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Doing business in Russia

Dear reader,

CMS is at the forefront of providing clients with specialist, business-focused advice in law and tax matters. With more than 4,500 legal professionals in 70 offices in 39 countries worldwide, who are trained in project management and work in sector-based teams, our key focus is on our clients and fulfilling their objectives.

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

From major multinationals and mid-caps to start-ups, we at CMS Russia have been welcoming investors to Russia for 25 years. We advise both international clients on every aspect of business in Russia, as well as assist Russian clients worldwide. Our history and expertise in the local market allow us to provide our clients with efficient, business-oriented and strategic advice. We provide a full range of legal and tax services across expert and sector areas including Banking and Finance, Commercial, Competition, Corporate and M&A, Dispute Resolution, Employment, Intellectual Property, Tax and others.

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

Russian legislation is changing rapidly and, although this guide describes the laws as of 1 January 2017, please contact us to check that it remains up-to-date. We would also recommend that you subscribe to our free CMS Russia news service through which you will receive our legal and tax alerts, invitations to our events and other news. You can do this by getting in touch with any of the CMS Russia key contacts listed at the end of this guide or our Marketing Department (cmsmoscow-marketing@cmslegal.ru).

We wish you every success.

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Political and administrative structure

Under the Constitution of the Russian Federation all state bodies are divided into:

— federal bodies;
— bodies of the "constituent subjects" of the Russian Federation; and
— local (municipal) bodies.

The holder of the highest office in the Russian Federation is the President.

The President

Under the Constitution of the Russian Federation, originally adopted on 12 December 1993 and from time to time amended (the "**Constitution**"), the President is the Head of State. The term of office of the President is six years. The President may only serve two consecutive terms. In 2012 Vladimir Putin was elected as President, replacing Dmitry Medvedev. The next presidential elections will take place in 2018.

The President appoints the Prime Minister and the Chairman

of the Central Bank of Russia. Both appointments must be endorsed by the lower chamber of the Russian parliament (the State Duma).

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

The President has broad authority to issue decrees and directives that in practice have the force of law. Under certain circumstances, he has the right to dissolve the State Duma.

The Government

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

The federal legislature

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

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

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

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

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

The judiciary

The judiciary is split into three branches:

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

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

The **courts of general jurisdiction** deal with criminal, civil and administrative cases involving individuals who are not engaged in business activities. Cases are heard by the district court unless they fall within the jurisdiction of the magistrates' courts or martial courts. The senior court of general jurisdiction is the **Supreme Court** of Russia (the "**Supreme Court**"). Decisions of the lower courts can be appealed through the intermediate courts, as far as the Supreme Court.

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

The Intellectual Property Court started operating in July 2013 as part of the commercial court system, (please see the *IP Court* section on page 154).

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

Regional and local political structure

In accordance with the Constitution (in its version of 21 July 2014), the Russian Federation consists of 85 "constituent subjects", i.e. regions within the federation. Regions are granted a certain degree of autonomy over their internal economic and political affairs. As cities of federal significance, Moscow, Saint Petersburg and Sevastopol enjoy the status of region.

The head of the executive branch of each region is directly elected in regional elections or by the legislative body of the respective region (if such option is set out in the constitution or the law of such region).

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

At the lowest level of the political system, local government was restructured as part of a major reform that started in 2003. This resulted in the creation of an intricate two-tier local government system where municipalities are subdivided into city districts on the one hand and municipal districts on the other, with municipal districts being further subdivided into urban and rural settlements.

Municipalities have their own budgets and depending on how much authority the regional government has delegated to them, they may enjoy certain limited taxation powers. They are also involved in the management of municipal land (they can act as landlords in lease agreements, allocate land plots for construction and act as seller during the privatisation of municipal land).

Legal environment

General background

The Russian legal system generally belongs to the continental European legal family. The legal structure developed at a rapid pace during the 1990s. During this period, significant reforms were enacted in almost every area of law as the country moved away from its Soviet command economy.

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

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

The Russian Civil Code (the "**Civil Code**") sets out the foundation of civil law and is the key source of law for business.

As part of the ongoing reform, significant amendments to the Civil Code concerning corporate law and the law of obligations came into force in September 2014 and June 2015. The key changes relate to the introduction of a number of concepts into Russian law which have for a long time been common to international practice in corporate, debt and general commercial areas, but have rarely, if ever, been recognised by the Russian courts. These amendments form the most significant development since the shaping of modern corporate law in Russia.

The most important innovations cover the following key areas:

- new classification of legal entities;
- corporate agreements;
- introduction of the "four-eyes" principle;
- conditional performance of obligations;
- the concept of representations (in Russian – "*zavereniya ob obstoyatelstvakh*") (an intended equivalent of "representations" and "warranties" as used in contracts under English law);
- the concept of the reimbursement of losses arising from the occurrence of certain events specified in a contract (the intended equivalent of the English law concept of an "indemnity");
- new types of civil law contracts, such as options, framework agreements and subscription agreements;
- rules for the conduct of negotiations to conclude a contract; and

— new mechanisms to secure the performance of contractual obligations by the parties.

These highly significant changes to the Civil Code are intended to accommodate the growing trend of submitting complicated transaction documents to Russian law and Russian courts. However, it is yet to be seen how the new concepts and provisions will be implemented in practice and whether they will be able to take the place of English law and international arbitration which were traditionally the "well-trodden path" in Russia.

WTO

Following 18 years of negotiations, Russia finally joined the World Trade Organisation in summer 2012 (please see the *Customs regulations* chapter on page 65).

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

Foreign investment

Legal regulation

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

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

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

Exclusions/restrictions

In addition to the so-called "strategic industries law" (please see the *Common forms of business structures for foreign investors* chapter on page 31), restrictions on foreign investment exist notably in the insurance and banking sectors.

Federal Law No. 4015-1 "On Insurance" dated 27 November 1992 currently prohibits foreign investors from owning more than 25% of the total market for

domestic insurance. Insurance companies in which foreign shareholders own more than 49% of the charter capital may not engage in certain types of insurance business, including, for example, life assurance.

In the banking sector, the Central Bank of Russia has the right to use reciprocity as a criterion to specify the types of business that subsidiaries or branches of foreign banks may be licensed to operate in Russia. In practice, however, branches of foreign banks are not able to carry out any banking activities on the Russian market. Additionally, a ceiling on the total amount of foreign bank capital, as a percentage of the total bank capital in Russia, can be imposed by federal law; however, no such limit applies at the time of writing. Under WTO rules, any such ceiling may not be less than 50%.

Sanctions

In 2014, the European Union and the United States of America (among others) imposed individual sanctions on certain Russian and Ukrainian nationals and entities that they believe to be responsible for the actions which led to the declaration of sovereignty by Crimea, and subsequently, it becoming part of the Russian Federation. Sanctions targeting certain sectors of the Russian economy (or so-called "sectoral sanctions"), as well as regional sanctions prohibiting certain economic activity related to Crimea and Sevastopol, have also been adopted.

In retaliation, Russia adopted countersanctions to prohibit the import of certain agricultural products, raw materials and foodstuffs from countries that have imposed sanctions on Russia (please see the *Customs regulations* chapter on page 67).

Sanctions against Russia

Even though each national sanctions regime will vary in scope, the restrictions imposed can be broadly characterised as follows.

Under the individual sanctions regime, travel restrictions and asset freezes have been imposed on individuals and entities listed under the relevant legal acts.

Sectoral sanctions have been imposed on the following sectors of Russian economy:

- **Energy sector**: the sale, supply, transfer or export of items for certain types of oil exploration and production projects in Russia and the provision of associated services is prohibited, or subject to prior authorisation by the competent authorities of the exporting country.
- **Financial sector**: major Russian financial institutions, as well as certain defence and energy companies, have been prohibited from dealing with bonds, equity or similar financial instruments with a maturity exceeding 30 or 90 days. It is also prohibited to make loans or credit available to any of the entities covered by the measures.
- **Defence sector**: Russia is subject to a weapons embargo. In addition, supplying dual use goods and technology to Russia is subject to individual authorisation by the respective

authorities of the exporting country. The authorisation will be denied if those items are intended for military use or for a military end-user. This type of sanction also affects the manufacture of civil goods and equipment.

The activities prohibited under regional sanctions include importations from and exportations to Crimea, as well as making new investments (either in general or in certain sectors).

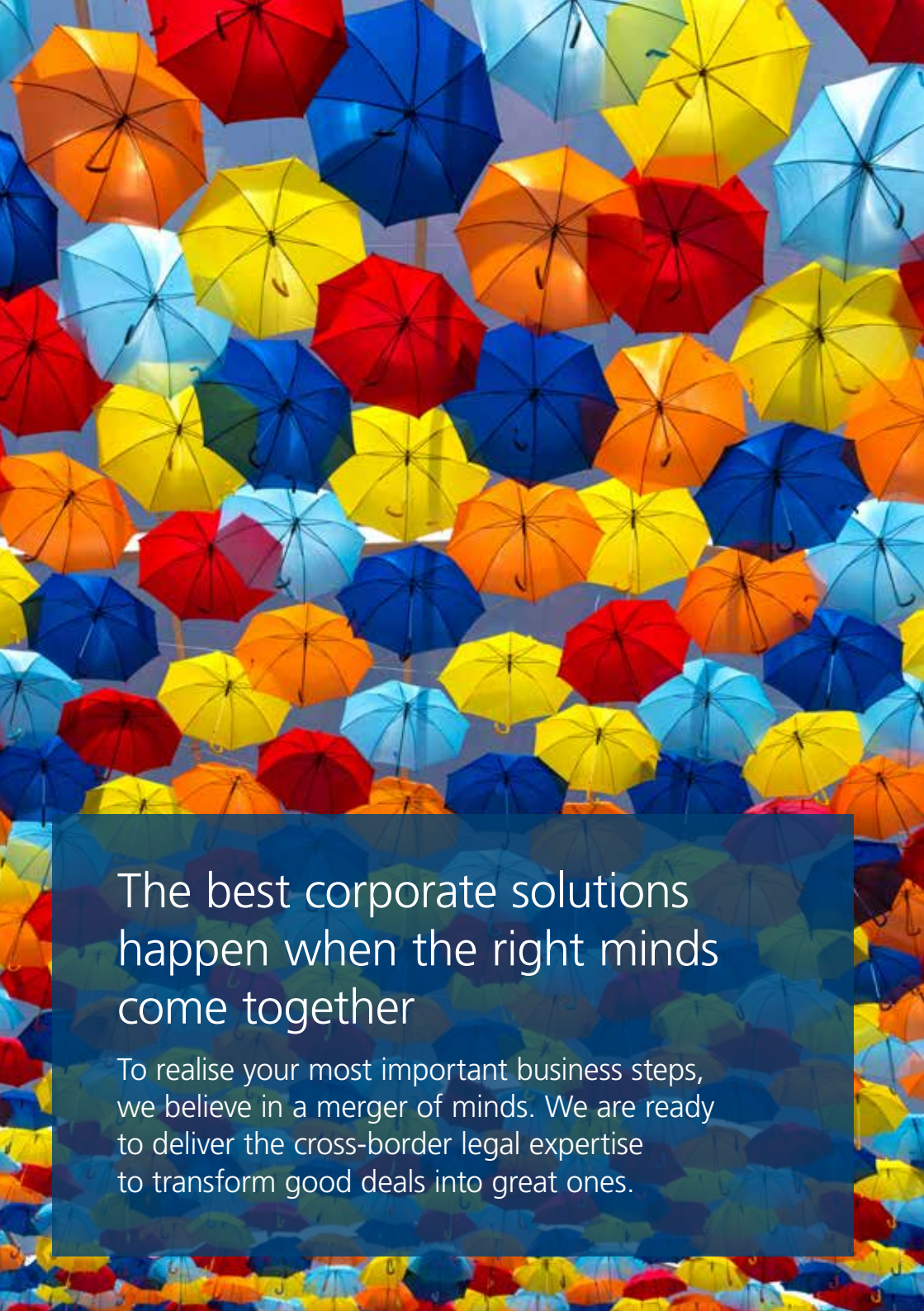
Sanctions imposed on Russia are not prohibiting all commercial activity. They are focusing on very specific individuals, entities, regions and economic sectors. Companies wishing to contract with Russian entities should carry out enhanced due diligence to ensure that they do not become involved in activities prohibited under the relevant sanctions regime.

Lobbying

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

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

"The Russian Civil Code sets out the foundation of civil law and is the key source of law for business."



The best corporate solutions happen when the right minds come together

To realise your most important business steps, we believe in a merger of minds. We are ready to deliver the cross-border legal expertise to transform good deals into great ones.

Common forms of business structures for foreign investors

General approach

Russian legislation provides for several types of business structure, of which the most commonly used are limited liability companies, joint-stock companies, representative offices and branches, as well as limited and unlimited partnerships. A basic description of each of these is set out in Part I of the Civil Code of 1994 (the "**Civil Code**"). Some other specialised structures also exist but are not commonly used by foreign investors. An individual is also entitled to conduct commercial activities in Russia, provided that he/she has the legal status of an individual entrepreneur. Foreign nationals can only register as individual entrepreneurs when they hold a temporary or permanent residence permit. The legal framework for individual entrepreneurs is also set out in the Civil Code.

Main types of structure

Russian legal entities

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

Joint-stock companies are classified as corporations that can be either public or private and limited liability companies are classified as private corporations.

Foreign investors in Russia mostly use the limited liability company and the private joint-stock company forms for their activity in Russia.

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

Limited liability company

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

Russian legislation prevents an LLC being wholly owned by another company ("*khozyaystvennoye obshchestvo*"), where that holding company is itself wholly owned by (i) another single legal entity; or (ii) a single individual.

The establishment, reorganisation and liquidation of an LLC is mainly governed by the Civil Code, Federal Law No. 14-FZ "On Limited Liability Companies" dated 8 February 1998 (the "**LLC Law**") and Federal Law No. 129-FZ "On State Registration of Legal Entities and Individual Entrepreneurs" dated 8 August 2001 (the "**Registration Law**").

Charter capital and contributions

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

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

The minimum charter capital of an LLC is currently RUB 10,000 (EUR 158[2]). The amount of the monetary fund for the charter capital must not be less than amount of the minimum charter capital.

The decision of the general meeting of participants to increase the charter capital and the list of members that were present at the general meeting have to be confirmed by a notary.

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

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

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

Net asset requirements and creditor protection

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

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

Participation

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

[1] Starting from 1 September 2013, the CBR performs the function of the securities market regulator and registers the shares issued by joint-stock companies.

[2] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

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

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

Beneficial owners

Since the end of December 2016, all LLCs must know who their ultimate beneficial owners are and take steps to collect certain information on them from the participants in the LLC. Such information must be disclosed to Russian state authorities upon request.

Management structure

The managing bodies of an LLC are:

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

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

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

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

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

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

The general participants' meeting has exclusive competence in respect of the list of matters specified by the Civil Code and LLC Law. This list can be extended in the company's charter at the discretion of the participants.

Resolutions of the general participants' meeting must be certified by a notary unless otherwise provided for by the charter. Alternatively, the particular resolution can be certified by the unanimous decision of the participants, except for the resolution on increase of the charter capital which in all cases must be notarised.

A **board of directors** is an optional supervisory body. Its authority typically includes appointing/dismissing the general director or approving certain types of transactions or transactions, the value of which exceeds certain thresholds.

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

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

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

The powers of the sole executive body can be provided to several executives of the company for individual or joint representation, which must be reflected in the Unified State Register of Legal Entities. However, this Register has not yet been amended to allow reflecting the authorities of each of the executives. As a result, the general rule that all executives indicated in the Register have equal and unlimited authorities applies and, thus, the four-eyes principle cannot currently be implemented vis-à-vis third parties.

A foreign national may be appointed as the general director of an LLC subject to compliance with work permit regulations (please see the *Employment/Migration* chapter on page 109).

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

Audit

The charter may provide for an **internal auditor** (either an individual or an internal audit commission established under the company's own charter). In some cases a company must have an internal auditor – as with companies having more than 15 participants – without which the general participants' meeting will not be able to approve the company's annual reports and balance sheets (as they

must first be approved by the internal auditor).

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

Transfer of participatory interests

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

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

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

A participatory interest transfer agreement must be notarised and the participatory interest is deemed transferred after the information on the transfer is registered in the Unified State Register of Legal Entities. This creates difficulties in the context of settlements between the parties to Russian agreements for the sale and purchase of participatory interests since the registration of the transfer takes five business days and is outside of the parties' control.

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

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

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

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

Right to withdraw

Participants in an LLC are entitled to withdraw from the company without the consent of other participants if: (i) this is permitted by the company's charter; or (ii) the transfer of participatory interest to a third party or another participant is prohibited and/or blocked by other participants; or (iii) the general meeting of participants approved a major transaction or a charter capital increase (in this event,

the right to withdraw is granted to any participant who voted against such decision or did not attend the meeting). The application of a participant for withdrawal from the company has to be notarised.

If a participant withdraws from the company, its participatory interest will be transferred to the company on the date when the withdrawal notice is served to the company. The company is then obliged to pay the exiting participant the "actual value" of its participatory interest in cash. The company may, however, pay the exiting participant in kind provided that the participant agrees to this.

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

Expulsion of a participant

Participants of the company are entitled to apply to the court for the exclusion from the company of a participant that commits a gross violation of its duties or whose actions or failure to act renders the company's operation impossible or significantly impairs it.

Where a creditor of a participant enforces against the latter's participatory interest, the LLC and/or the other participants are entitled to pay the actual value of such participatory interest to the creditor. If they do so, the participant withdraws from the LLC and its participatory interest is transferred to the other participants and/or to the LLC (depending on which of them satisfied the claim of the creditor).

Joint-stock companies

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

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

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

— the powers can be distributed between corporate bodies in various ways (e.g. management bodies can take over most questions of the general shareholders' meeting);
— the management bodies themselves can be omitted (e.g. the board of directors can act both as a management and supervisory body, a single director may replace the management board);
— the charter may provide a qualified majority of votes required to adopt certain decisions of the management bodies; and
— shareholders may define shareholders' rights in the charter non-proportionally to their stakes in the company, limit

the number of shares or votes held by one shareholder, provide for a pre-emptive right or consent on transferring shares to a third party.

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

Charter capital and contributions

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

The minimum charter capital is currently RUB 100,000 (EUR 1,587) for a public JSC, and RUB 10,000 (EUR 158) for a private JSC.

As with LLCs, **contributions** to the charter capital may be paid in cash or in kind. Other types of securities, such as corporate bonds, must be paid in cash only. Contributions in kind must be valued by an independent appraiser. It is possible to pay for new shares issued in a closed subscription by way of a debt-for-equity swap.

The charter capital may be increased by issuing new shares (within the number of authorised shares set out in the company's charter) or increasing the nominal value of the shares already in issue. Each capital increase must be filed and registered with the CBR, which is a lengthy process.

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

Net asset requirements and creditor protection

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

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

JSCs are required to file information on their net asset value with the Unified Federal Register of Activities of Legal Entities in addition to other filing requirements (www.fedresurs.ru). This requirement aims at increasing the transparency of the financial state of the company and protecting its creditors.

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

Beneficial owners

Since the end of December 2016, all JSCs must know who their beneficial owners are and take steps to collect the relevant information from their shareholders. Such information is to be disclosed to the state authorities upon request.

Management structure

The managing bodies of a JSC are:

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

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

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

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

The **collective management body** (e.g. board of directors, supervisory board) is responsible for the general management of the company but may not interfere with the exclusive competence of the general shareholders' meeting. It consists of at least five members and is mandatory for a public JSC.

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

The **collective executive body** (e.g. management board) is supervised by the collective management body of the company.

The company may have one or several CEOs (**sole executive body**). The sole executive body is responsible for the day-to-day running of the company and can represent the company without a power of attorney. In the case of appointment of several CEOs, they may be authorised to act individually or jointly and this

must be disclosed in the Unified State Register of Legal Entities. However, this Register has not yet been amended to allow reflecting the authorities of each of the executives. As a result, the general rule that all executives indicated in the Register have equal and unlimited authorities applies and, thus, the four-eyes principle cannot currently be implemented vis-à-vis third parties.

Legal entities may be appointed as the sole executive body.

A foreign national may be appointed as the general director of a JSC subject to compliance with work permit regulations (please see the *Employment/Migration* chapter on page 109).

Audit

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

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

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

Issue and transfer of shares

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

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

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

Acquisition of more than 30% of the shares in a public JSC by an existing shareholder or a third party triggers a mandatory buyout offer which needs to be supported by a bank guarantee and served to the remaining shareholders.

Shares of a **private JSC** are freely transferable between shareholders, although it is possible to introduce contractual restrictions by means of a shareholders' agreement. Share sales

to third parties are subject to statutory pre-emption rights of the other shareholders in the company (and the company itself if so provided in the charter).

Redemption of shares

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

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

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

Expelling a shareholder

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

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

Economic partnership

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

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

That said, the prohibition on an economic partnership acquiring or holding shares/interests in other companies and partnerships and on advertising its business generally precludes the use of this business structure for commercial trading operations or as holding companies for joint ventures.

Summary of legal forms

For ease of comparison between the legal entities described above, please refer to the comparative table on pages 23-25.

COMPARATIVE TABLE				
1	2	3	4	5
	PUBLIC JOINT-STOCK COMPANY ("PUBLIC JSC")	PRIVATE JOINT-STOCK COMPANY ("PRIVATE JSC")	LIMITED LIABILITY COMPANY ("LLC")	ECONOMIC PARTNERSHIP
Activities	Any type of activity (subject to licensing requirements)			Any type of activity (subject to licensing requirements) except for incorporating other legal entities, issuing bonds and other emissive securities, advertising
Term	Unlimited term, unless otherwise provided in charter			
Number of shareholders/ participants	Unlimited	Unlimited	1 to 50	2 to 50
Minimum charter capital	RUB 100,000 (EUR 1,587)	RUB 10,000 (EUR 158)		None
Type of interest in charter capital	• Ordinary shares • Preference shares		Participatory interests	
Issue of financial instruments	• Bonds • Other emissive securities			Prohibited
Subscription for shares	• Public subscription • Closed subscription	Closed subscription only	N/A	
Contributions to the charter capital	• Monetary funds • Contributions in kind			• Monetary funds • Contributions in kind, except securities other than certain bonds
Payment of the charter capital	Not less than 50% must be paid within three months, the rest within twelve months of the state registration of the company		The whole charter capital within four months of the state registration of the company	Specific procedure can be stipulated in the management agreement
Capital increase	Only after the charter capital has been fully paid up			Specific procedure can be stipulated in the management agreement
Capital decrease	• After notification of creditors and repayment of debts • Mandatory decrease in certain cases			

1	2	3	4	5
Managing bodies	• General shareholders' meeting • Collective management body • Collective executive body • Sole executive body (one or several CEOs)	• General shareholders'/participants' meeting • Collective management body (optional) • Collective executive body (optional) • Sole executive body (one or several CEOs)		• Director • The management structure is subject to the management agreement, e.g. any other managing bodies (board of directors, management board) are optional and subject to the management agreement
Transfer of shares/ participatory interests between shareholders/ participants	No restrictions, however acquisition of more than 30% triggers the mandatory offer obligation	No restrictions, unless otherwise provided for in a shareholders' agreement	Without restrictions, unless the charter provides for participants'/ company's consent or unless provided for in a participants' agreement	Without restrictions, unless otherwise provided for by the management agreement
Transfer of shares/ participatory interests to third parties	No restrictions, however acquisition of more than 30% triggers the mandatory offer obligation	• Can be subject to shareholders' pre-emption right under the charter • Can be subject to company's pre-emption right under the charter	• Subject to participants' pre-emption right • Can be subject to company's pre-emption right under the charter • Can be restricted by the charter • Can be subject to participants'/ company's consent • Subject to mandatory notarisation	Subject to all participants' consent and participants' pre-emption right
Exiting the company/ partnership (redemption/ withdrawal)	Shareholders may require the company to buy out their shares in limited cases: when they do not agree with certain decisions, including the reorganisation of the company, charter amendments which limit their rights, and the conclusion of major transactions		A participant may withdraw from the company if (i) permitted by the company's charter or (ii) the transfer of participatory interest to a third party or another participant is prohibited and/or blocked by other participants	Specific procedure can be stipulated in the management agreement

1	2	3	4	5
Expulsion of a shareholder/ participant	Squeeze-out by a shareholder who has acquired more than 95% of the voting shares	Shareholders may be expelled from the company through court action initiated by another shareholder[3]	Participants may apply to the court for the exclusion from the company of a participant that commits a gross violation of its duties or whose actions or omissions jeopardise the company's operations or significantly impair them	• Participants may bring a court action to expel any participant which grossly violates its obligations, or prevents or materially impedes the partnership's activities, or • Without bringing a court action if a participant fails to pay its interest
Liability of the company/ partnership	The company/partnership is not liable for the obligations of the shareholders/ participants			
Liability of shareholders/ participants	Liability is limited to the value of their shares/participatory interests (unless it can be demonstrated that their binding instructions to the company/partnership led to its insolvency)			

[3] Concept introduced by the amended Civil Code but yet to be implemented in the special legislation on joint-stock companies.

Other business structures

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

Representative office

Status

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

A representative office may, however, carry out representative functions on behalf of the parent company, including arranging marketing and advertising in Russia. It may also assist in other commercial and legal transactions between the parent and Russian organisations, including the rental of property.

At one time, an accredited representative office enjoyed a range of benefits that were not available to branches or companies. These benefits have been gradually withdrawn, although foreign employees of a representative office may still obtain personal accreditation. This involves certain practical benefits for the accredited foreign employee, such as the right to import and export personal effects free of customs duty and VAT, and it assists with obtaining multi-entry visas. In the past, there has been considerable debate about whether accredited employees of a representative office do actually require work permits. Now such employees must hold work permits in order to work in Russia (please see the *Employment/ Migration* chapter on page 109).

A representative office may hold a number of different types of bank account, including foreign currency 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 CBR regulations and other applicable legislation.

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

Management

A representative office acts on the basis of regulations approved by the parent company and is managed by the head

of the office who is authorised to conduct the business of the office and to represent the foreign company under a power of attorney. A representative office should also have a chief accountant.

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

Branch

Status

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

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

Foreign employees of a branch should also be personally accredited in the same manner as the employees of a representative office and, in addition, they must hold work permits in order to work in Russia (please see the *Employment/Migration* chapter on page 109).

Management

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

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

BUSINESS STRUCTURE	REPRESENTATIVE OFFICE	BRANCH
Formation	Two-step accreditation procedure: (i) review of the set of documents and confirmation of the number of foreign employees by the Chamber of Commerce and Industry of the Russian Federation; (ii) followed by registration by the Federal Tax Service	
Capacity	Technically restricted to representation, but functions in practice are often wider. Unable to hold title to property, or to import or export goods. May be unable to obtain certain permits and licences	Wider capacity. Usually able to obtain requisite licences and permits
Taxation	Capable of constituting a permanent establishment for Russian tax purposes and is subject to Russian taxation accordingly	Will constitute a permanent establishment for Russian tax purposes and is subject to Russian taxation accordingly
Foreign staff	Work permit for foreign employees is required	
Accreditation or renewal term	No limitation	

Other

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

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

Registration, liquidation and reorganisation of business structures

Registration of a Russian legal entity

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

Scope of registration

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

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

Registration mechanics

The tax authorities are responsible for the state and tax registration of companies, as well as for forwarding documents to the Federal Service for State Statistics and the Social Funds.

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

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

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

Payment of charter capital

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

Not less than 50% of the charter capital of a JSC must be paid within three months of its state registration, the rest within twelve months of the state registration of the company.

If a founder fails to pay the total amount of its shares/participatory interests within these time limits, then the non-paid shares/participatory interests become the property of the company. Such shares/participatory interests do not carry voting rights and are to be sold to the LLC's participants or third parties or cancelled (and the charter capital simultaneously decreased) within one year from the date of their transfer to the company.

Registration of the initial share issue

As shares in JSCs are treated as securities, certain additional registration requirements imposed by the CBR must be completed following the registration of the JSC's incorporation.

The share issue registration process consists of the following stages:

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

Anti-monopoly control

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

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

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

provided that, in either case, certain asset values or revenue thresholds are exceeded (please see the *Anti-monopoly issues* chapter on page 39).

Market regulator pre-registration clearance

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

Licensing

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

Accreditation and registration of a representative office and a branch

The function of registering representative offices and branches of foreign legal entities is now performed by the Federal Tax Service (except for the representative

offices and branches of foreign civil aviation companies and credit institutions that are accredited by Rosaviation and the CBR respectively).

As a result of accreditation, the representative office/branch is included in the State Register of Accredited Representative Offices and Branches of Foreign Legal Entities. Information from the State Register of Accredited Representative Offices and Branches of Foreign Legal Entities is publicly available on the Internet (www.service.nalog.ru/rafp.do).

In addition, representative offices and branches must be locally registered with the Federal Service for State Statistics and the Social Funds.

Company reorganisation

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

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

The creditors of a company can accelerate or terminate current obligations of a company participating in the reorganisation (e.g. a bank may accelerate a loan), however, this right of the creditors is significantly limited by the amended Civil Code.

Liquidation

A legal entity can be liquidated:

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

For more details, please see the *Corporate bankruptcy* chapter on page 90.

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

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

Shareholders' and participants' agreements

The Civil Code introduced a definition of "corporate agreement" that covers both shareholders' and participants' agreements.

These corporate agreements can be governed by non-Russian law (e.g. English law) if one of the parties to such agreement is a foreign person. This does not mean that the mere choice of foreign law will exclude the relevance of Russian law (its mandatory rules cannot be overcome) and the foreign law precedent commonly used in international joint ventures will

still need some adaptation for a Russian company but importantly, more general provisions of such agreements and boiler plate clauses can now be retained.

