinated to the Ministry of Education and Science and is responsible for the legal protection of intellectual property rights.

Russia is party to a number of the mostimportant international treaties and conventions on intellectual property issues, including:

- the Convention establishing the World Intellectual Property Organization ("WIPO");
- 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;
- the Nice Agreement on the International Classification of Goods and Services for the Purposes of the Registration of Trademarks;
- the Patent Cooperation Treaty ("PCT");
- 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.

Rights over the Results of Intellectual Activity and Means of Individualisation

General Provisions of the Civil Code

Part IV of the Civil Code sets forth a non-exhaustive list of the results of intellectual activity and protected means of individualisation. It stipulates some general requirements concerning their use and disposal. These are explained below.

The Licence Agreement

A licence agreement grants the right to exploit means of individualisation or a work which is under copyright protection within the limits set out in the agreement.

Under the Civil Code the licence must set out the following information; its duration, the territories for which the licence is granted and the ways the licenced object may be exploited. The licence may be granted on an exclusive or non-exclusive basis.

The agreement must fix the amount of remuneration, or the method of its calculation, in order to prevent the licence being 'onerous'. Remuneration may represent a sum fixed in advance and delivered as a single payment, or as periodical royalties, or as a percentage of income, or otherwise. The minimum amount of the authors' remuneration is fixed for certain types of works by government decree.

With regard to software and databases, the Civil Code permits the use of shrink-wrap licences, 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 vehicle 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).

Contracts for the Assignment of Exclusive Rights

Unlike a license agreement this type of contract provides for a total assignment of the exclusive property rights to that intellectual property. According to the Civil Code, such a contract involves transfer of the full and exclusive rights to that work or means of individualisation for the whole period for which the rights were protected.

State Registration of the Contracts

If the work or means of individualisation are subject to state registration, then the license, any assignment contracts, and any pledge contracts (as expressly provided for by the Civil Code), must also be registered or they risk being declared null and void.

Copyright and Neighbouring Rights

Copyright

Copyright covers scientific, literary and artistic work that is the product of creative work regardless of the value, type or mode of expres-

sion of that 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 their creations. The law 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;
- the right of distribution;
- the right of demonstration to the public;
- the right to import or export originals; and
- the right to provide access to the work by any means of telecommunication (including the internet).

Moral rights include (among other things):

- the right of authorship;
- the right to the name;
- the right to preserve the integrity of the work; and
- the right of publication.

The exclusive rights to the works are protected for the lifetime of the author, and for a further 70 years after his/her death. Infringement of copyright carries 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 holder of **neighbouring** rights is the performer of phonograms, the creator of databases and the broadcaster 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 rights.

The holding and the exercise of neighbouring rights is not subject to any obligatory registration formalities.

The rights enjoyed by holders of neighbouring rights may be granted by virtue of a license 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 result of an intellectual activity in the scientific and technical domain; and
— **industrial designs** which are the result of intellectual activity in the domain of artistic design.

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 be protected only if it is:

- New;
- Inventive; and
- Industrially applicable.

A utility model can be protected only if it is:

- New; and
- capable of industrial application.

A Utility model is not required to contain the inventive step required for a patentable invention.

An industrial design can be protected only if it is:

- New; and
- Original.

Unlike copyright, which attaches to the author's work from the day of its creation, a patent is only protected after state registration. The right to obtain a patent belongs to the inventor, his/her employer (in case of an employee's

invention) or their assignees. The application for patent protection is delivered to Rospatent, who examines the patent application and grants the patent if the relevant criteria are met.

The maximum duration for patent protection is as follows:

- 20 years from the date of filing of the application for an invention,
- 10 years from the date of filing of the application for a utility model,
- 15 years from the date of filing of the application for an industrial design.

The patent license *and* any assignment agreements need to be registered with Rospatent. It is also possible to obtain a compulsory license, following the decision of a court. Rospatent also regulates an open licence of a patent; an open licence may be chosen by the owner of the patent.

Trade Secrets and Know How

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 of 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. .

The law on Trade secrets (as amended to comply with part IV of the Civil Code) defines information that constitutes a trade secret and lists the measures that the rightholder must take in order to ensure protection of his know-how. The law also provides for civil, administrative and criminal liability for a breach of trade secret rights.

Employees' Works

The Code provides regulations concerning employees work. This includes literary work and patented objects that are created by employees as part of their employment duties.

As a general rule, exclusive rights to the results of employee's intellectual activities belong to the employer.