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

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

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

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

Strategic industries

The Foreign Investment Law[5], together with Federal Law No. 57-FZ "On Procedures for Foreign Investment in Companies of Strategic Significance for National Defence and Security of the Russian Federation" dated 29 April 2008 (the "**Strategic Industries Law**"), provides for a strict regulation of all transactions or agreements involving the participation of foreign investors in any entities engaged in activities in those sectors of Russia's economy which are deemed strategic for Russia's defence and security.

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

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

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

Restrictions on foreign investors

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

The procedure for obtaining a Strategic Approval is lengthy and cumbersome; however, if Strategic Approval is not obtained for a transaction requiring such

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

approval, the respective transaction is void under Russian law.

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

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

— directly or indirectly more than 50% of the voting shares in a Russian company operating in a sector deemed to be of strategic importance (a "**Strategic Company**") which does not conduct geological surveys on the subsoil and/or explore and extract minerals on subsoil plots of federal significance (i.e. not "operating federal subsoil plots");
— directly or indirectly less than 50% of the voting shares in a Strategic Company that is not operating federal subsoil plots, if the acquirer gains effective control over the company;
— directly or indirectly 25% or more of the voting shares of a Strategic Company operating federal subsoil plots; or
— control of a Strategic Company as a result of a change in the number of voting shares in that company.

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

Restrictions on state and international organisations

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

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

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

"Foreign investors in Russia mostly use the limited liability company and the private joint-stock company forms for their activity in Russia."

Anti-monopoly issues

General approach

General legal and regulatory framework

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

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

Trends

Clearly, the entry into force of the so-called "fourth anti-monopoly package" and the first results of its implementation are among the key developments in terms of strategic and practical impact on market players.

The most recent amendments to the Competition Law that came into effect on 4 July 2016 were aimed at reducing the burden on small and medium enterprises. More specifically, as part of this reform, the merger control threshold applicable to the value of assets of the target's group of companies (please see the table on page 39) had been raised from RUB 250m (EUR 3.97m[1]) to RUB 400m (EUR 6.35m). Further, subject to further conditions, a company with revenue below RUB 400m (EUR 6.35m) cannot be declared dominant.

In 2016, the FAS Presidium issued guidelines summarising its outlook and practice on certain important matters, including the determination of monopolistically high and low prices, vertical agreements, calculation of damages resulting from antitrust violations, and proof of prohibited agreements (cartels) and concerted actions.

Further changes can be expected in 2017: the FAS has put forward some initiatives relating to compulsory licensing of pharmaceuticals and the differentiation of liability for anti-competitive agreements.

Scope of application of the Competition Law

The Competition Law applies to:

— agreements/actions concluded or carried out in or outside Russia that may in any way influence competition in Russia; and
— agreements/actions concluded or carried out in or outside Russia,

[1] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

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We're here to anticipate problems before they happen. And when issues do arise, we help you act fast.

between Russian and/or foreign legal entities/individuals, which are related to:

- main (fixed) production assets and/or intangible assets located in Russia;
- shares or participatory interests in, or control over Russian legal entities; or
- control over foreign legal entities engaged in business activities in Russia.

The expression "legal entity engaged in business activities in Russia" encompasses all foreign entities that have supplied goods/works/services to the Russian market for an amount exceeding RUB 1bn (EUR 15.8m) during the calendar year preceding the date of the respective transaction.

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

Anti-competitive practices and restriction of competition

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

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

The Competition Law also includes rules on transaction clearance.

Abuse of a dominant position

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

An undertaking with a market share of less than 35% can be viewed as dominant only in the situation of collective dominance or if the thresholds provided for in the industry specific legislation apply.

A company with a revenue below RUB 400m (EUR 6.35m) cannot be declared dominant if certain other conditions set forth by the Competition Law are met (this exemption is mainly relevant for small and medium enterprises).

Dominance of a market is, in itself, not a violation. However, abuse of the dominant position gives rise to liability.

The actions of a dominant entity can be qualified as abuse if they harm the interests of market players or an unlimited number of consumers.

In addition to the prohibitions outlined below in the *Cartel agreements and concerted actions* section, dominant entities are prohibited from:

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

Cartel agreements and concerted actions

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

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

Vertical agreements

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

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

Economic coordination

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

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

Restriction of competition in general

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

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

As a general rule, the restrictions outlined in the *Cartel agreements and concerted actions, Vertical agreements, Economic coordination* and *Restriction of competition in general* sections above do not apply to agreements or actions between business entities that are part

of one group of companies if these entities are controlled by the same company/individual.

Unfair competition

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

- the distribution of false or incorrect information which may cause damage to a business entity, or impair its reputation (disparagement);
- the provision of misleading information in respect of a commodity's:
  - nature;
  - manner and place of production;
  - consumer characteristics;
  - quality and quantity; or
  - manufacturers;
- the incorrect comparison of the commodities produced by a business entity with those produced or sold by other business entities;
- an unfair acquisition and use of exclusive rights to the means of individualisation of a legal entity, goods, works or services;
- the sale, exchange or other placement into circulation of a commodity in breach of intellectual property rights, except for the means of individualisation of a competitor;
- the creation of confusion with a competitor's business or products; and
- the unlawful receipt, use and disclosure of commercial secrets, official secrets or other information protected by law.

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

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

Transaction clearance

Transactions subject to clearance

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

- the establishment of a Russian company if (i) its charter capital is paid up by shares and/or tangible or intangible assets of another company; and (ii) the new company, as a result, acquires:
  - more than 25% of voting shares in a Russian joint-stock company;
  - more than 1/3 of the participatory interests in the charter capital of a Russian limited liability company; or
  - more than 20% of the balance sheet value of the main production and intangible assets of the company which owns the assets (and whose assets are located in Russia);
- the reorganisation (in the form of a merger or accession);
- the conclusion of agreements between competitors on joint activities in the Russian Federation, including those on joint ventures;
- the acquisition of more than 25%, 50% or 75% of the voting shares in a Russian joint-stock company;
- the acquisition of more than 1/3, 50% or 2/3 of the participatory

interests in the charter capital of a Russian limited liability company;
- the acquisition of control over a Russian company;
- the acquisition of more than 50% of the shares/participatory interests or control over a foreign "legal entity engaged in business activities in Russia"; and
- the acquisition of the right to own, use or possess the main production and intangible assets of a company if the book value of the acquired assets located in Russia exceeds the following percentages of the total book value of the seller's main production and intangible assets:
  - 20% for companies operating on commodity markets; or
  - 10% for companies operating on financial markets.

Intragroup transactions

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

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

Thresholds

The thresholds set out on page 39 only apply to companies operating on the commodity markets. For those operating on financial markets, the requirements are different (please see the *Banking sector* chapter on page 74 for information on thresholds for banks (credit institutions)).

Liability

General remarks

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

Liability may include:

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

— fines and/or disqualification of company officials and, for the more serious anti-monopoly violations, up to seven years' imprisonment for company officials (under the Criminal Code).

Specific remarks

Prohibited agreements and leniency

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

However, the Code on Administrative Offences provides for a "leniency programme", i.e. a limited opportunity for companies that have participated in illegal anti-competitive agreements or actions to avoid penalties (the "**Leniency Programme**").

To obtain total immunity under the Leniency Programme, a participant to an anti-

PRE-TRANSACTION CLEARANCE THRESHOLDS*				
Agreements on joint activities in the Russian Federation among competitors				
Aggregate worldwide value of **assets** of the groups of companies involved	> RUB 7bn (EUR 111m)			
OR				
Aggregate worldwide **revenue** of the groups of companies involved from the sale of goods, works and services during the last calendar year	> RUB 10bn (EUR 158m)			
All other transactions				
Aggregate worldwide value of **assets** of the acquirer's group and the target's group of companies	> RUB 7bn (EUR 111m)	and	Aggregate worldwide value of assets of the target's group of companies	> RUB 400m (EUR 6.35m)
OR				
Aggregate worldwide **revenue** of the acquirer's group and the target's group of companies from the sale of goods, works and services during the last calendar year	> RUB 10bn (EUR 158m)	and	Aggregate worldwide asset value of the target's group of companies	> RUB 400m (EUR 6.35m)

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

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

Collective applications for the Leniency Programme are not accepted.

Changes to the Code on Administrative Offences brought by the "fourth anti-monopoly package" make it possible for the FAS to set the minimum amount of administrative fines against those who were the second or third to voluntarily report the conclusion of an anti-competitive agreement (cartel) to the competition authority.

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

Tax system

General approach

Trends

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

The key trend underlying recent Russian tax law developments is the so-called "de-offshorisation" of the economy which has become clearer in court decisions and legislation in 2016.

The most important amendments in this respect are as follows:

— The rules of CFC profit accounting were updated (in case of non-proportional distribution of profit, actual profit is taken into account in the determination of the taxable CFC profit of a controlling party).
— 2016 saw the introduction of an obligation for foreign legal entities to issue a statement on beneficiary ownership to Russian tax agents from whom payments originate, in cases when a foreign legal entity intends to apply double taxation treaty benefits.

2017 is the first time when notifications on controlled foreign companies need to be filed (controlling parties have until 20 March 2017 to do so).

In parallel, Russian authorities continue to tighten their control over taxpayers through applying the existing anti-abuse rules (notably, by developing the practice of application of transfer pricing requirements and extending the scope of application of thin capitalisation rules).

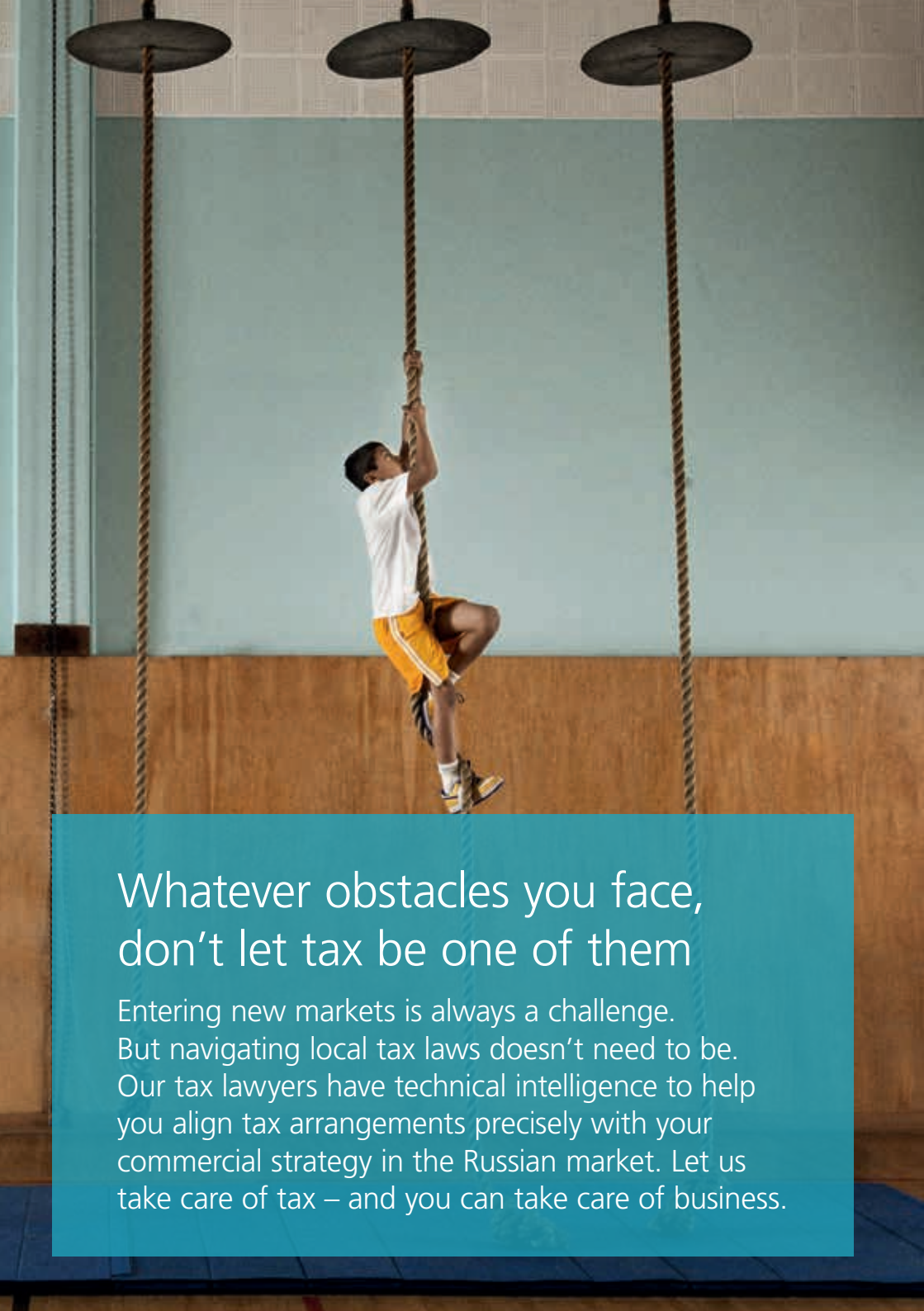
Core legal framework

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

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

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

— **Federal taxes** applied throughout Russia at uniform rates, such as VAT.



Whatever obstacles you face, don’t let tax be one of them

Entering new markets is always a challenge. But navigating local tax laws doesn’t need to be. Our tax lawyers have technical intelligence to help you align tax arrangements precisely with your commercial strategy in the Russian market. Let us take care of tax – and you can take care of business.

Certain taxes have a federal and a regional component (e.g. corporate profits tax) and may have their regional component reduced at the discretion of the relevant regional authority.

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

As a result of this tax structure, taxpayers may face tax and administrative burdens (including making tax filings and paying tax) both at federal and regional levels. Several tax payments may need to be made when a company has separate subdivisions in more than one Russian region.

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

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

Corporate taxation

Corporate profits tax

Taxpayers

Taxpayers are defined as:

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

Permanent establishments

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

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

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

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

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

The costs of a foreign company may be allocated to its Russian permanent establishment, provided that such costs were incurred for the purpose of that permanent establishment.

In the absence of a double taxation treaty, only the expenses incurred

by the permanent establishment may be deducted for tax purposes.

Definition of tax residency

Foreign companies may be deemed Russian tax residents if certain "key" and "auxiliary" criteria are met.

The key criteria are as follows:

- the activities of the executive body of the legal entity are regularly exercised in Russia, and more so than in any other country; and
- key corporate officials of the legal entity perform their actual daily management activities in Russia.

Auxiliary criteria apply by default when it is impossible to recognise a foreign company as a tax resident by using the key criteria above.

The list of auxiliary criteria notably includes the preparation of accounting and financial statements in Russia, as well as operational personnel management in Russia and record keeping in Russia.

Tax base

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

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

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

Deductibility of expenses

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

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

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

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

— representative expenses: up to 4% of payroll;
— pension and life insurance for employees: 12% of payroll;
— medical insurance for employees: 6% of payroll; and
— with respect to interest on loans and other borrowings:
  - for rouble loans, from 75% up to 125% of the Central Bank of Russia key rate since 1 January 2016;
  - for loans in Euros, from EURIBOR +4% up to EURIBOR +7%; and
  - for loans in US dollars, from LIBOR +4% up to LIBOR +7%.

If the interest rate under a controlled loan is outside abovementioned parameters, it must meet the requirements of the transfer pricing rules.

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

Depreciation

Depreciation should be calculated separately for each depreciable asset depending on the depreciation group it is classified as. The method applied should be clearly explained in the taxpayer's accounting policy. Once chosen, the accounting method may not be modified during the financial year (1 January to 31 December).

Two depreciation methods are available for profits tax purposes:

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

Depreciable property includes fixed and intangible assets with a useful life of at least one year and an initial value exceeding RUB 100,000 (EUR 1,587[1]).

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

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

Losses

Losses can be carried forward and offset against future taxable profits. From 2017 until 2020 inclusive offsetting losses from previous periods is temporarily restricted in terms of the amounts of losses to be carried forward. As a result of such a restriction, the reduction of the tax base should not exceed 50% of the losses incurred in previous years. Losses from the sale of fixed assets are recognised evenly over the remaining useful life of the assets.

[1] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

Transfer pricing

The Tax Code contains a specific section dedicated to transfer pricing principles, the tax supervision of transactions between related parties and advance pricing agreements.

Controlled transactions

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

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

Specifically, the list of related parties includes:

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

Methods

Russian legislation provides for the following five transfer pricing methods:

— comparable uncontrolled price method (CUP) having priority;
— resale minus method;
— cost plus method;
— comparable profitability method; and
— profit split method (treated as the "last resort" method).

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

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

Reporting and documentation requirements

Taxpayers are subject to an overall responsibility to prepare documentation justifying the prices applied in all transactions specified as controlled. Upon request from the tax authorities (which may be submitted from 1 June of the year following the year of the controlled transaction), taxpayers must submit the requested documentation.

In addition, companies are obliged on a yearly basis (before 20 May) to notify

their local tax inspectorates of all controlled transactions concluded between the same related parties during the previous calendar year. The notifications should contain general information on (i) the subject matter of the controlled transactions; (ii) the parties involved; (iii) the transfer pricing methods applied in the definition of prices; and (iv) the amount of profits received and expenses incurred as a result of these transactions.

Tax consolidation

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

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

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

Currently setting up consolidated tax groups is under a moratorium which is in effect until the end of 2018.

Tax rate

The general profits tax rate is 20%, with 3% of the tax being payable to the federal budget, and the remaining 17% being payable to the budget of the region where the company is incorporated.

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

Taxation of dividends

Dividends received by Russian companies

Dividends received by a Russian company from another Russian company, or from a foreign company, are taxed at a flat rate of 13%. Dividends received from "strategic investments" are exempt from Russian corporate profits tax. An investment is considered strategic when:

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

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

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

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

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

Controlled foreign companies (CFCs)

Definition of CFCs
Under Russian Law, CFCs are defined as foreign companies and structures that meet the following participation criterion: any foreign company or unincorporated structure (such as trusts, funds, etc.) which has a 25% participation interest owned by Russian tax residents (although the participation threshold is limited to 10% if other Russian residents also participate in the foreign company (or structure), and the total participation of all those Russian residents exceeds 50%).

At the same time, the profit of certain categories of CFCs stipulated by the Tax Code (for example, non-commercial organisations, active companies, residents of the Eurasian Economic Union, companies subject to high effective tax rate, etc.) are exempt from taxation in Russia.

Requirements
The Law provides for two key requirements that must be satisfied by Russian taxpayers who participate in CFCs and/or foreign companies: (i) notification requirements; and (ii) the obligation to pay taxes from the undistributed profits of the CFC.

In terms of the notification requirement, two main types of obligations of the Russian taxpayers are stipulated to submit notifications setting out:

— the details of the CFCs controlled by the taxpayer on an annual basis (not later than on 20 March of the year following the tax period in which the share of profit of the CFC is accounted for by the notifier); and
— setting out the taxpayer's participation interest in any foreign companies or structures other than CFCs, but only if such an interest exceeds 10% (not later than within one month from the date of exceeding the participation threshold);
— controlling party must submit the CFC notification prior to 20 March 2017.

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

If the taxpayer's aggregated income for three consecutive months, excluding VAT, is below RUB 2m (EUR 31,746), the taxpayer may be exempt if it applies for the exemption.

Tax base

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

- sale of goods, works and services within Russia;
- sale of e-services to individuals in Russia if effected by foreign companies with no presence in Russia (the so-called "Google tax");
- transfer of goods, works and services within Russia for the taxpayer's own purposes, if the relevant expenses are not deducted for the purpose of corporate profits tax;
- construction and building projects for the taxpayer's own use; and
- imports into Russia.

The **taxable base** is generally defined as the market value of the goods, works and services supplied, inclusive of excise duties but exclusive of VAT.

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

Exempt supplies

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

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

From 1 January 2017, the issuance of guarantees by non-banking entities is not VAT-able.

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

Input VAT

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

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

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

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

Any excess of input VAT over output VAT has to be refunded to the taxpayer. As a general rule, such a refund can only be made after the tax authorities have undertaken an audit. However, an accelerated VAT recovery procedure is also possible. Under this procedure, a taxpayer may recover VAT before the tax authorities complete the tax audit and have made a definitive decision on VAT recovery. According to these rules, companies which have existed for at least three years and paid taxes exceeding RUB 7bn (EUR 111m) over the last three years are eligible for the accelerated procedure, without having to provide a bank guarantee. Other companies can benefit from the accelerated procedure provided that they give a bank guarantee for the amount of VAT to be reimbursed.

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

Reverse charge

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

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

Filing and payment

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

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

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

Taxpayers must file their VAT declarations on a quarterly basis. VAT returns must be filed within 25 days after the end of the tax period.

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

All VAT taxpayers, irrespective of the number of staff, must file VAT tax returns electronically. This obligation also applies to branches and representative offices of foreign legal entities registered in Russia.

Excise duties

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

Excise duties are generally levied on the value of the product (please see the *Customs regulations* chapter on page 66).

Corporate property tax

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

Taxpayers

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

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

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

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

Tax base

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

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

Starting from 2018, implementing this tax relief will only be possible if it is introduced by the respective regional law.

The tax base for most assets is the average annual residual value of taxable property for financial reporting purposes. The cadastral value is used to calculate the corporate property tax base for the following types of property:

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

Tax rate

The rate is set at regional level.

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

The tax rate in respect of property for which the tax base is calculated based on the cadastral value may not exceed 2.2%. In Moscow, the maximum rate has been progressively increased from 1.5% in 2014 to 2% in 2016 and subsequent years.

Payments

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

Payroll-related levies

Taxpayers

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

Insurance contributions

Insurance contributions are paid to three separate non-budgetary funds: the Pension Fund, the Federal Social Insurance Fund and the Federal Mandatory Medical Insurance Fund.

From 2017, the administration and monitoring of social contributions for mandatory pension insurance, mandatory social insurance with regard to temporary disability and maternity and mandatory medical insurance is transferred to the tax authorities. In the 2017 calendar year, a regressive scale of insurance contributions is applicable: 22% is payable on the part of an employee's annual gross remuneration below RUB 876,000 (EUR 13,905) for contributions to the Pension Fund and 10% is payable on the part of any remuneration in excess of this amount; 2.9% (1.8% for foreigners and stateless persons temporary staying in Russia) is payable on the part of an employee's annual gross remuneration below RUB 755,000 (EUR 11,984) for contributions to the Federal Social Insurance Fund; and 5.1% is payable on the part of any remuneration for contributions to the Federal Mandatory Medical Insurance Fund.

However, payments and other compensation made to highly qualified foreign specialists (please see the *Employment/Migration* chapter on page 111) are exempt from social contributions.

Other payroll contributions

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

Taxes on natural resources

Taxpayers who use land, either on the basis of ownership rights or rights of permanent use, have to pay **land tax** to the local budget. The tax base used for calculation is the relevant land's cadastral value (which, in practice, is significantly lower

than its market value). The tax rate is set at a local level and may not exceed 1.5% of the cadastral value (0.3% in respect of certain types of land).

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

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

Transport tax

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

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

Sales duty

The provisions on sales duty were introduced to the Tax Code in 2014 and entered into force on 1 July 2015 in the territory of Moscow.

The taxpayers of sales duty are companies and individual entrepreneurs carrying out trade activities.

The sales duty base is defined as the value of movable or immovable property used for trade purposes. The amount of the sales duty paid is generally treated as an expense deductible for corporate profits tax purposes.

The sales duty rates are set by the regional authorities depending on the areas used for trade purposes.

State duties

According to the Tax Code, a state duty is a fee charged on companies and individuals for certain services supplied by state bodies.

By way of example, the state duties for registering a Russian company currently amount to RUB 4,000 (EUR 63) and for accrediting a foreign company's branch, RUB 120,000 (EUR 1,905).

The maximum state duties for the consideration of cases by the courts of general jurisdiction and by magistrates' courts ("*mirovye sudi*") are currently RUB 60,000 (EUR 952). The equivalent maximum state duties for the commercial courts now amount to RUB 200,000 (EUR 3,175).

Taxation of individuals

Income tax

Taxpayers

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

Tax residents are taxed on their worldwide income. An individual is considered to be a tax resident if he/she is physically present in Russia for at least 183 calendar

days during a 12-month rolling period. According to clarifications from the Ministry of Finance, however, the tax residence status of an individual should be defined by counting the days spent in Russia within the relevant calendar year.

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

Taxable income

This is gross income less deductions and exemptions.

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

Deductions and non-taxable income

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

- **standard deductions** are available for certain categories of taxpayers (disabled persons, war veterans, etc.);
- **social deductions** comprise of educational expenditures (per taxpayer and each of his/her children) and medical expenditures (per family), up to a combined annual maximum of RUB 120,000 (EUR 1,905);
- **investment deductions** relate to certain types of investment income of taxpayers, such as long-term investments in pension and insurance funds;
- **property deductions** relate to the purchase and sale of property (mainly residential real estate);
- **professional deductions** are generally permitted for individual entrepreneurs and include, for example, expenditure for the creation of intellectual property rights.

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

Tax rates

Residents

A standard flat rate of 13% applies to most types of income.

A rate of 35% applies to certain prizes, insurance receipts and interests from bank deposits in excess of specific limits.

Non-residents

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

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

Tax payments

Withholding of tax

Russian companies, individual entrepreneurs and permanent establishments of foreign companies are considered to be tax

agents. They must calculate, withhold and pay income tax on the payments they make to individuals.

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

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

Tax return

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

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

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

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

Individual property tax

Taxpayers

The owners of houses, flats, rooms, cottages, garages, other buildings or constructions are liable to pay individual property tax.

Tax rates

As from 1 January 2015, the cadastral value of the property is used as a taxable base to calculate individual property tax. The applicable tax rate depends on the type of taxable property concerned.

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

Special tax regimes

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

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

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

Simplified tax system

Taxpayers

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

— their annual turnover does not exceed RUB 112.5m (EUR 1.79m);
— the combined net book value of their fixed and intangible assets does not exceed RUB 150m (EUR 2.38m); and
— they employ fewer than 100 persons.

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

Tax rates

The rate for this tax regime is as follows:

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

The tax rate may be reduced under the relevant regional law down to 0%.

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

Tax on imputed income

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

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

Unified agricultural tax

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

Taxpayers

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

Tax rate

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

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

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

Production sharing

Taxpayers

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

PSAs provide for the sharing of profitable production between the Russian state and an investor. A part of "compensational production" is granted to the investor to compensate them for the expenses connected with the project. In general, this does not exceed 75% of the whole amount of production or 90% when the project is implemented on the Russian continental shelf.

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

General PSA regime

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

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

Special PSA regime

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

Incentives

Regional incentives

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

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

These incentives may include:

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

Special economic zones

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

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

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

Types of SEZ

There are four types of SEZ:

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

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

Skolkovo innovation centre

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

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

— 0% corporate profits tax rate applicable to income generated as a result of research, development and commercialisation for the first ten years of a participant's registration in the Skolkovo project;
— exemption from property tax and land tax;
— reduced payroll-related taxes;
— VAT exemption;
— reimbursement of customs duties and VAT payable upon the importation of goods;
— exemption from the obligation to keep financial accounting, unless

the participant's annual income exceeds RUB 1bn (EUR 15.8m); and
— exemption from the payment of state duties for the issuance of work permits, invitations and visas for foreign employees.

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

Territories of advanced social and economic development

Taxpayers can benefit from specific incentives granted to residents of territories of advanced social and economic development ("**TASEDs**") created at the end of 2014 in order to boost the development of the economy and attract foreign investment in those territories. Each TASED is established by a Resolution of the Russian Government.

Currently nine TASEDs have been created, located in the Far East of Russia (e.g. Kamchatka, Khabarovsk) and in Yakutia (in the industrial park Kangalassy). To obtain the TASED resident status, legal entities and individual entrepreneurs must conclude an investment agreement with the authorities.

TASED residents have a right to apply reduced corporate profits tax rate subject to conditions stipulated by the Tax Code and applicable regional regulations.

Free port of Vladivostok

The regime of the "free port of Vladivostok" has been introduced to the Russian legislation in 2015 in order to establish special status for a territory in Primorskiy Krai for a renewable term of seventy years. Most of the provisions regulating the status of the free port and respective incentives took effect on 1 January 2016.

The legislation on the free port of Vladivostok allows legal entities and individuals having obtained the resident status to benefit from certain tax, customs and administrative benefits and incentives.

In order to obtain such resident status, the applicant must fulfil the following criteria:

— implementing a new investment project; and
— investing an amount of at least RUB 5m (EUR 79,365) in the project's implementation (in the form of capital expenditures) within a period not exceeding three years as from the date when the investor obtained the resident status.

Legal entities or individual entrepreneurs satisfying the above conditions must (i) apply to the management company of the free port of Vladivostok (by submitting a set of supporting documents including, notably, the business plan of the investment project); and (ii) conclude an agreement on the conduct of the investment activity with the management company.

Incentives and benefits granted to the residents of the free port of Vladivostok include the following:

— from a **tax** standpoint: reduced corporate profits tax rate, simplified system of VAT refund and reduced rates of social contributions (in cases when the resident is subject to the general taxation regime and its proceeds from business activities in Vladivostok constitute at least 90% of the total amount of its proceeds);
— from a **customs** standpoint: possibility of benefiting from the customs regime of free customs zone;
— from a **migration** law standpoint: a simplified procedure of entry into Russia for foreigners employed by the residents of the free port of Vladivostok.

Double taxation treaties

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

Tax treaties signed by Russia are usually based on the OECD Model Treaty and the United Nations Model Convention.

The provisions of these treaties override Russian domestic law.

The table on page 61 contains the tax rates applicable under several DTTs 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.

In 2016, the DDT with Singapore was updated.

In 2017, a new DDT with Hong Kong came into force.

From 1 January 2017, foreign companies wishing to obtain benefits under DDTs must provide Russian tax agents with a statement on beneficial ownership.

"Russian authorities continue to tighten their control over taxpayers through applying the existing anti-abuse rules. They notably do so by developing the practice of application of transfer pricing requirements and extending the scope of application of thin capitalisation rules."

Country	Dividends	Interest	Royalties
Austria	5 or 15%[1]	0%	0%
Belgium	10%	0 or 10%[2]	0%
Canada	10 or 15%[3]	10%	0 or 10%[4]
China	5 or 10%[5]	0%	6%
Cyprus	5 or 10%[6]	0%	0%
France	5, 10 or 15%[7]	0%	0%
Germany	5 or 15%[8]	0%	0%
Hong Kong	5 or 10%[9]	0%	3%
Ireland	10%	0%	0%
Italy	5 or 10%[10]	10%	0%
Japan	15%	10%	0 or 10%[11]
Korea (South)	5 or 10%[12]	0%	5%
Luxembourg	5 or 15%[13]	0%	0%
Netherlands	5 or 15%[14]	0%	0%
Singapore	0, 5 or 10%[15]	0%	5%
Spain	5, 10 or 15%[16]	0 or 5%[17]	5%
Switzerland	5 or 15%[18]	0%	0%
Ukraine	5 or 15%[19]	10%	10%
UK	10%	0%	0%
USA	5 or 10%[20]	0%	0%

Notes:

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

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

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

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

[5] 5% for shareholdings of 25% or more, provided the investment is at least EUR 80,000, otherwise 10%;

[6] 5% if the initial investment is greater than EUR 100,000, otherwise 10%;

[7] 5% if the investment is not less than EUR 76,225 and if the recipient pays tax; 10% if only one of these two circumstances applies; otherwise 15%;

[8] 5% for shareholdings of 10% or more, provided the investment is at least EUR 80,000, otherwise 15%;

[9] 5% for shareholdings of 15% or more, otherwise 10%;

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

[11] 0% for royalties in respect of literary, artistic or scientific works including films and tapes; 10% for royalties in respect of any patent, trademark, design or model, plan, secret formula or process, or industrial, commercial or scientific equipment, or information concerning industrial, commercial or scientific experience;

[12] 5% for shareholdings of 30% or more, provided the investment is at least USD 100,000, otherwise 10%;

[13] 5% for shareholdings of 10% or more, provided the investment is at least EUR 80,000, otherwise 15%;

[14] 5% for shareholdings of 25% or more, provided the investment is at least EUR 75,000, otherwise 15%;

[15] 0% for government and state institutions, 5% for shareholdings of 15% or more, otherwise 10%;

[16] 5% for shareholdings of at least EUR 100,000 and if the dividends are exempt from tax; 10% if either condition is met; otherwise 15%;

[17] 0% if the actual recipient of interest is the government of the other contracting state, or for long-term bank loans (exceeding seven years); otherwise 5%;

[18] 5% for shareholdings of 20% or more, if the investment is at least CHF 200,000; otherwise 15%;

[19] 5% for shareholdings of at least USD 50,000; otherwise 15%; and

[20] 5% for shareholdings of 10% or more, otherwise 10%.

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Customs regulations

General approach

Russia is a member of the Eurasian Economic Union (the "**EEU**") of Belarus, Kazakhstan, Armenia, Kyrgyzstan and Russia and the World Trade Organisation (the "**WTO**").

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

The first stage of the creation of the EEU was the establishment of the Customs Union which resulted in the creation of a single customs territory between the founding states (Belarus, Kazakhstan and Russia). Following that achievement, the member states continued their phased economic integration by forming the Single Economic Space, which was technically established on 1 January 2012. The integration process had been completed by the signing of the Treaty on the EEU, which came into force on 1 January 2015 and the EEU superseded the Eurasian Economic Community (the previous integration stage). Ultimately, the EEU will result in the creation of a common market allowing free circulation of goods, services, capital and labour between its member states. Another aim of the EEU is the adoption of unified policies with respect to competition and natural monopolies. The scope of matters regulated at the EEU level is expanding and includes key sectors of the economy, such as a unified competition law, the free movement of capital and labour, a macroeconomic policy and others.

The customs borders of the EEU also gradually expanded. Armenia joined the EEU at the end of 2014, while Kyrgyzstan joined the EEU in 2015.

Customs regulation in the EEU Key features

- Customs control has been moved from the borders between the member states of the EEU to the outside borders of the EEU. As a result, customs, veterinary, sanitary and border control are now all performed at the outside borders of the EEU.
- Joint inspection by the customs authorities of the EEU member states (such as transport, vehicular control on the outside border of the EEU, and sampling of goods for obligatory veterinary control) are made on a "single window – one stop" clearance basis to accelerate border crossings.
- No obligatory customs-clearance procedures exist between the member states.
- Customs duties and other economic restrictions do not apply to trade

between the EEU members, with the exception of special protective, anti-dumping and compensatory measures.

— Each member of the EEU is obliged to use a unified nomenclature of goods and non-tariff regulatory measures for trade with non-member states.
— Import duties are payable to a special accumulation account and are allocated between the members of the EEU according to the following proportion: Armenia – 1.11%; Belarus – 4.56%; Kazakhstan – 7.11%; Kyrgyzstan – 1.9%; and Russia – 85.32%.
— Customs duty rates with respect to export to non-EEU countries are indicated in the laws of the respective exporting state. Export duties are paid to the budget of the country of production and are not allocated between the EEU members.
— 0% value-added tax ("**VAT**") is charged on goods exported within the EEU territory. Goods imported within the EEU territory are exempted from excise duties and indirect taxation.
— Customs authorities may challenge the declared customs value for customs clearance for a period of up to three years following the goods' release. For certain types of products, this term may be extended up to five years by internal legislation.
— There is a unified register for items of intellectual property registered in the territory of the EEU.
— Authorised economic operators ("**AEOs**") are in operation and provide simplified customs clearance procedures. They are permitted to store goods at their own warehouses and release them into free circulation before submitting a customs declaration. To carry on such an activity, a legal entity must obtain a special status of AEO under the national legislation of each member state of the EEU.
— Statistical databases for streamlining the control and analytical functions of the customs authorities, as well as enabling the exchange of information between the EEU member states are in place.

Recent developments of the EEU's customs regulation

At the end of 2016, all EEU member states except Belarus signed the new Customs Code which had been approved by the Intergovernmental Council of the EEU in mid- November . It will replace the current Customs Code of the Customs Union. The new document is a result of lengthy negotiations among the member states on key issues of customs regulation. These issues are covered by 20 international agreements, which are fully integrated into the EEU Customs Code.

To become effective, the new Code will have to be signed by Belarus and subsequently ratified by all the EEU member states.

Due to the "de-offshorisation" trend, special simplified procedures for AEOs importing goods from, or paying for imported goods through, territories listed as offshore territories by the Ministry of Finance were revoked.

The customs internal risk management system was extended to cover

operations with residents of offshore territories and operations potentially related to the non-repatriation of currency by Russian residents.

Excise duties with respect to certain products (e.g. tobacco and alcohol) were decreased in 2015. This is in line with the general trend that resulted from WTO accession. Tariffs are expected to continue to go down (please see the *WTO* section below).

All legal entities are required to submit forms declaring goods transported across the border of the EEU electronically (since 1 January 2014).

EEU member states are working on the unification of their currency control and anti-monopoly legislation and are working towards the adoption of principles which unify the currency control policy within the EEU.

EEU member states are working on improving customs valuation methods. The **requirement** to prove the absence of interdependence between the declarant and its supplier with respect to determining the customs value of goods has been replaced by the **right** to do so.

WTO

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

— the decrease of the average weighted customs tariff rate for the import of goods to the Russian territory from 10% to 7.8% (for industrial goods from 9.4% to 6.4%, for agricultural products from 13.2% to 10.8%); and
— the lifting of certain restrictions on foreign ownership in specific sectors such as telecoms, insurance and banking.

Various transitional periods were established with respect to certain products, industries and services.

The longest transitional period has been set for insurance and banking services. Foreign companies will be allowed to establish Russian branches in 2021. The maximum foreign participation in Russian banks is 50%.

Furthermore, the accession to the WTO Government Procurement Agreements, which was originally envisaged, did not materialise. Thus, Russia has reserved a right to limit access to public procurement to foreign goods and services.

Trade between EEU and non-EEU countries

Overall, there are 17 types of customs procedures, including the import and export procedures established by the Customs Code. Below, we give a brief description of the three most commonly used customs procedures and an overview of the general features of importing and exporting.

Most commonly used customs procedures

Release for internal consumption

Importation of goods for internal consumption is a procedure which provides for the foreign goods placed under it to be located and used on the customs territory of the EEU without restrictions as to their use and disposal, provided that all applicable customs duties and taxes have been paid.

Customs transit

Customs transit is a procedure under which goods are transported for a specified period[1], under the control of the customs authorities, over the customs territory of the EEU without customs duties and taxes being paid. Under this procedure, prohibitions and restrictions can apply except for measures of non-tariff and technical regulation.

Under customs transit, a special transit customs declaration and the payment of a security in respect of customs duties and taxes are required.

Customs warehouse

Customs warehouse is a procedure under which foreign goods are stored under the control of the customs authorities at a customs warehouse for a specified period without customs duties and taxes being paid and without applying measures of non-tariff regulation.

Goods may not be under the customs warehouse regime for a period of longer than three years, with an option to extend this period with the permission of the customs authorities. Goods with a limited useful life and/or sale duration must be assigned to other customs regimes and shipped from the customs warehouse at least 180 days prior to the expiration of such period.

Importing

Declaring procedures

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

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

Customs payments (VAT, customs and excise duty)

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

[1] Customs transit may not last longer than a period determined in accordance with the following formula: 2,000km per month from the point of crossing of the EEU border.

The forms and the timeframes for customs payment are determined by the legislation of the respective member state. For instance, under Russian law, customs payments for goods imported into Russia must be made on or prior to the day the customs declaration is submitted to the Russian customs authorities.

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

Customs value

The customs value of goods imported into the EEU is determined under the Treaty dated 25 January 2008 "On the Determination of the Customs Value of Goods Crossing the Customs Border of the Customs Union" and consists of the cost of the goods as well as insurance and transportation expenses.

The Russian customs authorities often try to challenge the customs value of the goods. When they increase the customs value, this may be contested in court.

Import duties

The EEU member states are obliged to apply the common customs tariff and unified nomenclature of goods to goods imported into the EEU and to the customs value of such goods.

Tariff privileges

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

Tariff preferences

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

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

Non-tariff restrictions

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

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

Restrictions on the import of certain goods

On 7 August 2014, the Russian Government issued Decree No. 778 pursuant to an Order of the Russian President. The Decree (as subsequently amended) prohibits the importation into Russia of certain agricultural products, raw materials and foodstuffs which originate from the USA, the EU, Canada, Australia, Norway, Ukraine[2], Albania, Montenegro, Iceland and Lichtenstein.

[2] Applicable from 1 January 2016.

Order No. 560 of the Russian President dated 6 August 2015 introduced a new measure to ensure the fulfilment of the above restrictions. Since this date, "sanctioned products" imported into Russia will be destroyed.

Exporting

Declaring procedures

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

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

Customs value

The customs value of goods exported from the EEU by a Russian-based company is determined under the internal legislation of the Russian Federation and consists of the cost of the goods as well as insurance and transportation expenses.

The Russian customs authorities often try to challenge the customs value of the goods. When they increase the customs value, this may be contested in court.

Export customs duties and payment

Export duties are to be paid to the country from which the goods originated. Export customs duties are set by the Russian Federation as there is no unified list of export customs duties for the EEU.

Non-tariff restrictions

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

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

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

VAT

Goods exported to non-EEU countries from Russia are subject to a 0% VAT rate and are exempt from excise duties, provided that the export of goods is properly documented. The following documents must be submitted in order to claim the 0% VAT rate:

- the contract for the exportation of goods;
- a customs declaration stamped by the customs authorities confirming that the goods were exported out of Russia;
- copies of transferring documentation (invoice, transfer and acceptance act, VAT invoice or "*shchet-faktura*").

The above documents must be submitted to the tax authorities within 180 days after the export of the goods, failing which the taxpayer loses the right to apply the 0% VAT rate on exports and must apply the general VAT rate (10% or 18%).

Recycling and environmental fees

Amendments to the Federal Law "On the Production and Consumption of Waste" under Federal Law No. 278-FZ dated 21 October 2013 introduced new types of fees.

The recycling fee must be paid for each wheeled or self-propelled vehicle imported into the Russian Federation. The procedures and amounts of the recycling fee are established under Government Decree No. 1291 dated 26 December 2013 and Government Decree No. 81 dated 6 February 2016. Certain categories of imported wheeled vehicles are exempt from the recycling fee, namely:

- personal vehicles of refugees or persons under the programme of resettlement of fellow citizens;
- vehicles of diplomatic and consular missions, international organisations; and
- vehicles which were manufactured 30 or more years ago, which are not intended for commercial passenger and cargo carriage, or retro-vehicles.

Since 1 January 2015, the environmental fee must be paid by importers of goods that are subject to recycling once they have lost their consumption properties (please see the *Environmental fees relating to emissions, discharges and waste management* section on page 169).

Mutual trade between the EEU members

Free circulation of goods

Declaring procedures and customs duties

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

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

Non-tariff restrictions

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

Indirect taxation within the EEU

Exporting goods

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

Importing goods

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

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

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

Works and services

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

- works/services related to immovable or movable property are subject to VAT in the state where this property is located;
- services in the spheres of culture, art, education, physical training, tourism, recreation and sports are subject to VAT in the country where the respective recreational, tourist, sport, etc. facilities are located; and
- consulting, legal, accounting, auditor, designer, marketing, research and development and some other types of services are subject to VAT in the state, where the purchaser of these services is located.

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

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

"Ultimately, the EEU will result in the creation of a common market allowing free circulation of goods, services, capital and labour between its member states."

Banking sector

Banking industry

The Russian banking industry is characterised by a large number of credit institutions (974 as of 1 January 2017[1]) and by a high level of concentration of capital.

The number of credit institutions has reduced in the last year. This is due to the Central Bank of Russia (the "**CBR**") switching their focus to the consolidation of credit institutions and the closer supervision of their activities in the current economic climate. Consequently, a noticeable number of banking licences were revoked in the last 12 months.

As of 1 January 2017, 55.3% of the banking sector's total assets[2] were held by the top five Russian banks[3]. State-owned banks[4] continue to play a significant role in the stabilisation and development of the Russian banking sector.

[1] www.cbr.ru/statistics/print.aspx?file=bank_system/cr_inst_branch_010117.htm&pid=lic&sid=itm_3982

[2] www.cbr.ru/analytics/bank_system/obs_1701.pdf

[3] As of 1 January 2017, the top five Russian banks in terms of net assets are Sberbank (RUB 22.7tn, i.e. EUR 360.32bn); VTB (RUB 9.5tn, i.e. EUR 150.8bn); Gazprombank (RUB 5.2tn, i.e. EUR 82.54bn); VTB 24 (RUB 3.1tn, i.e. EUR 49.21bn); and FK Otkritie (RUB 2.8tn, i.e. EUR 44.44bn); www.banki.ru/banks/ratings/ (all conversions are based on a notional rate of RUB 63 = EUR 1, as used for convenience throughout this guide).

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

Legislative and regulatory framework

The legislative framework regulating the Russian banking sector is provided under Federal Law No. 395-1 "On Banks and Banking Activities" dated 2 December 2002 (the "**Banking Law**") and Federal Law No. 86-FZ "On the Central Bank of the Russian Federation" dated 10 July 2002 (the "**CBR Law**"). Bank bankruptcy is regulated by Federal Law No. 127-FZ "On Insolvency (Bankruptcy)" dated 26 October 2002, which now governs the relevant procedures instead of the special bankruptcy procedures that were previously in force in the banking sector. These laws and related regulations:

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

The CBR is legally and financially independent from the Russian Government. The CBR consists of a Moscow-based Head Office, which includes its Board of Directors, National Banking Council

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

Financial and banking legislation rarely stands still

So neither do we. Our banking and finance lawyers are on the ground to anticipate, interpret and advise on the local, cross-border and international laws shaping your markets. So whatever's ahead, we're already taking action.

and central administrative departments, a number of regional branches in the various regions of the Russian Federation (which are called "National Banks" in certain republics), and its local departments.

Under the CBR Law and the Banking Law, the CBR is responsible for regulating banking activities and is authorised to adopt mandatory regulations concerning banking and currency operations. The CBR actively uses its powers, and has created a detailed and extensive body of regulation on key areas, including: capital and net worth requirements – Directive No. 1260-U dated 24 March 2003 and Regulation 395-P of 28 December 2012; mandatory economic ratios and reserves – Instruction No. 139-I dated 3 December 2012 and Regulation 507-P dated 1 August 2015; currency control – Instruction No. 138-I dated 4 June 2012; and provision for losses – Regulation No. 254-P dated 26 March 2004.

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

Licensing and operations

Licensing

A credit institution must be licensed by the CBR in order to conduct "banking activities", as defined under the Banking Law. Credit institutions may be incorporated either as joint-stock or limited liability companies. The CBR may **deny the issuance** of a banking licence in the event of: (i) the non-compliance of application documents with Russian law requirements; (ii) the unsatisfactory financial standing of the founders; (iii) the non-compliance with the qualification requirements of the managers; or (iv) a member of the supervisory board (board of directors) of the proposed bank having an unsatisfactory business reputation. The CBR may **revoke** a banking licence, for example, in cases of capital inadequacy, breach of banking and other Russian law requirements (including breach of anti-money laundering regulations), for carrying out banking operations that are not authorised by the relevant banking licence, or the insolvency of a bank.

Acquisitions

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

Banking rules

According to the Banking Law, the CBR must:

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

Anti-monopoly rules

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

— more than 25%, more than 50% or more than 75% of the voting shares, or more than 1/3, more than 50% or more than 2/3 of participatory interests, in a credit institution, or more than 10% of the assets of a credit institution; and
— the target is a credit institution whose assets exceed RUB 31bn (EUR 492.1m).

Operations

Banks may carry a wide range of banking operations and provide various services. Non-banking credit institutions may only conduct a limited number of banking operations, such as maintaining accounts and processing payments on behalf of various entities.

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

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

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

Under the Banking Law, a credit institution cannot engage in manufacturing, commodities

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

trading (excluding precious metals[7]) or insurance activities. However, these restrictions do not extend to any cash-settled commodity derivative transactions.

Deposit insurance

To protect individual depositors, Federal Law No. 177-FZ "On Insurance of Deposits of Individuals in the Banks of the Russian Federation" dated 23 December 2003 (the "**Deposit Insurance Law**") came into effect at the end of December 2003. It stipulates that a bank may only attract deposits from or open accounts for individuals if the bank is a member of the deposit insurance system.

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

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

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

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

Member banks pay a contribution into a deposit insurance fund. These contributions are calculated as a percentage of the average daily balance of individual deposits maintained with a particular bank, subject to an established cap. All individual depositors with deposits in member banks are entitled to 100% compensation for aggregate amounts up to RUB 1.4m (EUR 22,222).

The anti-money laundering law

Federal Law No. 115-FZ "On Combating Money Laundering and the Financing of Terrorism" (the "**AML Law**") came into force on 1 February 2002, and has been revised a number of times to reflect

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

the global developments in this area. It is the primary legislative act in the Russian Federation aimed at preventing money laundering activities and the financing of terrorism, and is supported by numerous recommendations, binding instructions and regulations of the CBR and other authorities.

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

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

The Regulated Entities must identify and report transactions of a suspicious nature to the Federal Financial Monitoring Service, a designated monitoring authority. These transactions, among others, include cash or non-cash transactions of at least RUB 600,000 (EUR 9,524) and immovable property transactions of at least RUB 3m (EUR 47,620), or the equivalent of these amounts in foreign currency. If one of the parties to a transaction is suspected of being related to terrorist activity, the transaction is subject to mandatory control regardless of the amounts involved.

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

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

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

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

Bank secrecy

Similar to other jurisdictions, Russia has a set of rules for bank secrecy which are set out in the Banking Law. Accordingly, a Russian licensed bank may disclose information about any of its customers (including the relevant customer's operations) only to that customer, courts of general jurisdiction, commercial courts, certain governmental bodies and law enforcement agencies. In the event of unauthorised disclosure of any information so received, the respective authorities bear civil (compensation of damages), administrative and criminal liability under Russian law.

In practice, if a third party wishes to gain access to information in relation to the account balance of an account holder, the account holder must expressly authorise their account bank to release the relevant information. However, some banks take the more conservative view that such authorisation is not possible on the basis that it is not specifically provided for in the banking legislation.

Please note that Russian authorised banks are also subject to Russian data protection legislation (please see the *Personal data protection* chapter on page 155).

FATCA

Critical provisions of FATCA (i.e. the US Foreign Account Tax Compliance Act 2010, which came into force on 1 July 2014) apply extraterritorially and in order to counteract tax evasion require foreign financial institutions to report to the US Internal Revenue Service (the "**IRS**") information on their clients who have US tax residency status.

In the absence of an intergovernmental agreement on a FATCA compliance mechanism between the US and Russian Governments[8] and but for the adoption, on 28 June 2014, of the Federal Law No. 173-FZ[9] regulating how Russian financial institutions can report to foreign (in particular US) tax authorities, these institutions (or more specifically, their officials), would have faced administrative sanctions and criminal charges for breaching Russian bank secrecy legislation following any transfer of data to the IRS. This law was, to an extent, to the relief of Russian financial institutions, but also imposed certain new reporting obligations on their officials, including an obligation on them to disclose to the Russian tax authorities that a client is a foreign taxpayer.

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

[8] A FATCA compliance mechanism was discussed between the US and Russian Governments in early 2014. However, the negotiations of an intergovernmental agreement which would allow Russian financial institutions to comply with extraterritorial FATCA requirements have been suspended.

[9] "On the Peculiarities of Financial Transactions with Foreign Citizens and Legal Entities and Amendments to the Code on Administrative Offences".

Lending in Russia

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

Lending documents and governing law

Principles of contract law in Russia are generally flexible allowing parties freedom to negotiate the terms of credit agreements to suit their commercial needs and requirements. In addition, under Russian conflict of laws rules, the parties to a credit agreement may generally choose a relevant foreign law as the governing law of the agreement, provided it involves a foreign element. It is usual for cross-border credit agreements to be governed by the law of a foreign jurisdiction more commonly used in an international business setting, for example English law or the law of the lending entity.

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

A notable ongoing development, which started in 2015, is that a Russian law LMA style syndicated loan agreement was developed and presented by the Russian Banking Association. The loan agreement

follows the format and generally reflects the substance of the English law LMA loan agreement subject to modifications driven by the Russian law requirements. The respective loan agreement is designed to be used primarily in syndicated transactions between Russian residents. However, there are already examples of transactions within the CIS concluded on the basis of this document. In addition to the activity of the Russian Banking Association, some attempts to introduce a concept of the syndicated facility into the Russian legislative framework have been made by the legislator as well. Thus, currently there are some ongoing discussions on a new law that is supposed to regulate the market of syndicated loans.

Jurisdiction

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

There used to be a practice in Russia that a loan agreement governed by a foreign law would provide for a so-called "optional arbitration clause". Such clauses provide one party (usually the lender) with the exclusive right to bring a claim either in arbitration or in court, while the other party's (borrower's) right is limited to arbitration. According to a Ruling of the Supreme Commercial Court dated 19 June 2012, such an optional arbitration clause may be held invalid. Therefore, the current prevailing practice seems to be using international arbitration as the only option in foreign law governed loan agreements.

Currency control

As noted in the *Currency control* chapter on page 88, a "transaction passport" maintained with a Russian authorised bank is required for a foreign currency loan to be paid into Russian and foreign bank accounts of a resident from a non-resident.

For payments received by a Russian company for the export of goods, the exporter is required to repatriate 100% of the proceeds within the period specified in the export contract. In this respect, servicing debt offshore from export proceeds may become problematic under Russian law. At the same time, certain useful exemptions apply for loans of more than two years made by lenders situated in OECD or FATF countries.

Security interests

The choice of law for security documents usually depends on the location of the secured assets (e.g. intangible assets), or the governing law of the assets (e.g. contractual rights). In Russia,

the principal form of security is a pledge, which normally is entered into in connection with identified assets (subject to the discussion further below). In the case of competing pledges, the first in time by creation generally has priority. However, there is the possibility to change the priority of pledges by entering into an agreement between the pledgees or between the pledgees and the respective pledgor. Russian law explicitly allows one pledge to secure different obligations of a borrower owed to different pledgees (lenders). The pledgees in this situation will be ranked equally unless they agree otherwise. In relation to the pledge of movable property (including rights), the priority may depend on the registration date in the register of notices of pledge over movable property (the "**Movables Pledge Register**") as described below in more detail.

Under Russian law, a universal security instrument (such as an English law debenture), which might secure all assets of a company, has recently become available. However, it is virtually unregulated and it has not yet been tested in practice. Provided that under Russian law pledging immovable property and pledging participatory interest both require obligatory state registration, it is not clear how the new pledge of all assets will be implemented. There is also a security instrument called a mortgage of enterprise under Russian law, which may provide as security real estate, movable property, inventory, etc. However, because of practical difficulties in putting the security in place, it is rarely used in practice.

Pledges over particular types of assets (e.g. real estate, participatory interests and registered intellectual property rights) are recorded on specific public registers. The pledge of goods in circulation must be recorded in a "pledge book", which is maintained by the company (pledgor) and which the pledgee may inspect.

Since 1 July 2014, a pledgee and a pledgor may register a pledge of movable property in the Movables Pledge Register through a notary. Although registration is not obligatory for the parties, if they do so, they will be afforded with some benefits. The pledgee whose pledge is registered in the first place will enjoy enforcement priority rights. If a subsequent pledge is registered before the initial pledge, the subsequent pledgee will have the first ranking security of the pledged asset.

A pledgor needs to have title to the secured assets and although the pledge can be "possessory" or "non-possessory", the secured party need not take possession of the secured assets. A pledge needs to be in writing and needs to accurately identify the pledged assets, the secured obligations and their term.

The following points are worth noting, in relation to certain types of assets.

Shares or participatory interests

A pledge of shares held directly in a joint-stock company must be registered in the joint-stock company's register (which must be held by an independent licensed company). If shares in a joint-stock company are held by a depository, then its involvement

is required and the pledge is registered with the depository. In this case, the shares may not be disposed of without the pledgee's consent.

For participatory interests in limited liability companies, pledges must be notarised and registered in the public Unified State Register of Legal Entities. Since July 2014, the pledge of participatory interests becomes effective from the date of its registration on the above register.

Immovable property

Under Russian law, interests in land (e.g. freehold and leasehold interests) are considered "immovable property" and must be registered. Pledges (or "mortgages") over the interests must also be registered in the Unified State Register of Immovable Property. A mortgage does not come into effect until it is registered by the relevant land registration authority (please see the *Mortgage* section on page 125).

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

Contractual and intellectual property rights

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

Pledges over contractual rights may be registered in the Movables Pledge Register.

Bank accounts

A pledge of monetary funds kept on a bank account was not recognised by Russian law until July 2014. A practice developed of using account withdrawal (direct debit) agreements between a creditor, debtor and the bank of debtor's account. These agreements have a number of practical limitations, and it was preferable (if appropriate) to sweep funds to offshore accounts where security may be available.

As mentioned above, Russian law now allows for the pledge of funds credited to the pledgor's bank account. For these purposes a pledgor will have to open and maintain a specific "pledge bank account". Some banking regulations to this end are still not in place and are being developed by the Central Bank of Russia.

Security trusts and syndication

Under secured syndicated credit agreements, it is common for security to be held by a representative (i.e. a security agent or trustee) for a syndicate. The concept of security agent was alien to Russian law up until the adoption of amendments to Russian law as of 1 July 2014.

Because of the lack of recognition of the institution of a trust in Russia and the accessory nature of Russian security, syndicated loans have been commonly

structured to minimise disruption to Russian security upon changes to the syndicate.

The following arrangements have been commonly used:

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

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

The introduction of the concept of the security agent into Russian law in July 2014 could change local syndication practice, but this is likely to require clarifications from the courts and possibly the adoption of further legislation. Under the new provisions, a creditor or any third party may, under a pledge management agreement, act as a security agent in favour of all the creditors. The security agent will enter into pledge agreements on behalf of all the creditors. To enforce their security, creditors will have to act through the security agent; they may not do so individually.

Enforcement

Enforcement may be carried out through a court or an out-of-court procedure. The court enforcement procedure is usually carried out by way of a public auction. The parties to a pledge agreement may, however, indicate another enforcement procedure to be applied by a Russian court.

The out-of-court enforcement procedure includes (i) the possibility of a direct sale of the assets (except for immovable property); or (ii) a creditor appropriating title to the secured assets (whereas previously only proceeds were available).

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

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

Suretyships and guarantees

Russian law suretyships and guarantees are commonly used in connection with financings in Russia. Under Russian law, a "suretyship" refers to a particular type of instrument that a company (or individual) may issue as credit support for the obligations of another. A suretyship is "accessory" in its nature and does not survive the principal obligation.

In accordance with recent amendments to the Russian Civil Code, the concept of "bank guarantee" has been replaced by that of "independent guarantee". Since 1 June 2015, such a guarantee may now be issued not only by a lending institution (in which case it is still called a "bank guarantee"), but also by any other commercial organisation. An independent

guarantee constitutes an on-demand guarantee that is independent from the principal obligation. Russian law now also expressly provides that an independent guarantee may include a procedure for increase or reduction of the amount of the guarantee on a certain date or upon occurrence of certain events. However, the guarantor may not reduce the amount of the guarantee at its own discretion.

Bankruptcy considerations

Upon the bankruptcy of a debtor or a pledgor, a moratorium against enforcement of security will be introduced whilst it is being determined if financial rehabilitation, external administration or bankruptcy liquidation should apply. Repayments or arrangements in preference of other creditors are likely to be subject to anti-preference provisions set out in bankruptcy laws. For more information related to bankruptcy and insolvency in Russia generally, please see the *Corporate bankruptcy* chapter on page 90.