However, if the employer fails to use, license or assign their employees work within a prescribed period, *or* the employer fails to notify the employee that he 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 had started to use the work, assigned the rights to it, or decided to keep it secret, the employee is entitled to a level of remuneration as agreed between the parties. If the parties fail to agree on the sum, then a competent court may set the level of remuneration.

Means of Individualization

Chapter 76 of the Civil Code provides for the protection of 'signs' which are used to distinguish and identify both natural and legal persons, and the goods and services they offer.

Company Names

The Company Name is indicated in the corporate documents of the company, which are filed with the Unified State Register of Legal Persons. They are protected in Russia from the moment of the company's state registration.

Besides the name of the company, the state register also contains information on the entity's legal form.

The exclusive right of a company over its company name may *not* be transferred or licensed to third parties. This exclusive right allows the holder to freely use the name; on its sign, on letters, on official documents, in advertising, on products and on packaging.

Additionally the name of a company can be protected as a Trademark or a commercial name (a trade name); this protection operates

independently of a company's exclusive right over its company name.

Trademarks/ Service Marks

A trademark is a distinctive sign that is used to distinguish the goods or services of a person or an entity. A trademark can be a verbal description, a figurative or three-dimensional sign, or a combination of all of these elements. The Civil Code provides a list of words and signs that may not be used as trademarks.

The right to a trademark may belong to an individual entrepreneur or to a legal entity. To be protected in Russia, the trademark needs to be registered with Rospatent in the State Register of Trademarks. Alternatively it may be protected in Russia under the Madrid System of the International Registration of Marks.

The maximum duration for trademark protection is 10 years from the date of filing of the application with Rospatent. There is an option to prolong this protection period, subject to the necessary payment being made.

As a general rule the exclusive rights to a trademark are transferable to a third party, unless such an assignment could cause confusion for consumers.

The exclusive right to use a trademark may also be the subject of a license agreement. This may permit a third party to use that trademark within the framework of the license, and in accordance with the quality requirements set out by the licensor.

Trademark protection may be terminated early if the trademark is not used during three consecutive years from the date of registration. An application must be made by an interested person, and filed at the Chamber of Patent Disputes

Unlike under the previous legislation, the Civil Code expressly provides the legal interest of an applicant in the annulment of the non-used trademark.

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 location referring to the place of origin of the product. An appellation of origin registered with Rospatent is protected throughout the entire territory of Russia. Any producer acting within the geographical area designated by the appellation of origin may enjoy the right to use that name and, if the appellation of origin has not yet been registered, to register it.

Trade Names / Commercial Names

Legal entities and individual entrepreneurs may use trade names separately from their company name. Unlike the company name this trade name is not necessarily mentioned in the Charter Documents of the Company, or in the Unified State Register of legal persons. The trade name may be used as a distinctive emblem to distinguish a legal person. A legal person can have only one Trade name. A legal entity or an individual entrepreneur may not use a trade name w hich can lead consumers to confuse that name with a third party's Company Name or trademark. The right to use a Trade name to individualise a Russian company is valid throughout the territory of the Russia.

This exclusive right ceases to exist if the holder 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 commercial concession agreement, or by a contract for the rent of an enterprise.

Violations of Intellectual Property Rights

It is estimated that the market for counterfeiting in Russia represents about 1% of the global counterfeits market, although counterfeiting is a phenomenon difficult to quantify. Counterfeiting affects all areas of the Russian economy, including: luxury perfumes, cosmetics, clothing, foodstuffs, spare parts for cars, CDs, DVDs, drugs and pharmaceuticals. Counterfeit products are mainly distributed through open-air markets.

Recognising the magnitude of the problem and its potential impact on consumers' health and well-being (especially with regard to medicines), Russia has now demonstrated willingness to fight counterfeiting and to ensure the compliance of its laws with international standards.

Russian legislation now provides for civil, administrative and criminal liability for the breach of intellectual property rights. The sanctions depend on the amount involved and if the persons or entities involved are repeat offenders.

For example, the Code of Administrative Violations provides for a fine ranging from 1,000 to 1,500 roubles (about 28 to 42 USD) for an individual and 30 000 to 40 000 roubles (about 833 to 1 110 USD) for a legal entity that imports, sells, or rents items in violation of copyright, rights over inventions and patent rights.

The Penal Code provides for a fine of up to 200, 000 roubles (about 5 556 USD), or imprisonment for up to two years, when the unlawful use, disclosure or appropriation of an invention or patent has caused significant damage to the author. The same sanctions apply to violations of copyright and to the sale of counterfeit works.

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