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

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

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

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

Other lending related issues

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

Pre-contractual negotiations

Since 1 June 2015, the Russian Civil Code establishes:

- a duty on those entering into contractual negotiations to act in good faith and not to enter into negotiations frivolously; and
- the notion of bad faith negotiations and defines the concept of bad faith as where one party to the negotiations provides the other party with incomplete information or conceals certain facts, or unexpectedly breaks off the negotiations without due cause.

If a party breaches the above requirements, it will have to reimburse the aggrieved party's losses, which are defined as the expenses incurred by the good faith party for the conduct of the negotiations and any expenses related to the lost opportunity to conclude a contract with a third party.

The new rules will clearly apply to negotiations carried out between Russian individuals and entities. We assume they would also apply to negotiations of agreements that shall mandatorily be governed by Russian law. Application of the new rules to cross-border negotiations is a more complex issue, which will remain uncertain until the relevant court practice has been formed.

To minimise the associated risks, the negotiating parties should establish the time when negotiations have formally started. This could be achieved by way of execution of a letter of intent (LoI) or any other document that could be used as evidence if a claim for reimbursement of expenses related to termination of negotiations (as described above) is filed.

In order to have an argument that Russian rules on pre-contractual negotiations do not apply to the parties and rules of a foreign jurisdiction apply, it is further advisable that the LoI or any document that evidences the commencement of negotiations contain applicable law provisions to avoid automatic application of the conflict of rules principle.

Corporate capacity and authority

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

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

In accordance with recent legislative amendments that came into force on 1 January 2017, "interested party transactions" (e.g. transactions that may involve affiliates or cross-management) do not require any corporate approval unless the management of the company

or a shareholder with no less than a 1%-stake requested such an approval. However, the company's charter may envisage different rules for corporate approvals of "interested party transactions".

Regulatory considerations on enforcement

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

— With regards to enforcement of the security, ownership of the Russian entity may be restricted as "strategic" under Federal Law No. 57-FZ "On the Procedure for Foreign Investments in Commercial Organisations of Strategic Importance for the National Security of the Russian Federation" dated 29 April 2008. For more details please see the *Common forms of business structures for foreign investors* chapter on page 31.

— Ownership may also need approval from the Federal Anti-monopoly Service under Federal Law No. 135-FZ "On Protection of Competition" dated 26 July 2006. For more details please see the *Anti-monopoly issues* chapter on page 37.

"Since 1 January 2017, the mandatory requirement that the "interested party transactions" must be approved by companies' management bodies no longer applies. Instead, the legislator has provided companies with a level of flexibility in terms of corporate approvals that can be supplemented in the companies' constitutional documents."

Currency control

General approach

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

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

Foreign currency transactions

Foreign currency transactions between residents

The following persons are considered to be "residents" for the purposes of the Currency Control Law:

— citizens of the Russian Federation, except for those who are (or are considered to be) living abroad for a period of at least one year;
— foreign nationals and stateless individuals who live permanently in Russia on the basis of a residence permit;

— legal entities duly registered under Russian law;
— branches and representative offices of Russian legal entities located outside the Russian Federation;
— diplomatic representatives, consular offices and other official representatives of the Russian Federation; and
— the Government of the Russian Federation, regions and municipal units of the Russian Federation.

Generally, foreign currency operations between residents are prohibited, although there are some exceptions. For example, residents may borrow from, and then repay to, Russian authorised banks[1] in a foreign currency. Contracts in Russia may be concluded with reference to foreign currencies. However, the actual payment must be made in roubles. This can lead to exchange rate differentials which may arise between the date the transaction is entered into and the payment date.

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

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

Foreign currency transactions between non-residents

The following persons are considered to be "non-residents" for the purposes of the Currency Control Law:

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

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

[1] Credit institutions holding a licence issued by the Central Bank of Russia for conducting operations in a foreign currency.

payments in Russian roubles within Russia are made to and from those non-residents' accounts opened with Russian authorised banks. Settlement under rouble transactions for sale of securities between non-residents is also permitted, although it can be subject to Russian securities market, anti-monopoly and other regulations.

Foreign currency transactions between residents and non-residents

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

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

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

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

Import and export of foreign currency in cash

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

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

Consequences of breach/ Penalties

Generally, as currency control agents, Russian authorised banks are under a duty to monitor compliance with currency control rules as far as transactions involving their accounts are concerned.

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

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

In addition, this Code prescribes fines for failing to:

- notify the tax authorities when opening or changing details of accounts held with banks located outside Russia;
- comply with the time periods and/or form of notification required when opening or changing details of accounts in banks located outside Russia;
- repatriate funds to accounts held in Russia in due time where required by law;
- comply with the requirement to ensure that a designated portion of export proceeds has been received by Russian companies in roubles[2]; and
- comply with rules for providing information or documents in relation to currency operations.

Breaches of these rules can result in penalties of up to RUB 20,000 (EUR 317[3]) for individuals, up to RUB 50,000 (EUR 794) for company officials, up to RUB 1m (EUR 15,875) for legal entities and, in certain cases, fines ranging from 75% to 100% of the value of the relevant transaction.

More serious criminal sanctions may apply under the Russian Criminal Code. In particular, it stipulates that persons failing to repatriate foreign currency over RUB 45m (EUR 714,285) to accounts in Russia, where required by law, may

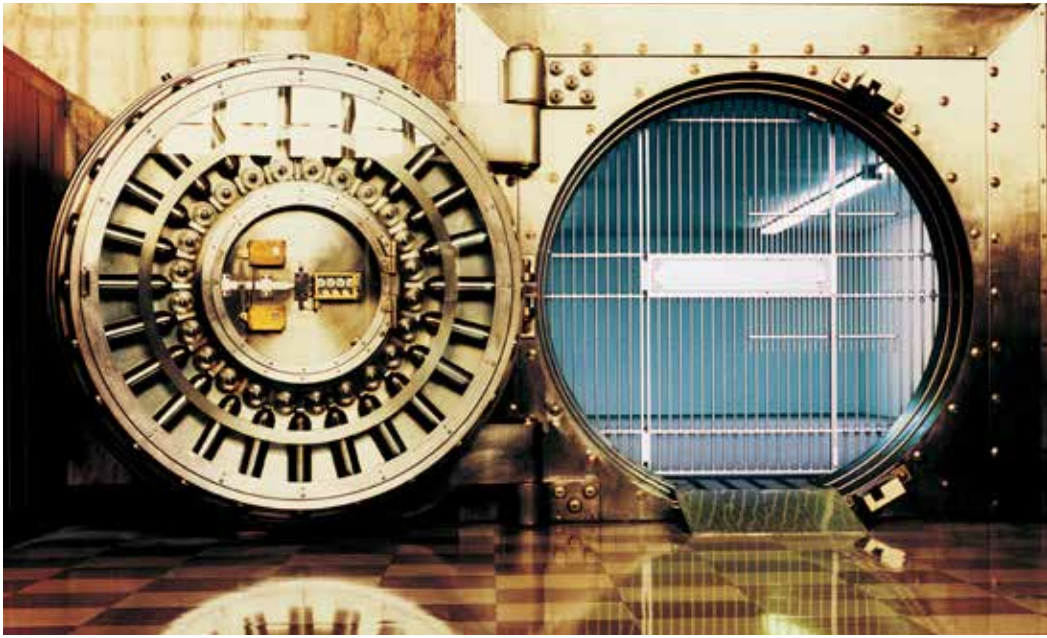
face imprisonment for a term of up to five years with a fine up to RUB 1m (EUR 15,875) or without it.

"Russian authorised banks are under a duty to monitor compliance with currency control rules as far as transactions involving their accounts are concerned."

[2] Currently – 0%.

[3] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

Corporate bankruptcy



General approach

The discussion in this chapter focuses on the Russian bankruptcy regime applicable to companies. The most important laws governing corporate bankruptcy proceedings are (i) Part I of the Russian Civil Code; and (ii) Federal Law No. 127-FZ "On Insolvency (Bankruptcy)" dated 26 October 2002, which is the principal piece of legislation on bankruptcy in Russia (the "**Insolvency Law**"). In addition, bankruptcy rules are set out in a number of regulations of the Government of the Russian Federation and other state bodies and are interpreted by the court practice, primarily in decisions and resolutions of the former Supreme Commercial Court and, currently, of the Supreme Court.

The Insolvency Law also includes bankruptcy regime applicable to credit institutions, which was previously regulated by a separate federal law. In addition, the new concept of personal bankruptcy (which falls outside the scope of this chapter) was introduced. At the moment, there is no information on whether the Russian legislative bodies or the Government are intending to prepare any further significant amendments to the Russian bankruptcy legislation.

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

Insolvency criteria

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

Stages of bankruptcy proceedings

Depending on the circumstances, the insolvent company may be subject to five different stages of bankruptcy proceedings:

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

Preliminary step: initiating bankruptcy proceedings

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

The following are permitted to file a bankruptcy petition with a commercial court to have a debtor declared bankrupt:

— the debtor itself;
— a bankruptcy creditor;
— the Federal Tax Service of the Russian Federation (the "**FTS**"); or
— a current or former employee of the debtor.

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

— if the claims of one or more creditors are fulfilled, the debtor will be unable to fulfil its payment obligations towards other creditors;
— persons who are authorised to take a decision to apply for liquidation on behalf of the debtor decide to petition the court for the commencement of bankruptcy proceedings;
— if claims against the debtor's assets are enforced, the debtor will be unable to continue, or will be significantly restricted in continuing, its operations;
— the debtor meets the "inability to pay" criterion (i.e. the debtor fails to perform its payment obligations when due as a result of insufficient funds);
— the debtor meets the "insufficient assets" criterion (the value of the debtor's payment obligations exceed the value of its assets); and/or
— as a result of insufficient funds, the debtor is unable to pay wages and other payments due and payable to its current or former employees pursuant to the Russian labour laws that are outstanding for more than three months.

A bankruptcy creditor or the FTS may file a bankruptcy petition with a commercial court to initiate bankruptcy proceedings if:

— an unsatisfied aggregate debt of a corporate debtor exceeds RUB 300,000 (EUR 4,762[1]), which

[1] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

is confirmed by an enforceable court decision or arbitral award (Russian or foreign); and
— one of the above insolvency criteria is met (i.e. there is evidence that the debtor is insolvent).

In accordance with the Insolvency Law, when a creditor is a credit institution, it is entitled to initiate bankruptcy proceedings with respect to its debtor immediately after the latter has met an insolvency criterion under the Insolvency Law. Credit institutions, unlike other creditors, do not require a court decision or arbitral award in order to ascertain their claims. However, in order to exercise this right, a credit institution has to publish a notice of its intention to file an insolvency petition against the relevant debtor in the Unified Federal Register of Legal Entities Notices (available at www.fedresurs.ru) at least 15 days before filing the relevant petition with the court (a similar publication requirement is now applicable to the debtor intending to file for its own bankruptcy).

Initiation of bankruptcy proceedings is not automatic and the applicant, being a creditor (except when it is a credit institution) or a debtor itself, must prove to the court that the debtor is insolvent.

A current or former employee of the debtor is entitled to file a petition for the initiation of bankruptcy proceedings if the employee has any severance or salary payment claims against the debtor.

Supervision

Supervision is a provisional stage of bankruptcy proceedings. Once supervision is introduced (automatically when the first bankruptcy petition is accepted by a court) a temporary manager is appointed to oversee the activities of the debtor. Such manager supervises the management bodies of the debtor, which remain in place. Supervision aims to (i) preserve the debtor's property; (ii) analyse its financial state; (iii) complete a creditors' register; and (iv) hold the first creditors' meeting.

When the court accepts the bankruptcy petition, it may also impose interim measures (e.g. an arrest (a freezing order)). The court's ruling applies immediately. However, even though the ruling may be appealed, the appeal process will not suspend the execution of the court's ruling.

Restrictions

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

— Creditors' claims against the debtor and its assets are to be submitted only through the commercial court supervising the bankruptcy proceedings. That court decides on their inclusion in the creditors' register maintained by the temporary manager (including the amount of the claim).
— The debtor is prohibited from paying out profits and dividends, as well as effecting set-offs that violate the order of priorities established by the Insolvency Law (subject to certain carve-outs relating to liquidation (close-out) netting as provided below). The debtor may not alienate or purchase shares, issue securities (excluding shares),

reorganise its company structure or incorporate subsidiaries.

— Any property transactions with a value exceeding 5% of the debtor's balance sheet value and any credit-related transactions are only permissible with the prior written consent of the temporary manager.

The debtor is entitled to increase its registered capital through a private placement of additional ordinary shares. It is not permissible to increase a company's registered capital in order to cover losses. However, a debt-to-equity conversion is now permitted. If the debtor's shareholders or third parties repay the full amount of creditors' claims according to the creditors' register, the bankruptcy proceedings will be terminated.

Temporary manager

The temporary manager is nominated from members of a self-regulated organisation of insolvency practitioners. The party filing a bankruptcy petition must propose a self-regulated organisation or nominate an individual from that organisation. Where the party filing the bankruptcy petition fails to suggest an individual, the temporary manager is nominated by the self-regulated organisation of insolvency practitioners. In both circumstances, the appointment is subject to the court's approval.

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

Termination of supervision

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

Financial rehabilitation

This procedure is aimed at restoring the debtor's solvency and rescheduling (re)payment of the outstanding debts. Financial rehabilitation may last up to two years and commences immediately upon a court's ruling.

Financial rehabilitation proposal

A debtor or creditors (both corporate and state) can propose financial rehabilitation at the first creditors' meeting. The details of the proposal depend on the party applying, but

it would include at least: a financial rehabilitation plan, a debt repayment schedule, information on the security offered for performance of the debtor's obligations under the debt repayment schedule and, in the case of a debtor's proposal, minutes from the general meeting of shareholders/participants authorising the decision.

Administrative manager

When the court initiates financial rehabilitation on the basis of a decision of a creditors' meeting, an administrative manager will also be appointed by the court. The role of the administrative manager predominantly involves monitoring the existing management bodies of the debtor, which remain in place. His/her key duties include: (i) maintaining a register of creditors' claims; (ii) examining reports on the progress of the financial rehabilitation plan; (iii) monitoring the debtor's discharge of current claims; and (iv) enforcing security provided to the debtor.

The powers of the administrative manager are, in broad terms, similar to those of the temporary manager.

Restrictions

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

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

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

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

External management

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

External manager

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

Amongst other actions, the external manager is entitled to:

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

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

Restrictions

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

A wide-ranging moratorium is imposed upon satisfaction of creditors' claims (excluding current payments (e.g. judicial expenses and payment of salaries)).

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

Termination

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

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

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

The court will evaluate the external manager's report and is entitled to approve or reject it. The court should approve the external manager's report if (i) all registered creditors' claims have been satisfied; or (ii) the creditors' meeting has decided to terminate the external management on the ground that the debtor's solvency had been restored and to proceed with paying out the creditors' claims;

or (iii) the creditors and the debtor have consented to a voluntary arrangement; or (iv) the creditors' meeting has extended the term of the external management. The court should reject the external manager's report if (i) the registered creditors' claims have not been satisfied; or (ii) there are no grounds for restoring the debtor's solvency; or (iii) there are some circumstances that prevent a voluntary arrangement. If (i) the creditors have petitioned the court to have the debtor being declared bankrupt; or (ii) the court has rejected the external manager's report; or (iii) such a report has not been presented to the court in due course, then the court may declare the debtor bankrupt and introduce the bankruptcy liquidation.

Bankruptcy liquidation

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

Consequences

The immediate effects of the bankruptcy liquidation include the following:

- Monetary obligations and mandatory payments of the debtor are accelerated by virtue of statute.
- Interest no longer accrues. The same applies to financial (or other) sanctions arising from a failure to fulfil monetary obligations and mandatory payments (other than current payments).
- Information on the debtor's financial state is no longer deemed to be confidential.
- Existing encumbrances over the debtor's property are removed and no further encumbrances are allowed.
- The powers of the debtor's general director and board of directors are terminated and vested with the bankruptcy manager.

Bankruptcy manager

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

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

Bankruptcy liquidation: order of priorities

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

Creditor claims made after the court's acceptance of the bankruptcy petition (so-called "current claims") are not included in the order of priorities as such and should be satisfied when they become due.

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

First priority claims include personal injury claims and moral damage claims. **Second priority claims** include: (i) severance benefits; (ii) the wages of the debtor's employees; and (iii) copyright royalties. **Third priority claims** include all other claims (both secured and unsecured, where secured claims mean claims secured by a pledge or a mortgage).

Notwithstanding that the claims of secured creditors are accounted for in the third priority, they are satisfied in accordance with a special procedure largely separate from that applying to the unsecured creditors, i.e. the proceeds from the sale of the pledged property (capped to the principal amount and any accrued interest) are allocated as follows among secured creditors:

— for claims under a secured credit agreement, the lenders are entitled to 80% of the realised proceeds, with the remaining 15% for the first and second priority claims, and 5% for insolvency expenses;
— for other secured claims (other than under a secured credit agreement) the respective thresholds are 70%, 20% and 10% respectively.

The Insolvency Law has been amended to ensure that pledges over bank accounts, a new type of pledge provided in the Civil Code, remain enforceable during bankruptcy.

Possible transition to external management

Where the financial rehabilitation or external management stages have not previously been instituted, the creditors' meeting may petition the court for a transition to the external management stage during the bankruptcy liquidation stage. To do so, grounds must exist to believe that the debtor's solvency can be restored, and these must be backed by financial data. The transition will only be permitted if the debtor has sufficient assets to pursue independent economic activity.

Liquidation (close-out) netting

Obligations under qualifying financial agreements that are concluded on the basis of master agreements (derivative or repo), stock exchange trading rules or clearing rules are terminated in accordance with the terms of these agreements, stock exchange trading rules or clearing rules. This leads to the determination of a close-out amount which is calculated in accordance with the terms of the relevant master agreement, stock exchange trading rules or clearing rules, and whose calculation can be made using close-out netting.

The Insolvency Law stipulates additional requirements for an agreement to be qualified as a master agreement. These criteria apply to domestic and cross-border transactions and agreements.

The above rules are applicable to financial agreements concluded prior to temporary administration or prior

to the implementation of one of the stages of bankruptcy proceedings. Temporary administration only applies to credit and other financial institutions (as defined in the Insolvency Law). This is a temporary governing body that is appointed by the supervisory body of the relevant credit institution in order to restore its solvency, preserve its assets and retain its licence, which is a mandatory requirement for credit institutions to operate in Russia.

Voluntary arrangement

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

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

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

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

"The Insolvency Law was significantly amended in 2015. The bankruptcy regime applicable to credit institutions which was previously regulated by a separate federal law, is now part of the general insolvency regulation, with certain specifics."

Employment/Migration

General approach

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

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

Formalising the employment relationship

Employment agreement

Under the Labour Code employment agreements must be concluded in writing (except for teleworkers with whom it is possible to conclude the agreement electronically, i.e. using electronic digital signatures) and contain certain mandatory terms and conditions. Such mandatory terms include place of work, job position, job duties, commencement date, term of employment, remuneration, working time regime, etc. Employment agreements may contain additional terms and conditions, such as probationary period and confidentiality clauses.

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

Term of employment

Employment agreements may be concluded for an indefinite term or for a fixed term; a fixed-term employment agreement may be concluded for a period of not more than five years.

The law provides for only a limited number of grounds when an employment agreement may be concluded for a fixed term. These include, in particular, the following (the list is not exhaustive):

- an employee replacing a temporarily absent employee;
- project-related or seasonal employees;
- general directors, deputy general directors or chief accountants;
- employees of companies created for a specific term and purpose;
- employees engaged under the terms of secondary employment.

To keep your people happy, keep ours on-hand

Our lawyers will help you navigate the maze of employer regulation and policy. Because we understand that taking care of business starts with taking care of people.

If a fixed-term employment agreement is concluded in breach of the Labour Code, the competent state authorities may recognise it as concluded for an indefinite term.

Salary

The statutory minimum gross monthly salary is set at RUB 7,800 (EUR 125[1]) for the whole of Russia. At a regional level, a higher minimum monthly salary may be approved. For example, as of 1 October 2016, the minimum monthly salary in Moscow was set at RUB 17,561 (EUR 280).

Salary is to be determined in the employment agreements and paid in roubles in instalments at least twice a month.

Probationary period

An employment agreement may provide for a probationary period which must not exceed three months. For general directors, deputy directors, chief accountants, deputy chief accountants and directors of representative offices, branches or other divisions, a longer probationary period may be established. This longer period must not exceed six months.

Both employers and employees are required to give the other party three days' written notice when terminating the employment agreement during the probationary period. When dismissing an employee for failure to pass the probationary period, employers have an obligation to provide the employee with reasons for dismissal in writing. The employee may appeal the employer's decision in court.

The following employees cannot be subjected to a probationary period:

- pregnant women and women with children under the age of 18 months;
- under-18s;
- young persons graduating from state-accredited educational institutions of primary, secondary or higher professional education, upon completing their education and applying for their first job within one year of graduation;
- certain other categories of employees as set forth in the Labour Code.

Working hours and leave

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

An open-ended working day regime may be established for certain categories of employees, if set out in the employer's internal regulations and relevant employment agreements. This type of working day regime entails the employee being periodically engaged in additional work upon the written request of the employer without requiring the employee's written consent. Under this regime, the overtime work does not result

[1] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

in additional remuneration but does provide the employee with at least three additional days of leave per year.

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

Confidentiality obligation imposed on the employee

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

Restrictive covenants

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

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

Liability

Liability of the employee

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

The Labour Code strictly regulates the **disciplinary procedure**, and non-compliance may result in the employee successfully challenging the disciplinary sanction in court.

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

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

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

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

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

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

Liability of the employer

The limitation period within which an administrative claim can be brought against an employer for failure to comply with labour laws is one year from the date that the violation was committed or, with respect to ongoing violations, from the date that the violation was discovered by the authorities. The maximum administrative fine that may be imposed on an employer's official for non-compliance with labour law requirements has been increased to RUB 20,000 (EUR 317). Furthermore, in the event of a recurring offence, the official may be disqualified for a term of up to three years. The maximum administrative sanctions that may be imposed on legal entities include an administrative fine of RUB 200,000 (EUR 3,175) and/or administrative suspension of activities up to 90 days.

Notably, in accordance with the current law-enforcement and court practice, the penalty for the same offence may be imposed simultaneously on both the company and the general director or other authorised officer of the company. Moreover, if the same offence is simultaneously committed against a number of employees, the total amount of administrative fine

imposed on the official or the entity for such offences may in some cases be calculated taking into account the total number of employees affected by the relevant offence.

Labour book

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

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

Specifics of hiring foreign nationals

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

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

Managing employment relationships

Internal policies

All employers in Russia (except for those that are qualified as "microenterprises") must adopt a set of mandatory internal policies that include Internal Labour Regulations, a Labour Safety Policy, Personal Data Protection Policies, Remuneration Policy and an Anti-corruption Policy. These policies must be in Russian or at least in a bilingual format, approved by the order of an authorised representative of the employer and brought to the notice of employees.

The same requirements apply to any global policies that the employer would like to be binding upon the employees in Russia.

Health and safety at work

Workplaces of all employees in Russia must be assessed from a work safety perspective. The workplace assessment is not required for homeworkers, teleworkers and employees working for individuals who are not registered individual entrepreneurs.

The main purpose of the work safety assessment remains the same as under previous rules, namely to provide employees with relevant guarantees and compensation, and to set additional pension and social insurance rates. These rates depend on workplace hazards, which are rated as either optimal, acceptable, harmful or dangerous.

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

Sick leave

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

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

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

Maternity and child care leaves

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

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

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

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

Trade unions

A trade union aims to represent employees and protect their social and labour rights and may be established in any company by at least three employees.

In the situations specified by the Labour Code (such as, for example, staff redundancy or termination of an employment agreement with

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

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

Disciplinary sanctions

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

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

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

Terminating an employment agreement

Cases and grounds for termination

An employment agreement may be terminated (the list is not exhaustive):

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

The employer may terminate the employment agreement only on the limited number of grounds expressly set out in the Labour Code, such as (the list is not exhaustive):

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

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

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

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

Specifics of employing foreign nationals

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

One of the recent positive developments is the extension of the highly qualified specialist regime to accredited representative offices of foreign companies in Russia since 1 January 2015.

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

Visas for foreign employees

Foreign nationals must apply for a visa. Citizens from the following countries of the Commonwealth of Independent States are exempt from Russian visa requirements: Armenia, Azerbaijan, Belarus, Kazakhstan, Kyrgyzstan, Moldova, Tajikistan, Ukraine and Uzbekistan.

Types of visas

There are five categories of visas: ordinary, official, transit, diplomatic and temporary

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

Business visas

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

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

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

Work visas

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

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

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

The employer must be registered with the Main Department for Immigration Issues of the Ministry of Internal Affairs of the Russian Federation (the "**Immigration Department**") to be permitted to issue invitations to foreign employees.

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

Procedures relevant to an employer

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

Quotas

All legal entities wishing to employ foreign nationals must apply by 1 July each year for a quota of foreign employees whom they

may employ. Certain professions and some categories of foreign employees (e.g. highly qualified specialists, foreign nationals who are exempt from the requirement to hold a work permit) are quota-exempt.

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

General authorisation for the recruitment of foreign nationals

The general rule is that any employer intending to recruit one or more foreign nationals must obtain a prior general authorisation from the Immigration Department to recruit foreign employees within its allocated quota. By way of exception, no such authorisation is required for highly qualified specialists and for foreigners from CIS countries.

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

Individual work permits

General remarks

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

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

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

— citizens of countries which are members of Eurasian Economic Union (currently Armenia, Belarus, Kazakhstan and Kyrgyzstan have joined the Union with Russia); and
— those holding a permanent residence permit or a temporary residence permit.

These categories of permit-exempt foreign citizens are not taken into account in their employers' quotas and general authorisations to recruit foreign employees.

Employers are obliged to notify the Immigration Department on conclusion and termination of employment and civil law contracts with all categories of foreign citizens within three working days following the date of conclusion or termination of the contract.

Language command requirements

From 1 January 2015, applications for work permits for non-visa foreigners need to include a dedicated certificate proving their command of the Russian language, Russian history and fundamentals of Russian law (the "**Russian Language and Civilisation**"), unless they hold a relevant Soviet or Russian certificate of education.

Distinct rules apply to foreigners subject to a visa regime. They are given more time to prove they meet the Russian Language and Civilisation requirements. Proof must be submitted to the authorities within 30 days from the issuance of the relevant

permit (rather than upon application). If they fail to do so, their permits will be cancelled.

All foreigners who obtained their residence or work permits before 1 January 2015 are only required to prove they meet the Russian Language and Civilisation requirements when applying to renew these permits.

Certain categories of foreigners are exempt from the Russian Language and Civilisation requirements, such as highly qualified specialists and their relatives, and full-time foreign students with accredited educational institutions in Russia.

Personal accreditation of foreign employees of representative offices and branches

If the employer is a representative office or branch of a foreign company in Russia, it must apply for approval for the relevant number of foreign employees from the Chamber of Commerce and Industry as part of the accreditation process for the representative office or branch. Within that approved number, the employer must apply to the Chamber of Commerce and Industry for a personal accreditation card for each foreign employee.

Personal accreditation does not relieve the employer from having to obtain a general authorisation for the recruitment of foreign nationals, a work permit and a work visa for its foreign employees.

Notification

There is a notification procedure which foreign nationals and their employers must follow. This procedure also applies to highly qualified specialists.

It is based on the following principles:

- The Immigration Department must be notified of arrivals and of any travel within Russia.
- A highly qualified specialist and the members of his/her family are allowed a period of 90 days from the date of entry into Russia, during which they are not required to register with the migration authorities. Once the foreign specialist has been in Russia for 90 days, he/she must be registered at his/her place of residence.
- Armenian, Belarusian, Kazakh and Kyrgyz employees and the members of their family have to register within 30 days.
- For all other foreign nationals, the registration procedure with the Immigration Department must be completed within seven working days.
- Foreign nationals staying in Russia or travelling to another Russian region for less than seven working days, who are not staying in a hotel or in "a hotel-like residence", are exempt from the notification procedure.
- Heads of State, heads of diplomatic missions, members of parliamentary or governmental delegations, heads of international organisations (and family members of these persons) are exempt from the notification procedure. Ship, train or aircraft crew members are exempt from the procedure under certain conditions.

Business trips within Russia

A foreign employee is permitted to go on business trips outside the Russian region(s) in which his/her work permit is valid only if he/she occupies a position which is included in the list of occupations approved by the Ministry of Health and Social Development.

In addition, the duration of foreign employees' business trips is regulated as follows:

— a total of ten days during the validity of a general work permit; and
— 30 consecutive days during the validity of a highly qualified specialist work permit.

Different rules apply to foreign nationals who hold temporary or permanent residence permits.

The duration of business trips of highly qualified specialists having a travelling character of work regime fixed in their employment agreements is not limited.

Highly qualified specialists

Highly qualified specialists are foreign employees with professional skills, knowledge and the proper qualifications in a specific area to which a specific regime applies.

The monthly remuneration paid to a highly qualified specialist must be at least RUB 167,000 gross (EUR 2,650), unless a lower amount is set by law or in international agreements for certain nationals.

The highly qualified specialist regime is available to Russian commercial legal entities as well as to Russian based duly accredited branches and representative offices of foreign legal entities.

When the above criteria are met, a simplified procedure applies for obtaining a highly qualified specialist work permit and work visa. Accordingly, a work permit may be obtained within 14 working days and the employer is exempt from fulfilling a significant number of formalities (obtaining a quota, general authorisation to recruit foreign employees, etc.).

In addition, opting for a highly qualified specialist regime provides employers and highly qualified specialist with increased flexibility, such as:

— A work permit is valid for up to three years, whereas an ordinary one is valid for only one year.
— A work permit is valid for multiple Russian regions rather than just the region where the employer is based.
— There are fewer restrictions on business trips (as mentioned above).

Bilateral and multilateral international agreements

There are several international agreements regulating foreign workforce issues. They affect in particular French, South Korean, Armenian, Belarusian, Kazakh and Kyrgyz citizens.

Arrangements applying to French employees in Russia

On 1 March 2011, the Agreement "On the Temporary Employment of Citizens of One Country on the Territory of the Other", as signed on 27 November 2009 between the Russian Federation and France, came into force.

Special filing procedures and review processes for obtaining authorising documents for employment have been established, with the goal of simplifying the temporary employment of the citizens of the two signatory countries.
In particular, documents allowing French citizens to enter and work in the Russian Federation have to be processed within one month.

Arrangements applying to Korean employees in Russia

An Agreement has been in force since 1 January 2012 between the Governments of the Russian Federation and the Republic of Korea (South Korea) on the temporary work activity of their respective citizens.

This Agreement simplifies the rules and procedures applicable to the stay and employment of (i) Korean employees of representative offices of legal entities in Russia; (ii) Korean employees working at or for Russian organisations belonging to a Korean group of companies; (iii) Korean top executives managing Russian enterprises; and (iv) some family members.

In particular, quotas limiting work activities do not apply to these persons.

Arrangements applying to Armenian, Belarusian, Kazakh and Kyrgyz employees in Russia

In accordance with the Agreement on the Eurasian Economic Union (the "**EEU**") signed in Astana on 29 May 2014, simplified rules of employment of foreign nationals apply to citizens of countries which are EEU member states. As commented above, currently, Armenia, Belarus, Kazakhstan and Kyrgyzstan have joined the EEU.

The Agreement introduces reciprocal preferences, thereby simplifying significantly the conditions of stay and employment of the countries' respective nationals.

Quota, general recruitment authorisation and work permit requirements do not apply to EEU employees in Russia. These migrant employees and family members are allowed to stay in Russia for the duration of a migrant employee's employment agreement (rather than the one year maximum previously applicable). The timeframe for notification of entering Russia is 30 days from the entry date (rather than seven working days).

Sanctions for violating migration legislation

If an employer fails to comply fully or in part with the relevant migration procedures, it risks a fine (calculated per breach) of up to RUB 800,000 (EUR 12,700) and/or the suspension of its activities for up to 90 days. The employer's officials may be liable to fines of up to RUB 50,000 (EUR 794). A foreign employee may also be fined up to RUB 5,000 (EUR 79), and may be deported from or banned from entering Russia. An entry ban can

be imposed on a foreign citizen who has been held administratively liable two or more times, including for violations of legislation other than in the field of migration (such as, for instance, road traffic regulations). Foreign citizens are therefore strongly advised to be as compliant as possible in view of the continuing trend of strict enforcement of entry bans.

Stricter sanctions apply to the violation of migration law requirements in Moscow, Saint Petersburg, the Moscow Region and the Leningrad Region, namely: individuals will pay fines of RUB 5,000-7,000 (EUR 79-110) and may be deported from Russia, officials – RUB 50,000-75,000 (EUR 794-1,190) and companies – RUB 800,000-1m (EUR 12,700-15,875) and/or have their operations suspended for 14 to 90 days.

"In accordance with current law-enforcement and court practice, both the company and the company's general director or other authorised officer may be held liable for the same violation of labour laws, work safety and/or migration law requirements."

Wherever you want to build, we've got the legal foundations in place

Drawing on decades of deals in real estate and construction, our team works to the same high standards in every market. So irrespective of where your real estate assets are, we can deploy specialist teams to advise you immediately.

Real estate and construction

General approach

This section relates to real estate and construction matters in Russia, which are governed by a complex body of laws and regulations. Key legislation in this respect includes:

- the Civil Code of the Russian Federation: Part I dated 30 November 1994; Part II dated 26 January 1996; Part III dated 26 November 2001 and Part IV dated 18 December 2006 (the "**Civil Code**");
- the Land Code dated 25 October 2001 (the "**Land Code**");
- the Town Planning Code dated 29 December 2004 (the "**Town Planning Code**");
- the Forest Code dated 4 December 2006;
- the Water Code dated 3 June 2006;
- Federal Law No. 102-FZ "On Mortgage (Pledge of Immovable Property)" dated 16 July 1998 (the "**Law on Mortgage**"); and
- Federal Law No. 218-FZ "On State Registration of Immovable Property" dated 13 July 2015 (the "**Law on State Registration**").

In 2015, new amendments into the Civil Code came into force. They mostly concern transactions in general; however, transactions involving real estate have been affected as well. In March 2015, major amendments to the Land Code regarding the formation and allocation of plots of publicly-owned land came into force (the "**Land Code Amendments**").

In July 2015, the Law on State Registration, which provides significant changes to the procedure for the state registration of rights and transactions with immovable property, was adopted. Starting from January 2017, the Law on State Registration replaced previously effective Federal Law No. 122-FZ "On State Registration of Rights to Immovable Property and Transactions" dated 21 July 1997.

Rights to real estate

Russian law provides for two basic types of rights to immovable property:

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

Public and private ownership rights

Real estate (including land plots) in the Russian Federation may be owned publicly or privately. In relation to land, we would like to outline a number of local specificities.

Public land ownership

Publicly-owned land means that the land is owned by the State (i.e. the Russian Federation or a region) or a municipality. Substantial areas of land in Russia (particularly in the City of Moscow, which has regional rather than municipal status) have always been state-owned.

Until 2001 (when the Land Code was adopted), the delineation of state-owned and municipal land plots was regulated by several legal acts. The process of delineation was complicated and, at times, confusing. It has been clarified by the Land Code. The Land Code Amendments prescribe the procedure of delineation in more details.

Public land plots may be privatised, subject to a number of statutory restrictions. For example, land plots falling within specially protected areas (such as national parks) or areas required for defence (such as military airports) may only be state-owned.

Private land ownership

Any legal entity or individual may own private land in the Russian Federation, subject to certain restrictions which regulate the legal status of the land plot.

Generally speaking, foreign nationals and legal entities enjoy the same rights to land plots as Russian individuals and legal entities. However, in respect of the ownership of land, foreign investors may not:

— own land in certain border territories or other territories specifically designated in the Land Code or federal laws (such as, for instance, land located within the boundaries of sea ports); or
— own agricultural land. This rule also applies to Russian companies with a foreign participation of more than 50% in their charter capital. Foreign investors (as widely defined above) may only lease agricultural land, which will complicate their Greenfield projects on this type of land.

Other rights to or affecting land plots

Russian land legislation also provides for other types of land rights, such as (among others) the right of permanent perpetual use of the land plot and the right of inheritable use. However, the use of such rights has no practical application for foreign investors. Legal entities were required to convert any pre-existing rights of permanent perpetual use into leasehold or freehold rights by 1 July 2012. Those who failed to do so may be held administratively liable and have to pay an administrative fine of RUB 20,000-100,000 (EUR 317-1,587[1]).

As in other countries, an easement (or servitude) may be established over a land plot which is owned by a third party. This grants the land user a variety of rights (including the right to build linear facilities such as cable lines and pole lines). The easement may be public or private and the distinction depends on the persons who are interested in it. If the easement is required by a particular person or legal entity, then only a private easement may be established in respect of the relevant land; if the general public is interested in the easement, then a public easement may be established.

Under Russian law it is possible to enter into an easement agreement with not only the owner of the land, but also with its legal holder (a tenant, a land user enjoying the right of free use, etc.).

[1] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

Real estate transactions

Sale and purchase transaction

Cadastral and state registration

A publicly- or privately-owned land plot may be bought and sold provided that (i) it has undergone all cadastral registration formalities; and (ii) the title to the land plot has undergone state registration. Failure to comply with these requirements may lead to any real estate transaction connected with the land plot being declared null and void.

There are some cases when the state registration of title to the land plot can be performed simultaneously with its cadastral registration (e.g. formation of a new land plot, provided certain conditions are met).

Both procedures require the submission of certain documents to the state registration authority (i.e. the Federal Service for State Registration, Cadastre and Cartography) or its regional/local departments ("*Rosreestr*") (the "**Registrar**"). The Law on State Registration now allows submitting documents to the Registrar in any region of the Russian Federation regardless of the immovable property's location.

Until recently, there were two main information resources for cadastral registration and state registration of rights to immovable property, namely the State Cadastre of Immovable Property and the Unified State Register of Rights to and Transactions with Immovable Property. In practice this often resulted in the duplication and inconsistency of records made in these two interrelated and independent systems. However, starting from 1 January 2017, these two systems were merged into a new information resource, i.e. the Unified State Register of Immovable Property (the "**State Register**") maintained by the Registrar in electronic form.

The State Register contains the information on both immovable property and the rights thereto. In particular, it includes: (i) a register of immovable property; (ii) a register of rights to, liens on and encumbrances over immovable property; (iii) a register of boundaries (e.g. the boundaries of the regions of the Russian Federation and municipalities, boundaries of use-restricted zones, territorial zones and other special territories); and (iv) registration files, cadastral maps and document journals.

Rights to buildings and structures in Russia are not effective until they are registered in the State Register. Such state registration (as evidenced by an extract from the State Register) is the only confirmation of the existence of the ownership right. Only a court decision may overrule state registration.

Since 15 July 2016, ownership certificates, which were previously the main confirmation of state registration of the ownership right to immovable property, are no longer issued and fully replaced by extracts from the State Register. From 1 January 2017, cadastral extracts also no longer exist. Starting from this date, both state cadastral registration and state registration of rights to immovable property are evidenced by an extract from the State Register.

Buildings on land plots

The Land Code prohibits the transfer of land without the buildings and structures standing on it. Ownership rights to a building may only be transferred together with the rights to the land plot beneath this building. In exceptional cases, title to parts of a building may be transferred separately from the land if it is impossible to separate the respective part of the land plot, or if there is a restriction on the acquisition of this land plot.

Owners of buildings located on a land plot other than their own generally enjoy a pre-emptive right to purchase the land plot, or a preferential right to lease it. If a land plot is under state or municipal ownership, the owners of buildings generally have exclusive rights to privatise the land plot.

Privatisation

Since 30 October 2001, it has no longer been possible to privatise buildings, structures or industrial facilities without simultaneously privatising the underlying land.

A building owner has pre-emptive rights to obtain freehold or leasehold rights to a publicly-owned land plot on which the owner's building stands.

In case of freehold, the buyout price is determined by the federal, region or municipal authorities. In any event, the price of such land plot must not exceed its cadastral value or any other price if so established by a federal law (except for cases when the land plot is to be sold through an auction).

Sale and purchase contract

General

Certain conditions of a real estate sale-purchase transaction are deemed material and must be clearly determined in the sale and purchase agreement, such as the subject matter (i.e. the land plot or building/structure/premises) and the price. In addition, the parties to the agreement are entitled to set out their own list of supplemental contractual provisions that they consider to be material to the transaction. Pursuant to the Law on State Registration, such material contractual conditions must now be recorded and reflected in the State Register.

If the sale and purchase agreement does not fulfil the above requirements, it is deemed not to have been concluded. This means that (i) the purchaser does not acquire the ownership right to the land plot or real estate; and (ii) the land plot or real estate must be vacated and returned to its owner in its original state and the sale price returned to the purchaser. These consequences arise only if a competent court declares the sale and purchase agreement as not having been concluded.

Purchase of future property

As a result of the adoption of Ruling No. 54 dated 11 July 2011 by the Plenum of the Supreme Commercial Court of the Russian Federation, sale and purchase agreements in relation to future property are considered valid, but the buyer's title to the property only arises after its commissioning and the subsequent registration of the seller's title.

The majority of investment contracts in Russia are recognised as sale and purchase agreements in relation to future property.

In practice, this means that, when a project is structured around an investment contract, the investor is denied ownership rights if the property is under construction or it is actually completed but the developer has not registered ownership. The reason for this is that legally the real estate does not exist until it is registered. Although according to the current Supreme Commercial Court practice there is no risk that an investment agreement will be considered as unconcluded, an investor (buyer) can only compel the seller (developer) to transfer the property once the developer has registered its own initial ownership to the property. Thus the investor is not able to register its ownership immediately after commissioning. Until such registration, the only option provided to the investor is to terminate the agreement and/or claim damages for loss. This solution is far from desirable for investors. There are options for investors which can be tailored for each project and require expert contract drafting. These can include securing obligations via pledges, penalties and/or bank guarantees and, for substantial real estate finance projects, using corporate mechanisms to take control over the developer.

Allocation of land for construction

Where the main type of permitted use is construction, publicly-owned land may be granted on lease only, unless an exception applies (please see the *Acquisition of public land for construction* section below on page 130).

Registration of transfer of title

The transfer of ownership title to real estate must be registered in the State Register. The sale and purchase agreement itself does not have to be registered but merely submitted and examined as part of the registration process. Since 1 January 2015, it is not obligatory to submit a document evidencing the payment of a state duty for the purpose of state registration. However, for the avoidance of any doubt, the provision of such document is still recommended. In addition, under the Law on State Registration when the applicant is a Russian legal entity, the registration authority is obliged to request its constituent documents directly from the competent authorities as a part of the interagency information exchange system and, therefore, it is no longer obligatory to submit constituent documents.

A registration authority must immediately notify the person/entity who has rights over immovable property that a state registration application has been filed in respect of its property. As a general rule, after seven working days from the application date, the ownership title to the real estate can be state registered.

Starting from the moment of state registration, the ownership title to immovable property is deemed to legally exist. However, rights to property which arose before the Federal Law No. 122-FZ "On State Registration of Rights to Immovable Property and Transactions" came into force (in January 1998) are deemed valid

even if they are not registered. According to the principle of publicity and reliability of the information entered into the State Register, any person acting in good faith may rely on any record made in the State Register. Where a person incurs losses as a result of illegal or incorrect data having been entered into the State Register due to a fault of the Registrar, he/she is entitled to claim compensation from the federal budget.

If the parties to a sale and purchase contract choose to conclude it before a notary (they are not obliged to do so), the notary will check the validity of the transaction and undertake the registration formalities with the Registrar. In this case, the state registration of the real estate rights will take three working days and the notary will be responsible for the validity of the transaction.

It is now possible to submit an application and the documents required for the purposes of the state registration of rights in electronic form, through special e-services of the Registrar. The first electronic state registration with the State Register was effected on 15 May 2015. Therefore, as this development is still fairly recent, the existing practice of paper-based registration continues to be followed until e-registration becomes widespread.

Any person may request general information about real estate (such as the owner or registered encumbrances) in the form of an extract from the State Register in paper or electronic format[2]. However, certain information relating to a chain of transactions on the transfer of rights, as well as information about the number of plots and/or properties owned by a certain person or legal entity, may be requested only by the owner of the relevant property.

Certain types of encumbrance (buffer zones of hazardous facilities, protective zones of cable lines and gas transmission lines, etc.) are not always recorded in the State Register. For this reason, it is highly advisable to conduct onsite investigations and legal due diligence of the land plot and any properties located on it, as well as to review the documents kept by the Registrar (e.g. cadastral passports of the property).

New practice of state registration

As mentioned, the Law on State Registration (effective from 1 January 2017) provides for certain changes to the procedure for state registration of real estate. The main goal of these changes is to ensure better guarantees to state registration applicants, increase the liability of the registration authorities, make real estate transactions more efficient and reduce the related investment risks.

However, despite some positive innovations, certain provisions of the Law on State Registration may adversely affect the real estate market players' activities. For example, the registration authority now has more grounds to deny state registration of rights. Formally, the Law on State Registration provides for a single ground

[2] www.rosreestr.ru/wps/portal/p/cc_present/EGRN_1

for such denial – failure to eliminate reasons preventing the state registration of rights within the period during which the registration authority suspends the state registration. However, at the same time there are currently 55 grounds allowing the authority to suspend state registration. Quite a number of these grounds are controversial, in particular because the applicant has no control over some of them (e.g. when a state authority failed to deliver any documents or information requested by the Registrar as part of the interagency information exchange system, when the transaction subject to state registration is void or when a state authority issues an act outside the scope of its competence or that of the signatory). As a result, the number of grounds to deny state registration has increased from 30 to 55.

Furthermore, many provisions of Federal Law No. 221-FZ "On State Cadastre of Immovable Property" dated 24 July 2007, which has been renamed as the Federal Law "On Cadastral Activities" with effect from 1 January 2017, will remain in force. Despite the fact that previous legislation will apply insofar as it does not contradict the Law on State Registration, such situation may result in practical problems with the state registration procedure. This is because registration authorities will need to develop a new practice for recording and registering rights to and transactions with immovable property.

The merger of Unified State Register of Rights to and Transactions with Immovable Property and the State Cadastre of Immovable Property, which were maintained by the Registrar until the end of 2016, into the State Register is taking place gradually. Therefore, the practice of state cadastral registration, state registration of rights and provision of information from the State Register can vary from one region of the Russian Federation to another. As a result, the application of the new rules in practice and the process of migrating data on immovable properties to the State Register should be closely monitored (at least, during the year 2017).

Leases

Land leases

The following persons may (subject to certain restrictions) lease a land plot: (i) Russian and foreign nationals; and (ii) Russian and foreign legal entities.

If the lease relates to public land, the land lease agreement will contain the general provisions dictated by the landlord, as they come from legal acts adopted by the relevant municipal or state body. In practice, they may not be changed. The conclusion of the lease will also generally presuppose a tender process (subject to certain exceptions). A lease agreement in respect of a privately-owned land plot may include any provisions provided they do not contradict any mandatory Russian law requirements.

Material lease conditions, such as the subject matter (i.e. the land plot itself) and amount of the rent, must be clearly determined in the lease agreement. In addition, the parties may set out their own list of supplemental contractual provisions that are material to the transaction.

If a lease agreement does not meet the above requirements, it is deemed not to have been concluded. If this occurs, the land plot must be vacated and returned to its owner, and any rents already paid to the landlord must be returned to the tenant.

Term

Russian legislation places no general limit on the term of a lease of a land plot. However, certain limits exist on leases of specific types of land. For example, the maximum permitted term for a lease of agricultural land or forest land is 49 years. The maximum permitted term for a lease of coastal land is 20 years.

The Land Code expressly provides maximum terms for various types of leases in respect of publicly-owned land plots (there are 21 types in total). For example, a lease agreement of a land plot required for the construction of buildings and structures now may be concluded for a term of three to ten years, a lease agreement of a land plot required for integrated urban development for a term of three to five years. The maximum term of a lease agreement concluded for a purpose of placing linear facilities (e.g. power transmission lines, pipelines, railways, etc.) is 49 years. A 49-year maximum lease term will also apply to those lease agreements which are to be entered into with the owners of buildings located on the publicly-owned land plot as well as to other lease agreements unless a specific maximum lease period is expressly provided by the Land Code.

It should be noted, however, that there is no time limit for commercial lease agreements.

Therefore, the impact of the lease term should be assessed before any material investments are made.

Any lease agreement concluded for a term of at least one year is subject to registration in the State Register. If the lease agreement does not meet these requirements, then it is deemed not to have been concluded. For third parties (i.e. anyone except the tenant and the landlord), the legal effect of this is that the lease is treated as if it was not concluded at all. In such cases, the land plot must be vacated and returned to its owner. However, in accordance with applicable court practice, failure to register a long-term lease agreement does not release the tenant from its obligation to make rental payments, provided that the respective land plot has been duly transferred to the tenant's possession and use.

The Civil Code provides that, where a lease agreement does not specify a term, then it is deemed to have been concluded for an indefinite term. In such cases, a lease may be terminated simply by either party serving a termination notice on the other party at least three months in advance of the intended date of termination.

Upon expiry of the lease, a tenant has a preferential right to conclude a lease of the same land plot for a new term. The lease agreement can expressly exclude this preferential right.

If the tenant continues to use the land plot after the expiry of the lease term and the landlord does not object, the lease will be considered to be renewed on the same conditions for an indefinite term and may be terminated at any time by either party serving a termination notice three months in advance. The Russian courts usually consider this provision of the Civil Code as a mandatory one. Therefore the courts are likely to strike down clauses providing for the automatic renewal of a lease. In order to avoid this uncertainty, the lease should contain an undertaking by the parties to enter into a new lease for the same term and on the same conditions.

Assignment

It is generally permitted (subject to certain restrictions) to sublet, assign, mortgage or contribute leasehold rights to a land plot to the charter capital of a company. Unless otherwise provided for in the lease agreement, sublease, assignment and mortgage agreements may be entered into without the consent of the landlord (but subject to a subsequent notification by the tenant). In any event, there are a number of circumstances when the tenant's right to sublease or mortgage the plot, or assign lease rights, may not be waived or restricted (such as in the case of leases of public land for more than five years).

Termination

The Civil Code grants both a landlord and a tenant the right to terminate the lease unilaterally, either in the limited number of circumstances stipulated by the Civil Code (via court procedure) or as expressly agreed in the lease agreement itself. In the latter case, both in-court and out-of-court procedures may be used.

The Land Code stipulates additional circumstances in which a landlord may terminate a lease. These include, among others, use of the land in a way that is inconsistent with its land category and permitted use, and appropriation by the state.

In relation to state or municipal land, the Land Code also grants a landlord a specific ground for the early termination of a lease which has been concluded for a term of more than five years. If a tenant commits a material breach of the terms and conditions of such a lease agreement, the landlord may apply for a court order enabling it to unilaterally terminate the lease early.

Commercial leases of buildings, structures and premises

Commercial lease sector

Commercial leases have been developing rapidly over the past few years. The market is generally dominated by the private sector of the economy, which means that the legal relationships are heavily influenced by commercial needs, the return on investment and the level of yield.

The commercial lease sector (especially in Moscow, the Moscow Region, Saint Petersburg and other large Russian cities) is also affected by international practice in respect of rent and methods of rent calculation: so-called "net", "double net" and "triple net" leases. A "triple net" lease (the most common type) is a lease

where the tenant is obliged, in addition to the payment of the base rent, to compensate the landlord for all expenses associated with the leased property (including multitenant buildings) such as property taxes, insurance, utilities, and maintenance and operation costs. Triple net leases are usually used for long term lease relations for large malls, business centres and warehouses due to their alleged positive impact on taxes, cash flow and other factors.

Structuring lease arrangements in respect of existing buildings, structures or premises

Long-term lease (the "LTL")

An LTL is a lease agreement which lasts for at least one year. An LTL is only valid upon state registration in the State Register. During the registration procedure the Registrar will examine the validity of the LTL. The material conditions of any lease should, therefore, be clearly determined, including the subject matter of the LTL (i.e. building, premises or structure) and the amount of rent or the rent calculation method.

Under recent amendments to Russian laws, the documents for the state registration of an LTL may now be submitted in electronic form.

Short-term lease (the "STL")

In order for the tenant to legally occupy the building whilst an LTL is being registered, an STL is usually entered into between the parties. Both agreements should be simultaneously executed.

An STL is a lease agreement executed for a period of less than one year (usually 11 months or 360 days). As the term of an STL is less than one year, it does not require state registration. It, therefore, requires only the signatures of the parties in order to be binding.

Structuring lease arrangements in respect of buildings, structures or premises under construction

As until recently it was absolutely impossible to lease future property under Russian law, market players have been using the following two or three-tiered legal structure:

— Preliminary Lease Agreement (the "**PLA**");
— STL; and
— LTL.

This lease structure is also favourable for investment acquisitions since it becomes much easier to calculate the sale value of the property in accordance with international valuation standards.

PLA

When a building, or any other property, is under construction, and a potential tenant wishes to "mark out" the building, as well as particular premises within the building, and "fix" the amount of rent, it enters into a PLA with the prospective owner to regulate their pre-registration relationship.

Prior to registration of an owner's title to the building, as well as the building itself, in the State Register, no LTL may be entered into in respect of buildings

or premises within buildings. The PLA, therefore, contains various obligations (such as the time period for construction, the tenant's requirements for works and fit-out of the building and/or premises).

In order to be legally valid, the PLA must clearly determine its subject matter, sufficiently describe the property to which it relates, and establish all the material terms and conditions of the main lease agreement to be entered into (the "**Main Agreement**").

The parties to a PLA should determine a time period within which the parties must enter into the Main Agreement. If no time period is specified, the parties should enter into the Main Agreement within one year from the date of execution of the PLA. If the parties fail to enter into the Main Agreement within this time period, the PLA will terminate. However, if the failure to enter into the Main Agreement was caused by one of the contractual parties, the courts may force the defaulting party to enter into the Main Agreement.

Main Agreement – STL and LTL

The STL and the LTL are executed after the initial state registration of the ownership title to the building in the State Register.

Alternative arrangement

In its Ruling No. 13 dated 25 January 2013, the Plenum of the Supreme Commercial Court of the Russian Federation considered the issue of whether it is legally possible to conclude a lease of future property.

This Ruling seems to make the conclusion of a PLA redundant. However, it remains preferable to use the original three-tiered legal structure (including signing a PLA). Once the property is registered, the parties enter into an LTL to avoid the risk of the state registration being rejected on formal grounds (i.e. because the landlord is unable to prove that it is the owner of the property before the state registration of ownership title to the property).

Real estate transactions and anti-monopoly control

As a general rule, real estate acquisitions and leases (land and/or buildings) are not subject to anti-monopoly control.

However, pre-transaction anti-monopoly control will apply to the acquisition and lease of production assets such as industrial-purpose structures, facilities of communal infrastructure if:

— their net value exceeds 20% of the net value of the assets of the seller or the landlord; and
— certain worldwide asset value or revenue thresholds of the relevant groups of companies are exceeded (please see the *Anti-monopoly issues* chapter on page 39).

Furthermore, under Federal Law No. 381-FZ "On State Regulation of Trade Activities in the Russian Federation" dated 28 December 2009, food retailers with a market share in a given locality exceeding 25% are prohibited from acquiring or leasing additional outlets in that locality.

Mortgages

Creating a mortgage

Both freehold and leasehold rights to land and buildings may be mortgaged; there are

no restrictions against this in either the Land Code or the Civil Code. Rights to buildings and parts of buildings may also be mortgaged.

The terms and conditions of mortgages are governed by the Law on Mortgage, which requires mortgages over the completed buildings and the underlying land plot be granted simultaneously.

A security interest over a land plot or other property is generally created by the parties entering into an express mortgage agreement. However, a mortgage may arise by operation of law (for example, a bank giving a loan to buy a property will become a mortgagee until the sale price is repaid in full).

A mortgage agreement must be drafted as a single contract, signed by both parties (who may choose to do so before a notary), and then registered with the Registrar. Mortgage agreements concluded before 1 July 2014 only come into effect upon registration in the State Register, failing which they are null and void. Mortgage agreements concluded from 1 July 2014 no longer need to be state registered. They therefore come into effect upon signing. However, mortgages as encumbrances over real estate still need to be state registered.

The parties have two registration options:

— submit a joint application and a set of necessary documents to the Registrar; or
— appoint a notary to submit a notarised application (this option is available if the mortgage agreement is notarised).

The Law on State Registration sets out the time period within which the Registrar must complete the registration formalities. For a mortgage of a land plot and non-residential property under a notarised agreement, the time period is three working days from the date of submission of the application to the registration authority (or one working day if the documents are submitted in electronic form) or five working days if the set of documents is submitted through a special multifunctional centre. For mortgages of land plots and non-residential property under a simple agreement, the time period is seven working days (if the application is made directly to the registration authority) or nine working days (if the application is made via a multifunctional centre).

Enforcing a mortgage

If a significant breach of a secured obligation occurs, the mortgagee may enforce the mortgage. There are two methods of enforcement: (i) through the courts, resulting in the secured property being sold at a public auction; or (ii) through an out-of-court enforcement procedure (provided that the possibility of the out-of-court procedure is prescribed for in the mortgage agreement or a separate agreement between the mortgagee and the mortgagor).

Russian legislation provides for the following options when the mortgagee is using the out-of-court enforcement procedure:

— appropriation of the mortgaged property by the mortgagee; or
— sale at an auction.

In a number of cases, the use of the out-of-court enforcement procedure is prohibited (for instance: if the first and second ranking mortgages provide for different types of enforcement procedures or if the mortgage secures different obligations in favour of co-mortgagees).

The Law on Mortgage also sets out a procedure for the distribution of the proceeds received as a result of the enforcement of the mortgage. For example, for both the out-of-court and court enforcement procedures, the sale proceeds are distributed subject to the priority of claims between (i) all mortgagees that filed their claims; (ii) other creditors; and (iii) the mortgagor. Such priority would have to be determined on the basis of the entries in the State Register.

Resolution of real estate disputes

In Russia commercial disputes between legal entities may be referred to the competent state courts or, if the parties so elect, to arbitration tribunals. However, until 26 May 2011, all disputes related to the execution of contracts subject to state registration, or rights and obligations arising from contracts subject to state registration (for example LTLs, sale-purchase agreements for a plot or property, mortgage agreements) were required to be heard and resolved in state courts. This was the official position of the Supreme Commercial Court of the Russian Federation.

On 26 May 2011, the Constitutional Court of the Russian Federation held that (i) the Supreme Commercial Court's practice contradicts the law; and (ii) any dispute related to a transaction subject to state registration may be heard and resolved in arbitration tribunals established in accordance with Russian legislation. One of these tribunals is the International Commercial Arbitration Court of the Chamber of Commerce and Industry of the Russian Federation. At that time, the Constitutional Court's decision was seen as a positive step for the development of Russian justice and for the improvement of the investment climate. However, very often this decision of the Constitutional Court is ignored by the state courts. In addition, if a real estate dispute involves some kind of public relations other than state registration arrangements (e.g. issuance of construction or commissioning permits), such a dispute can only be reviewed by the state courts. Therefore submission of any dispute for resolution at an arbitration tribunal should be carefully considered.

Planning and construction issues

Land plots are assigned to a land category and a permitted use in order to optimise utilisation of different plots of land.

Land categories

Under the Land Code, land in Russia is divided into seven land categories (each with a designated prescribed use):

— agricultural land;
— land of settlement;
— industrial land (for the purposes of industry, energy production,

transport, communication, television, radio broadcasting, cosmic activities, defence and other special purposes);
- land containing specially protected areas and objects (e.g. nature parks);
- forest land;
- land near water; and
- reserved land.

Specific provisions may apply, depending on the land category. For example, when agricultural land is being sold, Russian regions enjoy pre-emptive rights of purchase, as do municipal authorities, in the situations provided for by the relevant regional legislation. As mentioned above, foreign investors (including companies and individuals) may not own agricultural land, but may only obtain lease rights. Agricultural land that is not used in accordance with its designated prescribed use may be taken from its owner under a court decision.

Essentially, the most suitable categories for development and commercial construction are industrial land and land of settlement. It is possible to build warehouses, commercial buildings and production facilities on land plots within these categories provided that the type of permitted use allows it.

Permitted use of land

Along with a designated prescribed use and zoning, land plots in the Russian Federation are assigned a "type of permitted use". The type of permitted use characterises a land plot in accordance with territorial zoning and establishes the specific use of a certain land plot. Each land category has different conditions for the use of land, and the Land Code requires that each plot be used only in accordance with the applicable category and established type of permitted use.

On 1 September 2014, the Russian Ministry of Economic Development approved the classifier of types of permitted land use (the "**Classifier**"). The Classifier came into effect on 24 December 2014, and starting from this date a type of permitted use of a land plot may only be determined in strict compliance with the Classifier which provides for an exhaustive list of the types of permitted use. The local authorities have to bring local regulations on the territorial zoning (i.e. the rules of land use and development) in line with the Classifier by 1 January 2020. In view of this timeline, the changes will not have to be made in a hurry and it will be possible to take into account any projects already launched, or projects that are still in the planning stage.

Change of land category and permitted use

Land category

It is possible to change the category of a particular land plot. For example, the regional authorities may change a plot's land category from "agricultural" to "industrial" (e.g. for the allocation of a warehouse complex) subject to a number of obligatory procedures. A land plot may be assigned to the category of land of settlement only when it is annexed to the territory of the settlement (included in the borders of settlement). Again, this is done at a regional level if no town planning documentation has been adopted. As soon as the general plan of a settlement is adopted, the relevant

change procedure requires the general plan of the settlement to be amended. This is done at municipal level.

Changing the category of forest land or land near water is more complicated (as it involves federal authorities) and is strictly regulated. Legislation provides an exhaustive list of circumstances in which there may be a change of category in these cases.

Permitted use

The owner of a land plot may change the type of permitted use at its own discretion according to the adopted town planning documentation (general plan of the settlement and the rules of land use and development). Where town planning documentation is not adopted, a strict procedure must be followed in order to change the type of permitted use, which involves public hearings.

Town planning framework

The current federal Town Planning Code stipulates that each urban settlement must adopt city planning documents, including: (i) regional and municipal territory planning documents that establish the boundaries of various development zones in large territories; (ii) city general plans that set out the boundaries of various functional development zones within individual urban settlements; and (iii) rules for land use and development that establish territorial zoning and describe in detail what may be done in each territorial zone of each urban settlement. The town planning documents establish territorial and functional zoning of the settlement territories and indicate existing town planning limitations, such as "red lines" and protection zones.

Construction planned for any new development must comply with the prescribed town planning limitations and zoning. For example, the construction of a large shopping mall in a recreational zone would not be permitted.

The rules of land use and development must be adopted in line with a deadline provided by the Russian land legislation (with regard to the city of Moscow and the Moscow Region, by 1 July 2017). After this date, no new development on state or municipal lands will be allowed in Moscow or in settlements of the Moscow Region. However, it should be noted that the time limits have already been prolonged several times. Therefore, there is reason to believe that they may be prolonged again. Another important document in respect of a particular land plot is the land plot development plan ("*GPZU*"). The land plot development plan contains all information regarding the land plot necessary for construction: the type of permitted use, boundaries, minimum offsets from the boundaries, technical conditions for connection to engineering communications, etc. The land plot development plan is one of the mandatory documents that must be submitted in order to obtain the construction permit.

Construction

Various entities are involved in the construction process in Russia:

— a client ("*zastroyshchik*") – the entity who wants to build a property for itself or for its subsequent sale or lease;
— a technical customer ("*tekhnicheskiy zakazchik*") – a special professional

company engaged by the client in order to supervise and manage the construction of the property;
- a general designer ("*generalniy proektirovshchik*") who develops the design documentation;
- a contractor ("*podryadchik*") or general contractor ("*generalniy podryadchik*") who performs the construction works for the client, either by itself or through subcontractors; and
- various specialised engineering entities who carry out surveys required for the construction.

The client must have rights to the land plot (freehold or leasehold) where construction is envisaged.

Since the majority of land in Russia is still state-owned, before commencing any construction project in Russia, it is important to assess the issues of how to acquire land in Russia and who is responsible for obtaining, from various state authorities, the authorisations and permits required for construction.

Acquisition of public land for construction

The Land Code stipulates a specific procedure for making publicly-owned land available to individuals and legal entities for construction purposes. Both Russian and foreign nationals or legal entities interested in obtaining land for construction may apply to the relevant authority for the allocation of a land plot. Any refusal to allocate land may be appealed against in court (subject to certain restrictions).

Recent amendments to the Land Code have abolished the procedure of preliminary approval of the construction location in cases when a relevant state authority carries out all the preparatory work (i.e. determines the boundaries of the land plot and registers the land plot).

The Land Code Amendments introduce a new, two-step approach which involves firstly, the planning of territory utilisation, and secondly, the allocation of the land plot in accordance with the designated use.

As a general rule, publicly-owned land plots may be formed only after one of the following documents has been presented to the competent authority:

- a land survey plan ("*proekt mezhevaniya territorii*"); or
- a land layout diagram showing the location of the land plot on the cadastral map of the territory (the "**Land Layout Diagram**") ("*skhema raspolozheniya zemelnogo uchastka na cadastrovom plane territorii*").

The Land Layout Diagram option is available only if a duly approved land survey plan is not in place.

However, in certain instances a land plot may only be formed after a land survey plan has been presented. For example, this will be the case when a land plot is to be granted for the construction of power transmission lines, pipelines, railways, etc.

As a general rule, where the main type of permitted use is construction, a land

plot may be granted for a lease only. However, in certain circumstances, land plots may be sold through an auction (e.g. for the purposes of individual residential construction or farming).

As a general rule, allocation of land plots for construction is possible through a tendering process only in the form of an electronic auction.

According to the Land Code, there are 40 special grounds under which it is possible to lease a land plot without a tendering process (e.g. where the interested party is the owner of buildings and structures located on the land plot or where the interested party is a legal entity that is responsible for the construction of power, heat, gas or water supply utilities).

Formation of the land plot for its further sale or lease through an auction is performed as follows:

— a relevant state authority establishes the Land Layout Diagram (if the land plot has not been formed yet and there is no relevant land survey plan);
— if formation of the land plot is prescribed by the land survey plan or the Land Layout Diagram, the relevant state authority will arrange cadastral works and cadastral registration of the land plot;
— the relevant state authority will then obtain technical conditions for connection of the object to the engineering network;
— finally, the relevant state authority takes a decision as to whether to hold an auction.

An interested legal entity may also initiate an auction. In this case, it is responsible for carrying out all the preparatory works mentioned above.

The Land Code Amendments have abolished the priority right of the tenant of a publicly-owned land plot to renew the lease agreement without an auction. This was done in an attempt to enhance competition in the land market and to combat the abuse of rights by bad faith market players. Lease agreements made before 1 March 2015 will also have their priority right of renewal cancelled. However, there is an exemption from this general prohibition. In particular, a tenant may renew a lease agreement of a publicly-owned land plot without an auction if all of the following conditions are met: (i) the land plot was initially granted without a tender; (ii) the application to enter into a new lease agreement is made before the expiry of the current one; (iii) no other person has an exclusive right to the land plot; (iv) the current lease agreement has not been terminated; and (v) the grounds permitting the conclusion of the land plot lease agreement without a tender remain applicable before the lease expires.

Apart from the above, land plots may also be provided to a client by the state or municipal authorities through investment schemes or public private partnership ("**PPP**") schemes (please see the *Infrastructure and public private partnerships* chapter on page 175). In these cases, the title to the land plot is provided to the successful bidder within the time period set out in the respective agreement.

When a lease of public land located in the cities of Moscow or Saint Petersburg was concluded before 1 January 2011, the state authorities are entitled to terminate the lease unilaterally by giving one month's prior termination notice in the following cases:

— failure to complete construction in accordance with the terms specified in the lease agreement, or, if such terms are not specified, within the construction terms set out in the construction permit if the property under construction is less than 40% complete;
— if the construction permit has not been obtained within five years of the date of execution of the land lease; or
— if the law has changed and no construction activity may be performed on a land plot or the land plot is subject to encumbrances or third party rights preventing construction.

If the land lease agreement is terminated due to the reasons above, the client may only claim direct expenses duly documented. Loss of profit will not be recovered.

Seizure of land plots for government and municipal needs

A new procedure for the seizure of land for state and municipal needs came into force on 1 April 2015.

As a result, the following key aspects have been introduced: (i) a detailed state authorities' decision-making process for the seizure of land plots; (ii) a procedure for preparing and concluding seizure agreements; and (iii) the specifics of fixing the amount of compensation in view of land seizure (which must cover of the benefits foregone) – such compensation being payable not only to landowners, but also to land users and tenants of land plots.

Entities, holders of natural monopolies, subsoil users and others may initiate a land seizure procedure. Once the seizure decision is adopted by the relevant state authority, it is valid for three years from the date of adoption and may be challenged in court.

One more important fact is that the given legal developments specify the procedure of paying compensation in view of land seizure not only to the owners of land, but also to land users and tenants of land plots, including the coverage of benefits foregone.

Expropriation of incomplete construction facilities

One of the crucial changes introduced by the Land Code Amendments is connected with expropriation of an incomplete construction facility from the developer if the lease agreement of the publicly-owned land plot underneath this facility is terminated. An incomplete construction facility is disposed of by sale through an auction. Such a disposal will be possible only if all of the following conditions are met: (i) construction of the asset is not completed by the termination date of the lease agreement; (ii) the land plot was provided pursuant to a tender; and (iii) the delay in the asset's construction is not due to any action (or omission) of state or local authorities, or persons operating the utility networks to which the asset has to be connected. The purpose of these rules is to encourage developers

to meet deadlines for construction projects on leased publicly-owned land plots. These provisions, however, do not apply where a lease agreement has been concluded before 1 March 2015.

A decision to dispose of an incomplete construction facility may be adopted only by a court upon a claim to sell the facility through an auction. The claim may be filed by a state or local body authorised to dispose of the relevant land plot. The proceeds of the sale must be transferred to the former owner of the incomplete construction facility (i.e. to the developer). However, the developer may extend the term of the lease agreement of a publicly-owned land plot without an auction once, in order to complete the construction. This can only be done if an authority has failed to file a court claim to expropriate the incomplete construction facility in due time, if the court has dismissed such a claim, or if the asset has not been sold through an auction.

Construction permits

Any construction activity may only be performed on the basis of authorisations and permits issued by state authorities. In Russia the list of such permits and authorisations may differ depending on the type of property to be constructed.

A construction permit must be obtained prior to the commencement of any construction works. This is a formal document that confirms that the design documentation meets the compulsory requirements of the law.

Construction permits will be issued only in the following cases: (i) the applicant has all entitling documents to the land plot; (ii) a positive (state or non-state) expert opinion has been received by the applicant on the design documentation; and (iii) there are no contradictions between the entitling documents, design documentation and the land plot development plan.

The Town Planning Code requires the applicant for a construction permit to have rights (freehold or leasehold) to the land plot. If someone constructs a building on a land plot over which it has no rights, the building may be declared to be an "unauthorised structure" by the courts, and demolished at the expense of the person who developed the "unauthorised structure".

A construction permit may be obtained by a client or by a technical customer acting as the client's agent.

A construction permit contains a number of essential elements such as the time period for the construction works, the area of the constructed property and the name of the client. A valid construction permit is one of the documents required to commission the constructed property.

Commissioning

Property commissioning is the second most critical milestone in the construction process. Commissioning may be divided into two stages:

— commissioning of the works performed by the contractor/ subcontractors for the client; and

— commissioning of the constructed property by the state authorities.

The first stage is critical in respect of the contractual relationship with the contractor or general contractor since commissioning of the works performed is treated as their acceptance by the client. This means that a contractor or general contractor is entitled to claim for payment for the works performed (the payment mechanism is usually determined in the construction agreement) and the warranty period begins to run from the date of acceptance.

The second stage is critical for state registration of the property. During this stage the state construction supervisory authority examines the compliance of the constructed property with the construction permit, the design documentation and the land plot development plan. If certain parameters (such as the total area, total structural volume, etc.) differ, the commissioning permit will not be issued and it will be impossible to register the property in the State Register.

Starting from 1 January 2017, the state cadastral registration of a newly-built building or structure is based on the application of the authority issuing the commissioning permit and such an application is to be submitted by this authority to the Registrar within five working days. Moreover, it is now clearly specified that, for the purpose of state registration of the ownership title to a newly-built building or structure, it is sufficient that a lease agreement for the land occupied by the property be effective as at the commissioning date.

Admission certificates and licences

Legal entities providing the following construction and design activities must become members of self-regulated organisations ("**SROs**") which authorise their members to carry out certain activities by issuing admission certificates:

— designing buildings and structures;
— constructing, reconstructing and carrying out major repairs of buildings and structures; and
— engineering and surveying for the purposes of erecting buildings and structures.

As of writing, no survey, design and construction activities as mentioned above are permitted without the relevant admission certificate issued by an SRO. Failure to comply with this requirement could result in criminal or administrative liability. This also applies to subcontractors since Russian law does not recognise the "umbrella principle" in respect of admission certificates.

The list of activities subject to the admission certificate requirement is set by the Ministry for Regional Development of the Russian Federation. It currently contains many activities. Activities that are not listed in the Ministry's decrees are generally exempt from the admission certificate requirement. However, some construction-related activities are still subject to licensing requirements. Examples of these activities include the installation of a fire fighting system or the operation

of some industrial facilities classed as posing fire or explosion hazards.

Both Russian and foreign legal entities may obtain admission certificates. SRO membership fees depend on type of activity and may be substantial.

In July 2016, important amendments to the Town Planning Code concerning SROs and admission to the above mentioned survey, design and construction activities were approved by Federal Law No. 372-FZ dated 3 July 2016 (the "**SROs Amendments**"). Most amendments will come into force on 1 July 2017 (with some exceptions mainly concerning a new approach to the organisation of SROs' activities and the management of SROs, which became effective on 4 July 2016).

The most significant changes imposed by the SROs Amendments are the following:

— SROs for construction companies will now operate on a regional basis, i.e. any construction company must be a member of the SRO which is registered in the region of the Russian Federation where such construction company is itself registered. Exceptions from such regional registration principle are only provided for foreign legal entities and Russian companies incorporated in the regions where no construction SRO was incorporated.
— All admission certificates issued by SROs will become invalid starting from 1 July 2017. Therefore, the only document confirming the right to perform survey, design and construction activities will be an extract from the register of an SRO's members (which will be valid for one month from the date of its issuance).
— Technical customers must be members of an SRO in order to legally perform their activities.
— In some cases, companies will be allowed to carry out survey, design and construction activities without SRO membership. Such exemptions include, for example, the following:
  - performance of construction works when the total amount of the particular construction contract is less than RUB 3m (EUR 47,620);
  - performance of survey, design and construction works by state or municipal enterprises, by commercial legal entities in which the state, a region or municipality, a state or municipal enterprise has a stake of more than 50% or by legal entities incorporated by the state, a region or municipality – under some kind of contracts concluded with federal governmental authorities, state corporations, regional and local authorities, etc.;
  - performance of survey, design and construction works by subcontractors which do not have direct contractual relations with the client, technical customer, person responsible for the building's operation or regional operator.
— In addition to the general indemnification fund (securing liabilities of SRO members in the event of personal injury or property damage resulting from the destruction

or damage to a building or structure), there are some cases when SROs are required to set up one more fund, in particular, a compensation fund securing contractual liabilities of the SRO's members. Each SRO must incorporate such a fund when a certain number of SRO members (depending on the type of SRO) has informed the SRO of their intention to perform works or provide services under agreements concluded through tender procedures (i.e. under agreements with public authorities, state, municipalities and other publicly-owned counterparties). Such a fund is required to secure the liability of SRO members for the non-fulfilment or improper fulfilment of their contractual obligations under the abovementioned agreements.

— The SROs Amendments also regulate in detail requirements applicable to SROs, to their special standards and internal documents as well as other related organisational aspects of SROs' activities.

"Any legal entity or individual may own private land in the Russian Federation, subject to certain restrictions which regulate the legal status of the land plot."

Anti-corruption and compliance

General approach

Over the past decade, a number of anti-corruption measures have been introduced at the legislative and executive levels in Russia. However, the issue cannot be resolved all at once and the level of corruption in Russia is widely assumed to be relatively high according to international studies and ratings.

Recent developments and trends

As part of the Public Security Concept 2013-2020 approved on 20 November 2013, the President's National Anti-corruption Plan for the period 2012-2013 has been impliedly "prolonged" for 2014, 2015 and 2016. The main goals of the Government remain (i) to study the issues relating to conflicts of interest for certain categories of public officials; (ii) to organise training for federal officials involved in combatting corruption; and (iii) to consider how the Government can reduce the financial attractiveness of corruption.

Since 1 January 2013, Russian organisations have been obliged by law to develop and implement anti-corruption measures (please see the *Compliance requirements for companies* section below).

A hotly debated law prohibiting public officials and their relatives from owning bank accounts and

keeping funds and valuables abroad was enacted on 7 May 2013 (Federal Law No. 79-FZ). This law also imposes an obligation on public officials and their relatives to disclose information on real estate they own abroad and liabilities they owe abroad.

In December 2013, a new Department for Counteracting Corruption was created within the Administration of the President by Presidential Decree No. 878 dated 3 December 2013. The aim of this new governmental body is to check the validity of information provided in declarations of income, property and expenses as well as to conduct conflict checks involving Russian public officials.

Legal framework

Relevant legislation

For many years, there was very little anti-corruption legislation in Russia. However, in 2008, the first National Anti-corruption Plan was announced. As part of that Plan, Federal Law No. 273-FZ "On Fighting Corruption" was enacted on 25 December 2008 (the "**Anti-corruption Law**"). This law remains the principal legislative act on bribery in Russia. However, the relevant legislation is by no means consolidated and relevant provisions are found in a number of legal acts.

Russian law in this area is also affected by international treaties.

The current legislation on corruption now includes:

- International legislation:
  - United Nations Convention against Corruption dated 2003 (ratified by Russia in 2006);
  - Criminal Law Convention on Corruption No. 173 by the Council of Europe (ratified by Russia in 2007); and
  - OECD Convention on Combating the Bribery of Foreign Public Officials in International Business Transactions dated 1997 (ratified by Russia in 2012).
- Federal legislation directly addressing corruption:
  - the Anti-corruption Law;
  - Federal Law No. 230-FZ "On Monitoring the Correlation of Expenses by State Officials with their Incomes" dated 3 December 2012;
  - Federal Law No. 79-FZ "On the Prohibition for Certain Categories of Individuals to Open and Have Accounts, Keep Moneys and Assets in Foreign Bank Accounts outside the Russian Federation, Own and/or Use Foreign Financial Instruments" dated 7 May 2013;
  - Federal Law No. 172-FZ "On Anti-corruption Examination of Regulative Acts" dated 17 July 2009;
  - Law No. 2202-1 "On Public Prosecution" dated 17 January 1992;
  - Federal Law No. 79-FZ "On Public Civil Service" dated 27 July 2004 (the "**Public Civil Service Law**");
  - Federal Law No. 262-FZ "On Access to Information on Court Activities in the Russian Federation" dated 22 December 2008;

- the Criminal Code of the Russian Federation dated 13 June 1996 (the "**Criminal Code**"); and
- the Code on Administrative Offences of the Russian Federation dated 31 December 2001 (the "**Code on Administrative Offences**").

— Federal legislation indirectly addressing corruption, such as:
- Federal Law No. 3-FZ "On Police" dated 7 February 2011;
- tax law (please see the *Disclosure rules* section below); and
- Federal Law No. 44-FZ "On the Contractual System in the Sphere of the Procurement of Goods, Works or Services for State and Municipal Needs" dated 5 April 2013 (the "**Public Procurement Law**") – (please see the *Example of sector-specific anti-corruption measures* section below).

— Decrees of the President, the Federal Government and other executive bodies, adopted between 2008 and 2013, specifically:
- establishing the National Anti-corruption Plan (includes a list of steps and measures to be taken with a view to fighting corruption); and
- regulating the anti-corruption examination of the acts of governmental bodies.

However, the legislation is still fragmentary and sometimes confusing.

In addition to Russian law, laws of other states may be applicable to situations in Russia. The United Kingdom Bribery Act of 2010 and the United States Foreign Corrupt Practices Act of 1977, have a wide extraterritorial reach.

State agencies

Apart from the general law enforcement authorities (the police, public prosecution, etc.), several state agencies have responsibility for enforcement of federal anti-corruption measures, such as the President's Council on Counteracting Corruption (as a supervising body) and the Ministry of Justice (responsible in particular for the anti-corruption screening of draft legal acts). The Office of the Prosecutor General also investigates instances of corruption in criminal matters. Special parliamentary committees have also been established to monitor the income and assets of the members of Parliament.

Compliance requirements for companies

Relevant amendments to the Anti-corruption Law came into force on 1 January 2013. They require Russian companies, representative offices and branches of foreign companies to develop and implement internal measures aimed at preventing bribery. These include, amongst others, appointing compliance officers, adopting internal codes of ethics and policies for all employees, cooperating with law enforcement authorities.

In April 2013, the Russian Ministry of Labour and Social Protection issued non-prescriptive guidelines on the development and implementation of anti-corruption measures.

The guidelines provide the following eight principles for bribery prevention:

— conformity of an organisation's anti-corruption policy with current legislation and generally accepted rules;
— top-level commitment by setting an example;
— staff involvement;
— proportionate anti-corruption measures;
— efficiency of anti-corruption measures;
— liability and inevitability of sanctions;
— business transparency; and
— constant control and regular monitoring.

To date, no sanctions are provided for failure to take anti-corruption compliance measures. However, in the event of checks by the authorities (police, public prosecutor, etc.), an order to remedy the failure can be issued against the delinquent company. In turn, failure to implement this kind of order carries administrative sanctions, namely fines and/or the disqualification of the company's general director from holding office for up to three years.

Concept of corruption in Russian law

The Anti-corruption Law defines corruption as:

— the abuse of an official rank or powers;
— giving or receiving a bribe;
— commercial bribery;
— other illegal use of official rank by an individual contrary to the lawful interests of the state and society for the purpose of any form of material benefit for oneself or others; or
— the illegal provision of a material benefit to a public official by another individual on their own behalf, or on behalf of or pursuant to the interests of a legal entity.

Material benefit includes money, valuables, other property or pecuniary services, benefits of a "property character" ("*imushestvenniy kharakter*", e.g. travel offers), and other property rights.

Bribery is subject to the Criminal Code and consists of two interdependent elements: (i) the giving of a bribe; and (ii) the taking of a bribe. They are committed simultaneously and result in two separate crimes.

According to the Anti-corruption Law, a bribe involving money and other assets may be a property-related benefit, service or a favour, and must have a monetary value (renovation, building a house, etc.). Property-related services may include the transfer of property at an undervalue, a reduction of lease payments or loan interest rates.

If these benefits are provided to family members or friends of the official, with the official's approval or consent, and the official has used his/her official powers to the benefit of the briber, this also constitutes bribery.

Commercial bribery is the illegal transfer of material assets to a legal entity's manager in connection with his/her position as well as the unlawful rendering of property-related services, or the granting of other property rights to him/her for

taking action (or refraining from action) in the interest of the giver.

Possible targets of bribery

Even though the Anti-corruption Law contains a commercial bribery element, public officials constitute the main target of the legislation.

Definition of public officials for the purpose of anti-corruption legislation

For the purpose of Russian legislation public officials include any official or functionary executing managerial, regulatory, administrative or economic (financial) functions. Specifically, these officials hold state (i.e. federal or regional) or municipal offices established by law and discharge those functions entrusted by law, specific normative acts or on the basis of an order of a respective superior official.

Officials without executive authority may still commit breaches of the Anti-corruption Law when, in their official capacity: (i) they have the opportunity to prompt another official to act (or refrain from acting) and; (ii) they have been bribed for general patronage or connivance. Even if a briber is coerced into offering a bribe by a person presenting himself/herself as an official, the former may still be liable for a bribery offence.

Prohibitive measures for public officials

Under the Public Civil Service Law, public officials are prohibited from:

— engaging in entrepreneurial activities;
— receiving from legal entities or individuals remuneration in cash or non-cash gifts (except for gifts with a value of up to RUB 3,000 (EUR 47[1]) given during official events);
— travelling abroad at the expense of legal entities or individuals; and
— disclosing confidential or relevant information obtained during civil service in favour of legal entities or individuals after retirement.

The Public Civil Service Law also stipulates a mechanism for regulating conflicts of interest involving public officials.

Disclosure rules

Under Russian tax law, public officials and their close relatives (their spouses and minor children) must file compulsory income declarations. The tax authorities and the recently established Department for Counteracting Corruption are empowered to check the income of officials and demand an explanation as to the origin of their assets, if these assets do not correlate with the income level of the individual.

A new requirement for public officials and their close relatives to disclose expenses that exceed their declared income was introduced as of 1 January 2013. It applies to expenses incurred since 1 January 2012 in connection with the acquisition of immovable property, motor vehicles, securities and/or participations in legal entities.

[1] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

Public officials may be dismissed for loss of confidence by their "employer". Their dismissal may result from a conflict of interest while in public service, or from a failure to disclose income or expenses which should have been disclosed. If it is discovered that an official is involved in entrepreneurial activities or affiliated with legal entities, he/she must be dismissed on these legal grounds.

Responsibility and penalties for corruption

Laws enacted between 2008 and 2012 have substantially increased the penalties for corruption in Russia. Specifically, fines for offering and accepting bribes are now calculated as multiples based on the amount of the bribes (i.e. the higher the bribe, the higher the fine).

Public officials

Apart from bribery, the Criminal Code holds public officials liable for crimes committed against the state and/or municipal authorities, such as:

- abuse of powers;
- exceeding rank and authority;
- illegal entrepreneurial activities; and
- forgery by an official.

If a public official is prosecuted for several crimes, the court will first consider each of them independently and then as a whole to determine the gravity of the offence and resulting sentence.

Under the Criminal Code, only individuals may be held liable for crimes specified in the Code (including bribery/commercial bribery); however, legal entities may be punished for corrupt activities under the Code on Administrative Offences. The liability of a legal entity does not exempt a culpable individual from liability, and vice versa.

Interestingly, a bill extending the criminal liability of legal entities has been under consideration by the State Duma since 2015, although it is not yet known when the respective law will be enacted.

Individuals

Individuals are subject to:

- liability to reimburse losses in full (under the Russian Civil Code);
- disciplinary actions resulting in the termination of employment (under the Russian Labour Code);
- up to 10 years' imprisonment for abuse of authority;
- up to 8 years' imprisonment for commercial bribery (for the bribe giver);
- up to 12 years' imprisonment for abuse of authority in conjunction with commercial bribery;
- up to 15 years' imprisonment for a public official who receives a bribe;
- up to 15 years' imprisonment for bribe giving; and/or
- disqualification of a bribed public official from holding public office for up to 15 years.

In addition to or instead of the abovementioned liability, those giving or receiving bribes (including commercial bribes) may be fined 10 to 100 times the amount of the bribe offered/received.

In addition, amendments to anti-corruption legislation adopted in July 2016 extended the criminal liability for mediation in bribery in commercial and other organisations (setting the penalty for up to seven years' imprisonment) as well as mediation in bribery of public officials (setting the penalty for up to 12 years' imprisonment).

Legal entities

Legal entities may be prosecuted for:

- the illegal employment of a current or former public official, carrying a fine up to RUB 500,000 (EUR 7,937); and
- the illegal payment of a bribe on behalf of a legal entity, carrying a fine of at least RUB 1m (EUR 15,875) plus seizure of the amount paid.

Example of sector-specific anti-corruption measures

The Public Procurement Law contains provisions which are designed to counter bribery by:

- requiring the holding of auctions or competitive tenders for the purchase of goods, works and services for federal, regional and municipal needs ("**Public Procurement**");
- regulating in detail the procedural aspects of Public Procurement (including requirements applying to tender participants);
- prohibiting tender rules that limit the number of participants; and
- requiring Public Procurement decisions to be adopted by more than one public official (i.e. shared responsibility in adopting these decisions).

"In 2016, criminal liability was increased in respect of various corruption-related breaches."

Your smartest ideas need the toughest protection

When an idea's really good, everyone wants to be part of it. That's why your intellectual property needs to be supported by CMS.

Intellectual property

General approach

Over recent years Russia has demonstrated its willingness to reinforce its efforts in combating the infringements of intellectual property rights.

Negotiations aimed at Russia's accession to the World Trade Organisation led to Russia becoming a member in 2012. In the run-up to WTO accession, Russia adopted new legislation matching international standards for the protection of intellectual property rights by, in particular, increasing sanctions for, and improving legal mechanisms to combat infringements of intellectual property rights. The resulting legal framework in the field of intellectual property is generally in line with international standards, allowing right owners to adequately protect their intellectual property rights.

Examples of Russia's commitment to advancing the fight against copyright infringements include the adoption of:

— a law that connected administrative fines for the production of fake goods with the number of fake goods produced in summer 2013;
— the so-called "Anti-piracy Law"[1] which applies to the procedural issues of blocking almost all types of copyright infringing content on the Internet (please see the *Intellectual property rights infringements* section on page 152); and
— a set of amendments to the Russian Civil Code (the "**Civil Code**") in spring 2014 expressly providing for:
  - the presumption of guilt of intellectual property rights infringers; as well as
  - the legal possibility of contacting Internet providers with a request to stop infringement of intellectual property rights on the Internet.

International standards

Russia is a party to a number of the most important international treaties and conventions covering different intellectual property aspects, including:

— the Convention establishing the World Intellectual Property Organisation;
— the Universal Copyright Convention;
— the Berne Convention for the Protection of Literary and Artistic Works;
— the Paris Convention for the Protection of Industrial Property;
— the Madrid Agreement on the International Registration of Marks and the Madrid Protocol;
— the Singapore Treaty on the Law of Trademarks;
— the Nice Agreement on the International Classification of Goods and Services for the Purposes of Registration of Trademarks;
— the Patent Cooperation Treaty;

[1] Federal Law No. 187-FZ dated 2 July 2013.

— the Locarno Agreement Establishing an International Classification for Industrial Designs;
— the Geneva Convention for the Protection of Producers of Phonograms against Unauthorised Duplication of their Phonograms; and
— the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).

General legal framework

Civil Code

The need to ensure consistency in the legal regulation of intellectual property has led to the adoption of Part IV of the Civil Code. This codifies the existing general legal rules concerning intellectual property rights whilst introducing some new provisions and principles.

Part IV of the Civil Code came into force on 1 January 2008 and replaced previous legislation regulating intellectual property rights, including the copyright law, the trademark law, the patent law and the software law. It was modernised as part of the Civil Code reform by the enactment on 12 March 2014 of a set of amendments concerning intellectual property rights (the "**Civil Code Amendments**") that came into force on 1 October 2014. The main changes are reflected below.

Part IV of the Civil Code includes an exhaustive list of intellectual property rights and the various legal methods for protecting these rights. It also sets out some general requirements concerning their use and their enforcement.

Regulatory orders

In addition to Part IV of the Civil Code, certain intellectual property issues are regulated by orders of the Federal Service for Intellectual Property ("**Rospatent**").

Rospatent is subordinated to the Ministry of Education and Science and it is responsible for the registration of intellectual property rights to trademarks, patents, software, databases, as well as for the registration of, alienation of, and encumbrances over these registered rights.

Novelty in the judicial sphere

The Russian Intellectual Property Court (the "**IP Court**") started operating in 2013. As expected, this has led to an increase in professionalism and a sound legal approach with regard to judgments in this field, not only from the newly established court but also across the Russian court system as a whole (please see the *IP Court* section on page 154).

Contractual aspects of intellectual property rights

Licence agreement

General

A licence agreement grants the right to use intellectual property rights within the limits set out in the agreement.

Under the Civil Code, licence agreements must set out the following information:

— the licensed object;
— the duration of the licence;
— the territories for which the licence is granted;

— the manner in which the licensed object may be used; and
— the amount of remuneration (i.e. the royalty payments) or its method of assessment.

The licence may be granted on an exclusive or on a non-exclusive basis. By granting an exclusive licence, the licensor is not only unable to issue subsequent licences to others, but is also prohibited from itself using the rights transferred under such licence, unless otherwise agreed by the parties. If the licensee is entitled to issue sublicences, this must be expressly provided for in the agreement.

Licences are deemed to be granted for consideration, even if the licence agreement is silent on remuneration. The agreement may fix the amount of remuneration (royalty payments), or set out a method to determine it. Remuneration may take the form of a lump-sum fixed in advance and delivered as a single payment, periodical royalties, or as a percentage of revenues.

Commercial entities are now prohibited from entering into exclusive licence agreements worldwide and for the whole term of the respective intellectual property protection on a free-of-charge basis.

Shrink-wrap licences

The Civil Code permits the use of shrink-wrap licences for software and databases which may be granted to each user (i.e. where the conditions of the licence are provided for on the wrapping of the CD (or other means of delivery) and the first use of the software or database by the consumer means they agree to adhere to the conditions of the licence). This type of licence agreement is considered to be royalty-free, unless otherwise provided for in the respective licence agreement.

Open licences

The Civil Code Amendments introduced the legal concept of an open licence to use works of science, literature or art. In essence, this type of licence is deemed to be a contract of adhesion and the law therefore requires the terms and conditions to be freely accessible to anyone who wishes to review them.

Licence conditions must contain the scope of the use of the work. Unless otherwise stated in the licence conditions, licences will be granted free-of-charge and be valid throughout the world for five years (if the open licence is for computer programmes and databases, this will be for the duration of the exclusive rights).

Assignment of exclusive rights

According to the Civil Code, this contract involves transferring the full and exclusive rights and title to an object of intellectual property rights for the entire period during which these rights are protected. Notably, the Civil Code Amendments expressly prohibit free-of-charge assignment agreements between commercial entities (unless otherwise regulated by the Civil Code).

Governmental registration of contracts

If a trademark, software, database, invention, utility model or design

is registered with Rospatent, then any licence, assignment contracts or pledge contracts (as expressly provided for by the Civil Code) also require registration with Rospatent in order for the contract to be valid for third parties.

Rights over the results of intellectual activity

Copyright and neighbouring rights

Copyright

Copyright covers scientific, literary or artistic work that is the product of creative work regardless of the value, type or mode of expression of the work. Copyright protects both disclosed and undisclosed works. Copyright protection arises when a work is created. There are no registration requirements.

Chapter 70 of the Civil Code gives an author certain rights over his/her work. It sets out exclusive property rights over the work, as well as moral rights for the author of the work.

These exclusive rights include (among other things) the:

- right of reproduction;
- right of distribution;
- right of demonstration to the public;
- right to import or export originals; and
- right to provide access to the work by any means of telecommunication (including the Internet).

Moral rights include in particular the:

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

The exclusive rights to the works are protected for the lifetime of the author plus 70 years.

Infringement of copyright may lead to civil, criminal and/or administrative liability.

Neighbouring rights

Neighbouring rights cover the creation and use of performances, phonograms, broadcasting programmes, cable distribution organisations, and databases.

The owner of neighbouring rights may be the performer of phonograms, the creator of databases or the broadcaster of media (which has been created by the broadcaster).

Under the Civil Code performers enjoy exclusive property rights and moral rights, whilst radio and television broadcasters enjoy only exclusive property rights.

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

The rights enjoyed by owners of neighbouring rights may be granted by virtue of a licence agreement, or a contract for the exclusive assignment of rights.

Patents

Patent protection covers:

- **inventions**, which are a technical solution in any field related to a product or a process;

— **utility models**, which are the devices that are the result of intellectual activity in the scientific and technical spheres; and
— **industrial designs**, which are the result of intellectual activity in relation to the appearance of the product.

Chapter 72 of the Civil Code regulates the protection of inventions, utility models and industrial designs.

Patent protection is subject to conditions, which depend on the type of object being protected.

An invention can only be protected if it is:

— new;
— has an inventive step; and
— is capable of industrial application.

A utility model can only be protected if it is:

— new; and
— capable of industrial application.

An industrial design can be protected only if it is:

— new; and
— original.

The concepts of dependent invention, dependent utility model and dependent industrial designs have been defined in the Civil Code Amendments. To use them, it will be necessary to be authorised by the patent holder of the inventions, utility models or industrial designs. Without such authorisation, the dependent objects of intellectual property cannot be used. Unlike copyright, which protects the author's work from the day of its creation, a patent is only protected after being registered with Rospatent. The right to obtain a patent belongs to the inventor, his/her employer (in case of an employee's invention) or to their assignee(s). The patent application is filed with Rospatent for examination. Rospatent will grant the patent if the relevant criteria are met.

The maximum duration for patent protection is as follows:

— 20 years from the filing date of a patent application for an invention, with the possibility of up to a 5-year patent term extension;
— 10 years from the filing date of a utility model application, with the possibility of up to a 3-year term extension; and
— 5 years from the filing date of an industrial design application, with the possibility of up to a 5-year term extension, which may be renewed so that the entire period of life of a design patent may be up to 25 years.

The patent licence and/or any assignment agreement need to be registered with Rospatent. It is also possible to obtain a compulsory licence, following the decision of a court. Rospatent also registers open patent licences, which may be chosen by the owner of the patent.

Since October 2014, industrial design applicants no longer need to file a list

of essential features of the design by registration, which had traditionally been serving as the basis for determining the scope of protection of the design. This means that designs are protected within the scope of the image of the design and its description. This change has narrowed the scope of protection of industrial designs.

Trade secrets and know-how

IP-related information which has actual (or potential) commercial value can be defined as a trade secret or know-how as long as the necessary criteria are met. In particular, the information must be unknown to third parties because there is no free access to it. Further, the owner of the trade secret must take active measures to protect the secret and ensure that there is no free access to it (in particular, by implementing the so-called "trade secrecy regime").

The Law on Trade Secrets[2] (as last amended on 12 March 2014) defines the information that constitutes a trade secret and lists the measures that the right owner should take in order to ensure the protection of know-how. The law also provides for civil, administrative and criminal liability for a breach of trade secret rights.

Employees' work and employees' invention

The Civil Code regulates employees' work. This includes literary work and patented objects that are created by employees as part of their employment duties.

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

However, if the employer fails to use, license or assign its employees' work within a prescribed period, or the employer fails to notify the employee that it has decided to keep the work secret, the exclusive rights to the work (or invention) will be transferred to its author, i.e. the employee. This does not apply to know-how.

If the employer has started to use the work, assigned the rights to it, or has decided to keep it secret, the employee is entitled to be remunerated as agreed by the parties. If the parties fail to agree on the amount, then a competent court may determine the remuneration. On 1 October 2014, long-awaited rules on the amount of remuneration of employee inventors of patentable inventions, industrial designs and/or utility models ("**IP Objects**") came into force[3]. They set minimum amounts for three different types of compensation, namely for: (i) the creation of a patentable IP Object; (ii) use of an IP Object by the employer; and (iii) the licensing or assignment of an IP Object by the employer.

As clarified by the Civil Code Amendments, the right to remuneration from the employer is not inheritable. However, the rights from the agreement concluded between the employee and the employer, as well as any outstanding remuneration which the employer has not paid, are transferred to the employee's heirs.

[2] Federal Law No. 98-FZ "On Trade Secrets" dated 29 July 2004.

[3] Russian Government Decree No. 512 dated 4 June 2014.

Trademarks, appellations of origin, company names and trade names

Chapter 76 of the Civil Code provides for the protection of means of individualisation, i.e. the protection of those intellectual property rights that are used to distinguish and identify companies or the goods or services they offer.

Company names

The company name is indicated in the corporate documents of the company, and it is reflected in the Unified State Register of Legal Entities. The company name is protected in Russia upon the company's registration with the tax authorities.

The exclusive right of a company over its company name may not be transferred or licensed to third parties. This exclusive right allows the owner of the company name to use the name freely, in particular, (i) on signs; (ii) on letterheads; (iii) on official documents; (iv) in advertising; (v) on products; (vi) on packaging; and (vii) on the Internet.

Additionally, the company name may be protected as a trademark or as a commercial name (a trade name).

Trade names/commercial names

Legal entities may use trade names separately from their company name. Unlike the company name, the trade name is not necessarily mentioned in corporate documents, or in the Unified State Register of Legal Entities. The trade name may be used to distinguish a legal entity. A legal entity can have only one trade name. A legal entity may not use a trade name which would create confusion with a third party's company name or trademark or which would mislead consumers. The right to use a trade name to individualise a Russian company is valid throughout Russia.

This exclusive right ceases to exist if the owner does not use the trade name for one year. The right to use a trade name is protected independently, regardless of the company name or trademarks. It may be transferred by a franchise agreement, or by a contract for the lease of an enterprise.

Trademarks/service marks

A trademark is a designation which is used to distinguish the goods or services of companies. A trademark can be a word, figure or a three-dimensional designation, or a combination of all of these elements. The Civil Code provides a list of words and designations that may not be used as trademarks.

To be protected in Russia, the trademark needs to be registered with Rospatent in the Register of Trademarks. Alternatively, it may be protected in Russia under the Madrid System of the International Registration of Marks.

The maximum duration of trademark protection is ten years, which is calculated from the date of filing of the application with Rospatent. There is an option to renew this ten-year protection period, subject to the necessary petition and payment being made.

As a general rule, the exclusive rights to a trademark are transferable to third parties, unless this assignment would be misleading for consumers. The exclusive right to use a trademark may also be licensed to allow a third party to use that trademark within the framework of the licence and in accordance with the quality requirements set out by the licensor.

Trademark protection may be terminated early if the trademark is not sufficiently used during any three consecutive years after the date of registration. Any interested person may file an application for non-use invalidation with the Chamber of Patent Disputes under Rospatent.

Information on applications for the registration of a trademark is to be published in the official gazette of Rospatent, as well as in Rospatent's online database according to the Civil Code Amendments. As of 1 October 2014, any person may object to a particular trademark as soon as this information has been officially published.

Appellation of origin of goods

The appellation of origin of goods is the name of the place where the goods come from. It may designate a country name, a city or any geographical area referring to the place of origin of the product.

An appellation of origin registered with Rospatent is protected throughout Russia. Any producer (or group of producers) acting within the geographical area designated by the appellation of origin may enjoy the right to use that name provided it has first obtained a certificate from Rospatent and, if the appellation of origin has not yet been registered, to register it.

The newly introduced system of official publication of trademark registration applications and right to object described above will apply to appellations of origin.

Intellectual property rights infringements

Situation in Russia

Counterfeiting and piracy are difficult to quantify in general, and this is especially true in Russia. It affects all areas of the Russian economy, including: consumer products, automotive, pharmaceuticals, etc. Counterfeit and pirated products are mainly distributed through "open-air" markets, although they may often be found in reputable department stores.

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

When counterfeit or pirated goods are imported to Russia, Russian customs officers can assist right owners in stopping the infringement of their intellectual property rights provided the right owners applied to have the relevant rights entered into a special Customs Intellectual Property Register. Actions of customs officials *ex officio* in some cases are also

possible. The powers of customs officials are limited to copyrights and trademark rights (they do not cover inventions, utility models or designs). The maximum protection period for registered rights is two years, renewable at the request of the right owner.

Notably, parallel importation is considered as a trademark infringement in Russia, although recent trends in the court practice and relevant legislative initiatives are controversial in this respect. Moreover, since the spring of 2015, the Russian authorities have been pushing for parallel imports to be allowed in the near future, at least in relation to certain types of goods (such as pharmaceuticals, medical devices, automotive parts, cosmetics, perfumes, alcoholic beverages (except beer) and hygiene products). The possibility of abandoning the regional principle of exhaustion of trademark rights for these goods is now being discussed at the regional level of the Eurasian Economic Union.

Liability

Russian legislation provides for civil, administrative and criminal liability for the infringement of intellectual property rights. The sanctions depend on the amount of the counterfeit goods involved and on whether the individuals or legal entities involved are repeat offenders.

Civil penalties

The civil law route entitles the trademark owner to file a claim in court for the:

- termination of the infringement;
- seizure/destruction of the counterfeit goods (or removal of counterfeit signs or labels); and
- payment of compensatory damages or statutory liquidated damages (in an amount of RUB 10,000-5m (i. e from EUR 158-79,365[4]), or double the value of the infringing goods or of the right to use the infringed trademark under regular market conditions).

The Anti-piracy Law provides copyright and neighbouring rights owners with an efficient tool of copyright enforcement – web blocking injunctions. This law covers all copyrighted works and objects of neighbouring rights, except photographic works.

Sanctions under the Russian Code on Administrative Offences

The trademark infringer is administratively liable if the damage caused by the infringement is less than RUB 1.5m (EUR 23,810). Different sanctions apply to different infringements.

For example, since August 2013, the levels of the applicable fines for the production of fake products depend upon the scope of the infringement, which will be based on the value of the counterfeit goods seized.

The most serious sanctions apply to legal entities that produce or sell counterfeit goods. The fine that may be imposed in this case would be triple the value of the counterfeit goods seized, and in any event not less than RUB 40,000 (EUR 634). The counterfeit goods will also be confiscated.

[4] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

Sanctions under the Russian Criminal Code

If the damage caused by the infringement reaches or exceeds RUB 1.5m (EUR 23,810) or if the offender repeats the offence, he/she may be held criminally liable.

The unlawful use, disclosure or appropriation of an invention or patent that has caused significant damage to the author will result in a fine of up to RUB 200,000 (EUR 3,175) or equal to the offender's income for 18 months, or imprisonment for up to two years. Similar sanctions apply to infringement of copyright and to the sale of counterfeit goods.

When the offender is a legal entity, criminal sanctions will be applied against the entity's officials, as legal entities cannot be held criminally liable under Russian law. This may change in the future, as the introduction of corporate criminal liability is on the Russian Parliament's agenda.

IP Court

The IP Court, which is located in central Moscow, started its operations in July 2013 as part of the Russian commercial ("*arbitrazh*") court system.

The creation of the IP Court is aimed at (i) improving the specialisation of judges and increasing their professionalism in delivering IP-related judgments; and (ii) relieving the commercial courts of the great number of disputes between Rospatent and individual entrepreneurs or legal entities.

The IP Court reviews:

- as a court of first instance – challenges of regulatory and legal acts of Rospatent;
- as a court of first instance – claims for the invalidation of the registration of intellectual property rights and disputes over the ownership of intellectual property rights; and
- as a court of third instance (i.e. a second appeal or a cassation) – cases concerning the infringement of intellectual property rights between legal entities and/or individual entrepreneurs.

The cassation rulings of the IP Court can be further appealed to the Supreme Court of Russia. Other rulings are appealed against at the IP Court.

Analysis of the IP Court's activity shows that its launch was both an important and long-awaited development in Russian intellectual property practice. It has favourably affected intellectual property owners, since intellectual property disputes (including those associated with intellectual property prosecution issues) in Russia are reviewed by judges specialising in this area of law. Intellectual property practitioners note an increase in professionalism and a sound legal approach in IP-related judgments in Russia.

"Intellectual property practitioners have noted an increase in professionalism and a sound legal approach in IP-related judgments in Russia since the launch of the IP Court."

Personal data protection

General approach

In comparison to Western jurisdictions, data protection is an area of law that is still developing in Russia. Russia signed the 1981 Strasbourg Convention for the Protection of Individuals with regard to Automatic Processing of Personal Data (the "**Strasbourg Convention**") on 7 November 2001. It entered into force in Russia on 1 September 2013.

Key privacy legislation

The main law regulating this legal issue in Russia is the Federal Law No. 152-FZ "On Personal Data" (the "**Data Protection Law**"), and it was adopted in July 2006. A number of provisions of the Data Protection Law are based on the Strasbourg Convention.

The Data Protection Law provides a framework that is complemented by a number of regulations of the Russian Government, as well as by the orders of governmental authorities. In addition, some provisions of the Russian Labour Code and the Russian Code on Administrative Offences are also applicable.

The regulation of data protection in Russia gathered momentum between 2011 and 2012. In 2011, the Data Protection

Law was substantially amended, and new requirements for the protection of personal data processed in personal data information systems were approved by Russian Government Decree No. 1119 dated 1 November 2012.

In 2015, the Data Protection Law was amended to introduce new personal data localisation requirements, which were a hot topic within the business community. In addition, the so-called "right to be forgotten" was implemented in the Russian legislation and came into force in 2016.

That being said, the same legal gaps remain. For example, regulation that is constantly developing at an international level, such as whistleblowing, big data, BYOD[1] and social media, requires substantial development in Russia. Also, Russian law needs to be updated in line with developing technologies. Particular attention should be given to the regulation of personal data protection in relation to cloud technologies. Cloud services are increasingly popular within a variety of different business sectors, and the lack of relevant legislation might be an obstacle to their development in Russia.

Trends

It is anticipated that in 2017 the legislator's efforts will primarily be directed at increasing penalties for violations in the sphere of personal data. The relevant bill is expected to be adopted by the State Duma in the near future. Also, the law-enforcement practice for non-compliance with the data localisation requirements has developed in the past year. Sanctions imposed include entering the infringer in the register of offenders and blocking access to the infringer's resource.

At present, guidance on the practical implementation of the regulations on personal data protection remains underdeveloped, and compliance with these regulations often represents an issue for companies.

As processing the personal data of individuals represents an important part of their businesses, companies in the healthcare, insurance and banking industries, as well as those selling mass consumption goods, are at the highest risk of sanctions for violations.

Supervisory authority

The authority in charge of supervising compliance with personal data protection requirements is the Russian Federal Service for Supervision in the Sphere of Telecom, Information Technologies and Mass Communications ("**Roskomnadzor**"). Roskomnadzor is empowered to apply administrative sanctions to legal entities and individuals who fail to comply with the requirements of the Data Protection Law.

Scope of the Data Protection Law

The Data Protection Law defines, in particular, personal data and data processing. It also regulates the rights of data subjects, consent rules, cross-border data transfer and the obligations of data controllers.

[1] Bring your own device.

Personal data

Like the Strasbourg Convention, the Data Protection Law does not contain an exhaustive list of data which is deemed to be "personal data". Thus, what constitutes personal data must be assessed on a case-by-case basis. Personal data is defined as being any information referring directly or indirectly to an identified or identifiable individual. This individual is the data subject.

The Data Protection Law sets forth a special category of data: "sensitive personal data". This covers any information referring to a person's racial or ethnic origin, political opinions, religious or philosophical beliefs, personal health, sex life and criminal record. This concept corresponds with the Strasbourg Convention.

Data processing operations

The Data Protection Law applies to all personal data processing operations performed within Russia. However, in practice, Roskomnadzor has intervened to protect the rights of Russian data subjects in cases of personal data processing abroad. In recent years Roskomnadzor successfully blocked several websites hosted or managed from abroad that contained Russian citizens' personal data and continues this policy.

Personal data operations caught by the Data Protection Law include any processing, whether performed manually or automatically. They also include data collection, storage, recording, deletion, transfer, etc. Notably, the Data Protection Law applies when data processing is performed by Russian state bodies, local authorities, legal entities (including branches and representative offices of foreign legal entities) and individuals.

On the other hand, the Data Protection Law does not apply to personal data processing if it is performed:

— by individuals for their private needs,
— in accordance with the Russian legislation on archives;
— in relation to data qualified as a state secret under Russian law; or
— in accordance with Russian legislation on providing information relating to the courts of Russia.

Rights of the data subjects

Under the Data Protection Law a data subject is entitled to:

— request details of the processing of his/her personal data by a data controller (what data is being processed and why, etc.);
— revoke his/her consent to the data processing at any time;
— request, in certain cases, the rectification, blocking or deletion of his/her personal data; and/or
— be compensated for damage suffered (including moral damages).

Obtaining consent from the data subjects

Personal data may be processed (i) with the prior, voluntary, express and informed consent of the individual; or (ii) if the law expressly permits processing without the data subject's consent.

Consent can be given in any form provided that it is capable of being evidenced (except for when qualified consent is required by law, as described in the next paragraph). In practice, consent may be given orally, in writing, electronically or by implication. In any case, the data controller must always ensure that it can prove that consent was obtained.

Obtaining "qualified consent"

Consent must be obtained in the form of a written document ("**Qualified Consent**") in the following cases:

- the processing of sensitive personal and/or biometric personal data; and
- the cross-border transfer of personal data to countries which do not ensure an adequate level of protection of personal data (please see the *Cross-border transfer of personal data* section below).

Qualified Consent must be established in writing and contain, amongst other things, the following elements:

- name, address and passport details of the data subject;
- name and address of the personal data controller;
- purpose of the personal data processing;
- list of the personal data to be processed for which consent is given;
- list of the operations to be performed with the personal data and a general description of the methods to be used for personal data processing;
- the term during which the personal data will be processed and how consent can be withdrawn; and
- the data subject's signature (either hand written or electronic).

Cross-border transfer of personal data

The Data Protection Law distinguishes two types of cross-border data transfer:

- the transfer of data to countries with adequate protection of personal data ("**Safe Countries**"); and
- the transfer of data to countries without adequate protection of personal data ("**Unsafe Countries**").

Safe Countries comprise (i) signatories to the Strasbourg Convention; and (ii) countries that are not signatories to the Strasbourg Convention, but are included in the list contained in Roskomnadzor Order No. 274 dated 15 March 2013. In the near future, Roskomnadzor plans to amend the existing list, which consists of 17 countries.

The cross-border transfer of personal data to Safe Countries may be performed in accordance with the requirements of the Data Protection Law applicable to internal data transfer. As for the cross-border transfer to Unsafe Countries, this requires first obtaining the Qualified Consent of the data subject, except in cases expressly provided by the Data Protection Law.

Data controllers and data processors

The Data Protection Law defines the data controller as an entity (either a state agency, municipal authority or a legal entity) or individual who, independently

or together with others, organises the processing of and/or processes personal data, and determines the purposes and scope of personal data processing, the content of personal data which is to be processed, as well as actions performed with the personal data.

Main obligations for data controllers

The main obligations of the personal data controllers are to:

- notify Roskomnadzor of their intention to process personal data, except when an exception applies (please see the *Exceptions to the requirement to register with Roskomnadzor* section below). However, they can only start to process data after being entered on the register maintained by Roskomnadzor (see www.pd.rkn.gov.ru/operators-registry/operators-list/);
- ensure that the registration data in the register maintained by Roskomnadzor is up-to-date (and make the relevant applications in relation to any updates);
- ensure personal data security (please see the *Technical requirements* section below);
- develop and adopt the regulation on personal data, which should describe the procedure for processing personal data (including the list of data, the purposes of data processing, etc.);
- appoint a data protection officer who will be responsible for the organisation of data processing within the company;
- periodically perform the internal audit and assessment of the effectiveness of measures applied to protect personal data;
- retain control over such measures and the level of protection of personal data (in particular in cases where data processing is outsourced); and
- ensure that the recording, systemisation, accumulation, storage, clarification (updating, modification) and retrieval of Russian citizens' personal data is conducted in databases located within Russia (please see the *Localisation requirements* section below).

Exceptions to the requirement to register with Roskomnadzor

Notification is not required, in particular, to process personal data:

- of employees, when such data is processed by their employer for the purposes of realising their employment relations – employers must however comply with other data processing requirements provided by law (in particular those provided in the Data Protection Law as well as the Russian Labour Code);
- received by the data controller to conclude an agreement with the respective data subject, provided that personal data is not disclosed to third parties and is used for the sole purpose of fulfilling the agreement;
- of members of a public union or religious organisation processed by these unions and organisations for the purposes of their activity, provided that the personal data is not disclosed to third parties;
- made public by the data subject;
- which includes only names, surnames and patronymic names of the data subjects;

— which is necessary for the issue of a one-time pass to the data subject to enable access to the premises of the controller (or for similar purposes);
— which is included in state databases of personal data (including those created for the purposes of the protection of the security of state and public order);
— processed without the use of automatic processing methods; or
— processed in accordance with regulations on transport security.

Technical requirements

As regards security measures, the Data Protection Law has implemented the Strasbourg Convention's provisions on data security.

Personal data must be protected against unauthorised access, alteration, transfer, disclosure by transfer or deletion as well as damage and accidental destruction. In order to ensure the security of personal data, the data controller must, in particular:

— use technical devices certified by the competent Russian authorities and keep a record of the devices on which the personal data is stored;
— determine the level of damage which may be caused in the event of unauthorised processing of personal data; and
— establish rules relating to access to personal data, etc.

The Data Protection Law does not provide further details on the technical and organisational measures mentioned above, although some detailed requirements are provided in the relevant regulatory orders. The latest was adopted on 11 February 2013 regarding information that is not a state secret but is contained in the state information systems. In the absence of practical guidelines, implementing these requirements is problematic and, at times, impossible.

Localisation requirements

Since 1 September 2015, data controllers who collect personal data of Russian citizens have had to ensure that the recording, systemisation, accumulation, storage, clarification (updating, modification) and retrieval of Russian citizens' personal data are conducted only in databases located within Russia.

There are some exceptions to this requirement depending on the purpose of the personal data processing, such as:

— when achieving the objectives of international treaties or laws;
— when a data controller implements its statutory powers and duties;
— for the administration of justice;
— when public law entities and organisations that provide state and municipal services are fulfilling the corresponding functions; and
— when conducting the professional activities of journalists and/or the lawful activities of mass media, or scientific, literary or other creative activities provided that this does not violate a data subject's rights and legitimate interests.

When notifying Roskomnadzor of the commencement of processing of personal data, data controllers are

required to state the location of the database containing Russian citizens' personal data.

Outsourcing

Data controllers may outsource the processing of personal data. To do so they must enter into an agreement with a data processing service provider (a "**Technical Processor**"). The agreement must contain certain substantial conditions as set out by the Data Protection Law. Data controllers nevertheless remain responsible to data subjects for the fulfilment of their obligations.

The Technical Processor must ensure the confidentiality and protection of the personal data. In itself, technical processing does not require a specific licence. However, licences are needed to provide confidential information protection services and/or to develop specific software for the protection of confidential information (including personal data).

Liability

Administrative remedies and other sanctions

If it is found that a data controller has violated the requirements of the Data Protection Law, Roskomnadzor and/or the relevant court may:

— require the data controller to rectify the violation(s);
— issue a warning to the data controller; and/or
— impose any of the following fines on:

- individuals: RUB 300-500 (EUR 4.7-7.5[2]), to be increased to RUB 700-5,000 (EUR 11-79) from 1 July 2017;
- officials of legal entities: RUB 500-1,000 (EUR 7.5-16), to be increased to RUB 700-5,000 (EUR 11-79) from 1 July 2017;
- legal entities: RUB 5,000-10,000 (EUR 79-158), to be increased to RUB 15,000-75,000 (EUR 238-1,190) from 1 July 2017.

Judicial remedies

Data subjects can file for court action against a data controller, and in particular, to seek compensation for damage caused as a result of the illegal treatment of personal data.

Criminal law issues

In serious cases, unlawful data processing may also be deemed to amount to an illegal collection and distribution of information on the private life of a person constituting a private or family secret. Under the Russian Criminal Code, such violations are punishable with a fine, compulsory work or imprisonment.

Register of offenders

Since 1 September 2015, a personal data subject may apply to the court for measures to be taken to restrict access to information relating to him/her that is processed via the Internet in violation of the Data Protection Law.

In addition, the court decision will always provide for certain information about those

[2] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

who breach these rights to be recorded on a newly created Register of Violators of Personal Data Subjects' Rights. Relevant information will include in particular:

— the violator's domain names or other links to website pages on the Internet containing information unlawfully processed; and
— network addresses which enable the identification of such websites.

Notably, these measures may be applied against foreign entities that do not even have representative offices in Russia, but whose activity is targeted at the Russian market. Roskomnadzor is allowed to put a website of any foreign entity in the above register for non-compliance with localisation requirements, thus preventing access to the website from Russian IP addresses on the basis of a judgment.

Right to be forgotten

Since 1 January 2016, Russian Internet users have the right to demand that the online links to information about them be removed. Within ten days after the receipt of a relevant request from an individual, a provider must remove relevant link(s) or give reasons for its refusal to do so. This refusal may in any event be appealed by the individual at court.

Individuals are not entitled to request the removal of links to information about any criminal conviction, unless this conviction is overturned, annulled or spent, or any potential criminal offence, unless the relevant limitation period has expired.

"In 2016, the practice of Roskomnadzor widened and became stricter, which led to the blocking of several well-known websites. Increased penalties are expected in 2017."

Oil & gas

Alongside other natural resources, oil and gas remains the "flagship" and one of the most highly regulated sectors of the Russian economy. Its legal framework is centred around the regime of the Russian subsoil, its use and licensing.

Legislative framework

The key legislation framing up the legal regime of the Russian oil & gas industry are:

— Federal Law No. 2395-1 "On Subsoil" dated 21 February 1992 (the "**Subsoil Law**"); and
— Federal Law No. 225-FZ "On Production Sharing Agreements" dated 30 December 1995 (the "**PSA Law**").

The Subsoil Law serves as the cornerstone of the legislation on the use of subsoil in Russia and essentially regulates all key issues relating to geological surveying, exploration and production of natural resources, including oil and gas. The PSA Law specifically deals with the collaboration of Russian and foreign investors with the Russian state in geological surveying, exploration and production of natural resources under production sharing agreements.

Ownership and licensing

In Russia, all subsoil resources belong to the state until such time as they are extracted by a private investor pursuant to a duly granted licence. Following such extraction, the resources become the property of the licence holder.

The Federal Agency for Subsoil Use ("**Rosnedra**") is responsible for awarding licences in respect of any onshore blocks, except for so-called "strategic" blocks (as defined below). Licences to strategic blocks (including offshore) may only be awarded to investors pursuant to a decision of the Russian Government.

Restrictions on foreign investors

Strategic blocks

Licences

Under the Subsoil Law, foreign companies are prohibited from obtaining licences to use strategic blocks (blocks of federal significance), which include:

— those containing deposits with the following reserves, as evidenced by the state register of reserves:
  - recoverable oil reserves of 70m tons or more; or
  - gas reserves of 50bn cubic meters or more;
— subsoil plots located in the inland sea waters, territorial sea waters, or on the continental shelf of the Russian Federation (the so-called "offshore" blocks); and

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— subsoil plots that can only be developed using land used for defence or security purposes.

Unless otherwise provided by federal law, if a subsoil plot is included in the published list of subsoil blocks of federal significance, such subsoil block will retain this status indefinitely, notwithstanding any subsequent change to the criteria listed above.

The Russian Government may restrict the participation of Russian companies with direct or indirect foreign participation in an auction or tender for the right of subsoil use of a strategic block.

Acquisitions of Russian companies operating a strategic block

Under the so-called "strategic industries law"[1], when a foreign investor, a foreign state or an international organisation wishes to acquire a certain stake in a Russian company operating a strategic block, it must seek the approval of a special commission headed by the Chairman of the Russian Government (please see the *Strategic industries* section of the *Common forms of business structures for foreign investors* chapter on page 31).

Offshore blocks

Offshore blocks may only be licensed to a Russian company (i) that is more than 50% owned by the Russian state; and (ii) that has at least five years of offshore development experience.

[1] Federal Law No. 57-FZ "On Procedures for Foreign Investment in Companies of Strategic Significance for National Defence and Security of the Russian Federation" dated 29 April 2008.

Non-strategic blocks

Foreign companies are not disqualified by law from obtaining a licence in respect of a non-strategic block. However, in practice, foreign licence holders of a non-strategic block in Russia are rarely encountered. Therefore, foreign companies usually hold mineral rights to such blocks indirectly through their Russian subsidiaries.

Licences

Issue and term of licences

Mineral rights are documented by a licence which is essentially a permit issued by the Russian state to conduct a particular type of activity in respect of a given subsoil block. Subsoil licences do not give any surface rights to the territory on which the activity is to be carried out. Therefore subsoil users must obtain land use rights (usually under a lease) separately (please see the *Real estate and construction* chapter on page 121).

Licence for geological surveying licences

A licence for geological surveying is issued without a tender or auction:

— generally for up to five years;
— for up to seven years in respect of subsoil blocks located at least partially within certain Russian regions; and
— for up to ten years for offshore blocks.

The validity term of a geological surveying licence can be extended to enable the licence holder to complete the works under the licence.

Exploration and production licences

Exploration and production licences can be issued for the project life span. Their term can be extended provided that the licence holder has not breached any terms of the licence.

Exploration and production licences may only be issued through a tender or auction, except (i) where a holder of a geological surveying licence has made a commercial discovery; and (ii) in respect of some of the strategic blocks exempted by the Russian Government from the standard tender/auction procedure.

Combined licences

Combined licences cover geological surveying, exploration and production. They can be granted in respect of blocks with proven reserves that require substantial additional exploration.

The issue conditions and term of this type of licence are the same as for an exploration and production licence.

Transfer of licences

Since subsoil licences are acts of government, neither the licences themselves, nor any mineral rights thereunder, are transferable (including by way of sale, pledge or other disposal or encumbrance), except pursuant to special rules set out in the Subsoil Law.

These rules specifically permit the transfer in certain instances (except for the transfer of licences to strategic blocks to companies with foreign participation), including a transfer:

- within a group of companies (from a parent to a subsidiary, from a subsidiary to a parent and between subsidiaries as directed by the parent);
- following a merger or consolidation of the licence holder with another company;
- following a spin-off or split-off of a new company (from the licence holder);
- from a shareholder to a joint venture where the shareholder holds at least 50% of the equity interest (subject to certain conditions). Foreign investors often enter into joint ventures with Russian companies on this basis in order to obtain access to their subsoil licences.

Any such transfer requires a special decision of Rosnedra. Licences to strategic blocks may not be transferred to entities with foreign participation other than with the permission of the Russian Government.

For the above reasons, an "acquisition" of a Russian subsoil licence is mainly possible through a purchase of interest in the company holding the licence, or by forming a joint venture with the current licence holder to which the licence is subsequently transferred. In certain cases where obtaining an equity interest in the licence is not possible for regulatory or other reasons, contractual arrangements are put in place to give the foreign investor benefit of the licence.

PSAs

In Russia, production sharing agreements ("**PSAs**") have been aimed at providing investors with greater stability in the tax and regulatory aspects of subsoil development in the long run (please see the *Tax system* chapter on page 57 for an outline of the PSA tax regimes).

Since 2003, the PSA regime has been significantly curtailed. PSAs are only available if the block was put out to auction and the auction failed. This means that PSA is a second choice of the state, used where the relevant blocks are not of interest to subsoil users on standard licence terms. Hence, the most lucrative blocks are awarded on the basis of the general subsoil licensing regime.

"In Russia, all subsoil resources belong to the state until such time as they are extracted by a private investor pursuant to a duly granted licence."

Environment and energy efficiency

General approach

Over the past years, Russia has adopted complex environmental legislation that is generally in line with commonly accepted international standards. Its practical implementation, however, remains limited due to the general character of regulations and the inconsistent application of the corresponding penalties. This forces the legislator to develop the respective regulations further with clearer commitments and a more transparent system of liabilities and sanctions.

The development of Russian environmental legislation in close connection with other relevant sectors is also driven by the desire to incentivise Russian-based production and therefore support the so-called "localisation" trend.

For example, on 1 July 2015, a new Federal Law on industrial policy[1] (the "**Industrial Policy Law**") entered into force, setting out the main principles that govern new incentives intended to support the development of industrial production

[1] No. 488-FZ dated 31 December 2014.

in Russia. The new law includes specific support to be granted to projects involving the use of so-called "best available technologies" ("**BATs**"), which are closely linked to the implementation of environmentally efficient solutions.

Notwithstanding these incentives, investment in environmentally efficient technology in Russia remains low in comparison to developments in the rest of the world. This is due to regulatory constraints as well as to a lack of public awareness and understanding of environment and energy efficiency issues.

Legislation on environmental protection

The main federal law setting out the fundamental principles of environmental regulation in Russia is Federal Law No. 7-FZ dated 10 January 2002 "On Environmental Protection" (the "**Environmental Protection Law**"). The Environmental Protection Law provides for an overall framework for environmental management and imposes general requirements related to the construction and operation of various facilities that may be harmful to the environment.

Types of environmentally dangerous facilities

The Environmental Protection Law classifies facilities depending on the level of their environmental pollution and indicates which methods of state control are applicable to each category of facility, as per the table below.

The criteria to classify facilities are currently established by Governmental Decree No. 1029 dated 28 September 2015.

In addition to the forms of state control stated in the table below, facilities of categories I and II are subject to an obligation to meet the requirements of maximum allowable emission and discharge values.

Environmental fees relating to emissions, discharges and waste management

The environmental fees (pollution discharge fees) are calculated for each waste ingredient and pollution type depending on the level (volume or weight) of the danger they pose to the environment and public health.

Category of facility	Facility description (level of environmental pollution)	Method of state control
Category I	Environmentally dangerous facilities (generally relate to the industries of energy, heavy metallurgy, etc.)	Integrated activity permits (valid for seven years and applicable from 1 January 2019)
Category II	Facilities with moderate environmental impact	Declarations on environmental impact (valid for seven years and applicable from 1 January 2019)
Category III	Facilities with insignificant environmental impact	Industrial ecological control programmes (also applicable to categories I and II)
Category IV	Facilities with minimal environmental impact	None

The following activities are subject to environmental fees:

— the emission of polluting substances into atmospheric air by stationary sources;
— the discharge of polluting substances into bodies of water; and
— the storage and burial of production and consumption waste.

The corresponding environmental fee structure is calculated depending on the following elements:

— pollution within the permissible norms;
— pollution within the established limits (temporary agreed norms);
— application of an increasing coefficient for certain regions and environmental facilities based on ecological factor;
— application of an increasing coefficient for the discharge (x5); and
— application of an incentive system (reducing or increasing coefficients up to x100 depending on the application of environmentally friendly technologies and BATs, implementation of measures and plans aimed at reduction of pollution, etc.).

In particular, on 22 April 2016, a Governmental Decree setting the rates of the environmental fee relating to the management of production and consumption waste came into force[2]. Such environmental fee must be paid by goods manufacturers and importers who fully or partially fail to perform their waste management obligation by not meeting the established compulsory recycling targets[3]. The list of goods, in respect of which this environmental fee is payable, is quite broad and contains 36 types of goods including textiles, paper products, petroleum products, plastic products, batteries, computers and communications equipment. The environmental fee rates are set in Russian roubles for each ton of the product and/or packaging to be recycled and range, for example, from RUB 2,025 (EUR 32[4]) for accumulators to RUB 33,476 (EUR 531) for rechargeable batteries. The first environmental fee is payable by 15 April 2017 (for goods marketed in 2016).

Industrial policy legal framework

In line with the shift towards an import substitution model for the Russian economy, the Industrial Policy Law prioritises regional development and favours Russian-based manufacturers. This will likely force international investors to change their business models by favouring industrial production within Russia.

For example, the Industrial Policy Law introduced preferences for Russian-based production with priority for goods

[2] Russian Government Decree No. 284 dated 9 April 2016.

[3] The compulsory recycling targets are set and reviewed by the Federal Service for Supervision of Natural Resources. Since 2016, rather high compulsory recycling targets have been set, for instance, for (i) metal containers (20%); (ii) tyres and rubber products (15%); (iii) petroleum products, glass, batteries, bottles and plastic bottles (10%), and there is a risk that these targets will gradually increase.

[4] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

produced in Russia, including the odd-one-out principle for public procurements.

However, given the framework nature of the new Industrial Policy Law (meaning that other laws will need to be amended and complex secondary legislation adopted, including more than ten new Government Decrees), implementation of the regulatory framework may prove to be less straightforward in practice.

Special investment contracts

The Industrial Policy Law created a new contractual framework for projects in the industrial sector by introducing the concept of special investment contracts which may be concluded for a period of up to ten years. Under such contracts, investing companies that undertake to modernise existing industrial production facilities or set up new ones will be guaranteed long-term incentives by the Russian State.

What mainly distinguishes special investment contracts from other contractual arrangements formalising public-private partnerships is that the state does not contribute budgetary funds or state-owned property to the relevant project.

The cost of these state incentives is expected to be offset by the anticipated positive economic effect for the state in the form of new infrastructure, jobs and taxes being paid by new businesses.

Incentives

The Industrial Policy Law introduced the following incentives for the industrial sector:

- financial support in the form of various subsidies (for R&D expenditures and for the development of industrial infrastructure) to be granted on the basis of tenders, with priority being given to projects involving the use of BATs (please see next section for more details);
- refinancing of loans by the regions and access to long-term loan financing on competitive terms;
- various types of tax incentives, such as special incentives for projects that are to be implemented before 2025 and have been duly approved by the Russian Government; and
- creation of dedicated state funds to stimulate industrial development (by way of loans, grants, equity participation in project companies, leasing, etc.).

BATs

The concept of BATs is relatively new in Russian environmental law. It was introduced by Federal Law No. 219-FZ dated 21 July 2014 and will only enter into force to the full extent on 1 January 2020. Moreover, the implementation of this concept requires a vast number of secondary legislative acts to be adopted, including Government Decrees on the applicable list of industries, BAT qualification, BAT handbooks, etc.

The criteria for a technological process, technological method or equipment to be considered as a BAT generally include the following:

— minimal level of negative environmental impact;
— cost efficiency of implementation and operation;
— use of resource-efficient and energy efficient methods;
— implementation period; and
— industrial introduction at two or more enterprises impacting the environment in Russia.

A list of industry-specific BATs will be provided in specialised handbooks to be adopted by the end of 2017 (to be developed by a BAT Bureau created in January 2015 at Rosstandart).

In terms of applicable incentives, manufacturers who implement BATs can offset the amount they spend on improving environmental efficiency at their facilities against environmental fees for emissions and discharges. Moreover, companies shifting to BATs will be eligible for financial support through a special fund granting loans for modernisation purposes.

Energy efficiency

Russia offers unique opportunities for investors who want to implement projects in the energy efficiency ("**EE**") sphere and, more particularly, for representatives of countries that already possess experience of implementing EE and energy saving ("**ES**") technologies.

The main piece of legislation for EE matters is Federal Law No. 261-FZ "On Energy Saving and Energy Efficiency Increase and Amending Certain Legislative Acts of the Russian Federation" dated 23 November 2009 (the "**EE Law**"). It created a legislative, economic and organisational stimulus for ES and increasing EE.

To facilitate the efficient use of energy resources and to support and encourage ES, the EE Law provides for several groups of EE requirements applicable to various sectors, notably including the construction (EE requirements as to buildings, structures and installations) and the public sectors.

EE requirements for buildings, structures and installations

According to Russian EE rules, buildings, structures and installations (with only a few exceptions) must comply with the **obligatory requirements**. The Ministry of Housing and Building is responsible for setting these requirements under a special Decree adopted by the Government. The EE requirements are to be revised at least once every five years and should cover:

— the maximum energy consumption limits for buildings/structures;
— requirements relating to the architectural, functional, technological, construction, engineering and technical solutions influencing the EE of buildings/structures; and
— requirements relating to specific construction elements of buildings/structures, applicable equipment, technologies and materials.

These EE requirements on design, construction, reconstruction and major

repairs identify the parties (developers/builders/owners) responsible for implementation. Failure to comply with them may result in administrative liability[5].

EE requirements for public sector

One of the main priorities of the EE Law is the public sector. For instance, **energy consumption reduction targets** are set for publicly financed institutions. Moreover, companies with state participation and companies carrying out regulated types of activities are also obliged to adopt and implement programmes aimed at increasing EE.

All purchases by state or municipal clients must be made in accordance with ES and EE requirements fixed by the Ministry of Economic Development with the agreement of the Ministry of Energy, the Ministry of Industry and Trade, and the Federal Anti-monopoly Service. These requirements which concern the public procurement of certain types of goods, works and services whose performance requires considerable amounts of energy consumption, include, in particular:

— limits on energy consumption; and
— technological solutions influencing the EE of goods/works/services ordered.

The federal authorities referred to above must monitor and analyse the EE of publicly procured goods, works and services on an annual basis, and they must prepare annual proposals for reviewing the EE requirements for public procurement.

Energy service agreements

Energy service agreements are entered into between a customer (private or public sector) and a contractor to provide works and services aimed at ES and greater EE.

These agreements must include the following **mandatory conditions**: (i) the volume of ES guaranteed by the contractor; (ii) the expiration date (which may not be less than the term necessary to achieve the ES set by the agreement); and (iii) other mandatory conditions required under Russian legislation.

The **discretionary terms** of an energy service agreement may include, among other things (i) a clause setting the price for the works and services, subject to the results attained or expected to be attained upon the performance of the contract (e.g. the value of ESs); and (ii) a clause stipulating the obligation of the contractor to install and commission energy meters.

Clauses containing the essential elements of an energy service agreement may be included in contracts of sale and purchase, supply and transport of energy resources (except natural gas not used as motor fuel). Model terms of these contracts have been approved by the Ministry of Economic Development.

Energy audit mechanisms

The EE Law provides for two main types of energy audit: **voluntary** and **obligatory**.

[5] A "per breach" penalty for company officials at the rate of RUB 20,000-30,000 (EUR 317-476); for individual entrepreneurs – RUB 40,000-50,000 (EUR 634-794); for legal entities – RUB 500,000-600,000 (EUR 7,937-9,524).

As a general rule, energy audits are deemed voluntary, except under circumstances stipulated by the EE Law[6].

Energy audits may only be conducted by companies and individual entrepreneurs who are members of self-regulated organisations. The audit should be aimed at:

— collecting objective data on the volume of energy used;
— defining EE indicators;
— defining the ES potential and increasing EE; and
— developing and evaluating a list of possible programmes which target EE increase.

The results of the energy audits must be reflected in an **energy passport** comprising information on the presence of energy meters, the volume of energy used and the variations of such volumes, etc. Copies of energy passports are forwarded to the Ministry of Energy which is responsible for processing, systematising and analysing the information contained in these passports.

Incentives

In order to encourage private investors to participate in the EE programme, the EE Law proposes a range of financial/tax incentives.

Such incentives for commercial companies include, in particular:

— investment tax credits of up to 100% for companies investing in EE and ES technology;
— accelerated depreciation of assets categorised as having high EE or assets classified in the top EE class ("**Qualifying Assets**");
— three-year corporate property tax exemption on newly accounted for Qualifying Assets; and
— partial compensation of interest on loans granted by Russian banks for the purpose of investing in ES and increased EE technology.

"Russia offers unique opportunities for investors who want to implement projects in the energy efficiency sphere and, more particularly, for representatives of countries that already possess experience of implementing energy efficiency and energy saving technologies."

[6] According to art. 16 of the EE Law, an obligatory energy audit must be conducted, in particular, in respect of: (i) certain regulated companies; (ii) companies producing or transporting energy resources (oil, gas, etc.); (iii) companies investing in ES and EE and financed by federal, regional or local budgets; and (iv) companies with a yearly energy consumption exceeding the threshold set by the Government of the Russian Federation. The above companies must conduct energy audits at least once every five years.

Infrastructure and public private partnerships

General approach

Over the last decade, infrastructure and public private partnership ("**PPP**") projects have been of great interest to both the public sector and private investors.

Throughout 2014, 2015 and 2016, the number of PPP projects in Russia increased significantly (up to 1,000), mainly due to regional projects, especially in the communal utilities (including water, wastewater, waste management) and energy sectors.

On the one hand, projects like the Western High-Speed Diameter (one of the largest PPP projects in Europe), the M4 Toll Road, the Pulkovo Airport, the M-1 Odintsovo By-Pass and the Moscow-Saint Petersburg Toll Road projects have been successfully implemented over the last few years and are now operating well.

On the other hand, other high profile PPP projects have been postponed, suspended indefinitely, converted into public procurements or even cancelled (e.g. the Moscow-Saint Petersburg High-Speed Rail project (VSM-1), the Neva Water project, the Orlovsky Tunnel, the Palace of Arts on Vassilevsky Island, the Nadex, etc.).

That being said, there is still a healthy pipeline of infrastructure and PPP projects in Russia, including the PLATON project (fee collection from vehicles with more than 12 tons' capacity) and *TsKAD* (Central Ring Road) around Moscow, as well as many regional projects, which shows that the PPP sector is far from stagnant.

The adoption of a new federal law on PPP in July 2015, which had been debated for several years, became a significant milestone in the development of the PPP legal framework in Russia. The new federal PPP law is aimed at stimulating private investment in Russian infrastructure and its fine-tuning process to meet market requirements continued well into 2016.

Russian federal and regional authorities alike are becoming increasingly engaged in the development of PPP. At the federal level, Russia's lower chamber of Parliament (the State Duma) operates a PPP council. Several federal ministries also manage PPP councils, including the Ministry of Culture, the Ministry of Public Health, the Ministry for Economic Development and the Ministry for Construction and Communal Utilities (especially active in recent years). At the regional level, most regions have adopted their own PPP laws which will remain in effect

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until 2025, notwithstanding the adoption of the federal PPP law.

The trend over recent years shows that Russian authorities view the PPP sector as a leading area for infrastructure development and for attracting foreign investment.

Key PPP legislation

Federal PPP legislation

At the federal level, PPP projects are regulated by:

- Federal Law No. 224-FZ "On Public-Private Partnership, Municipal-Private Partnership in the Russian Federation and on Amendments to Certain Laws of the Russian Federation" dated 13 July 2015 (the "**PPP Law**");
- Federal Law No. 115-FZ "On Concession Agreements" dated 21 July 2005 (the "**Concession Law**");
- the Civil Code of the Russian Federation (the "**Civil Code**");
- the Land Code of the Russian Federation and laws regulating land;
- the Town Planning Code of the Russian Federation and laws regulating construction activity;
- the Budget Code of the Russian Federation (the "**Budget Code**") and associated regulations (e.g. the Governmental Decree No. 18 "On Procedure for Management of the Fund of National Welfare of the Russian Federation" dated 19 January 2008); and
- laws and decrees regulating specific industries (e.g. Federal Law No. 257-FZ "On Motorways" dated 8 November 2007).

PPP Law

The PPP Law was finally adopted in July 2015 and entered into force on 1 January 2016.

Generally, the PPP Law is aimed at unifying the principles regulating PPPs, defining the powers of public authorities when entering into partnerships with the private sector and specifying the procedures for entering into PPP arrangements.

In particular, the PPP Law includes the following provisions that help define, characterise and regulate PPPs:

- While the PPP Law does not set out an exhaustive list of forms for implementing PPP projects, it nevertheless allows for private ownership over the infrastructure facilities (thus enabling BOO, BOOT and other standard PPP models based on private ownership). This is in contrast to the Concession Law which requires the state to retain ownership over the infrastructure facilities.
- PPP is defined as the cooperation of a public partner (the Russian Federation, a region of the Russian Federation or a municipal authority) and a private partner (a Russian legal entity) on the basis of a PPP agreement entered into pursuant to a tender procedure and aimed at increasing the quality and availability of public services by attracting private investment.
- A PPP project may be initiated either by the public or the private partner; thus providing investors with a right to enter into a PPP agreement through a non-tender private initiative procedure.

— Major Russian state-controlled PPP market players (such as state banks VEB, Sberbank, VTB, Gazprombank and state investment funds such as the Russian Direct Investment Fund) are expressly prohibited from controlling more than 50% in a private partner. As a result, they will need to enter in consortia with private entities, including foreign investors, to finance PPP projects under the PPP Law.
— A PPP agreement is to be signed for a minimum of three years.
— PPP agreements regulated by the PPP Law are distinct from concession agreements, which are implemented on the basis of the Concession Law, and the PPP Law does not apply to concession agreements.
— The list of objects under PPP agreements (the "**Objects**") is exhaustive and includes, in particular, private roads, bridges, roadside utilities, public transportation (excluding metros), railways, pipelines, sea and river ports, airports, electricity generation plants, public health facilities, social infrastructure and, since 2016, agricultural and industrial facilities – which is expected to promote investments in those two sectors. Any infrastructure that cannot be held in private ownership according to Russian law is excluded from the scope of regulation of the PPP Law and may only be subject to a concession agreement.
— Under a PPP agreement, the private partner must (re)construct the Object fully or partially finance such (re)construction as well as operate and/or maintain the Object. The private partner may also be required to prepare the design documentation, and fully or partially finance the operation and/or maintenance of the Object.
— As a general rule, the private partner remains the owner of the Object after the PPP agreement expires provided, however, that the amount of financing provided by the private partner exceeds the financing of the public partner.
— If, during the effective term of a PPP agreement, the applicable federal, regional and/or local laws and regulations are amended and this adversely affects the private partner, then the parties must review the provisions of the PPP agreement in order to restore the economic balance initially envisaged by the parties, as well as the property and financial interests of the private partner.

The PPP Law also generally defines such matters as the preparation of the PPP agreement, the content of the tender documentation, the tender procedures and control over the implementation of PPP projects. Under the PPP Law, some aspects of the implementation of PPP projects are to be regulated by subordinate legislation adopted by the Russian Government.

Despite the adoption of the PPP Law, some important issues still remain unresolved.

First of all, the PPP Law only applies to the types of Objects expressly listed therein. For example, public utilities (heat, water and gas supply facilities) are not mentioned in the PPP Law and, thus, the relevant PPP projects can only be implemented under the Concession Law.

Secondly, the PPP Law provides limited guarantees for the return on investment and only for those projects where the activity of the private partner is regulated and prices (tariffs) are fixed by public authorities, such as in waste infrastructure projects.

Concession Law

The Concession Law was adopted in 2005. Since 2005, it has been repeatedly amended in order to make it more practical to implement concession projects in various sectors.

The Concession Law applies to certain types of infrastructure such as roads and roadside utilities, pipelines, sea and river ports, airports, public utilities, railways, subways and other public transportation, and public health facilities.

The Concession Law sets out the general rules for entering into concession agreements, including the tendering rules and the material terms that these agreements must include.

In July 2014, the legislator introduced new amendments to the Concession Law (which entered into force on 1 February 2015 and on 1 May 2015). These are primarily aimed at providing additional guarantees to the concessionaire. In particular, it is now possible for an investor to initiate a concession project and enter into a concession agreement without a tender through a private finance initiative. The grounds on which the grantor may decline the offer of an investor to enter into a concession agreement are limited by law. Furthermore, a change of concessionaire is now permitted before the conceded object is commissioned (subject, however, to the grantor's consent), which was previously expressly prohibited.

On 1 January 2017, long-debated amendments to the Concession Law entered into force to attract new investment projects in public utilities, including the heating, water and wastewater sectors.

Regional PPP legislation

Over the last decade, most Russian regions have adopted their own regional PPP laws in order to provide options for implementing PPP projects based on private ownership over the infrastructure objects. At the time, private ownership based schemes were either not provided for under federal law, or expressly prohibited by the Concession Law. The most notable example is the Saint Petersburg PPP law of 2006.

Significant regional projects implemented under the Saint Petersburg PPP law include the Western High-Speed Diameter and the Pulkovo Airport.

Whilst some other Russian regions have followed Saint Petersburg's example by adopting their own regional PPP laws, the adoption of the new federal PPP Law in July 2015 has significantly affected this practice.

Under the PPP Law (which is a federal law), the regional PPP laws may remain in force, but will have to be brought in line with provisions of the PPP Law by 2025.

In the meantime, all PPP projects implemented since 2016 are regulated

by the PPP Law and not regional PPP laws. As a result, regional PPP laws remain applicable until 2025 only for those PPP projects that were initiated before 2016.

Alternative schemes or quasi-PPP

Alternative PPP schemes have been implemented in the past on the basis of other legislation, such as the investment contracts of the Budget Code, long-term leases with investment undertakings governed by the Civil Code, and public-private joint ventures based on the privatisation legislation as well as general civil and corporate law principles. These alternative schemes have always been questionable from a legal perspective and some courts applied the Concession Law or the so-called "Public Procurement Law"[1] with respect to such contracts, resulting in the cancellation of many projects. With the new PPP Law that recently came into force, the legality of alternative schemes (i.e. those not provided for by the PPP Law or the Concession Law) is even more questionable, with the exception of those options expressly provided for by other federal legal acts.

For example, the Public Procurement Law provides for the conclusion of life cycle agreements for the (re)construction and operation of infrastructure. This option is widely used in Russia since Government Decree No. 1087 dated 28 November 2013 provides that life cycle agreements may be used for the design and construction of roads, ports, communal utilities, waste management, rail objects as well as for the procurement of aircrafts, vessels and transport vehicles, including railway and subway cars. For instance, in 2014, the city of Moscow signed such agreements for the financing, manufacturing and maintenance within the 30 year life cycle of more than 1,000 cars for Moscow's metro.

Another alternative quasi-PPP mechanism becoming increasingly popular is signing a special investment contract with the Russian Government which provides guarantees and other incentives. Several such contracts were signed with industrial investors in 2016, and more are soon to come. More investors are expected to be attracted by the decrease of the investment threshold for signing special investment contracts in various sectors from RUB 750m (EUR 11.9m[2]) to RUB 300m (EUR 4.76m), which is currently being discussed within the Russian Government.

Russian PPP environment

Governmental commitments

The Russian authorities have adopted several programmes aimed at modernising infrastructure, including roads, railways, airports, power generation plants, as well as healthcare and social infrastructure.

The Government provides support to private investors in order to attract foreign investment. For instance, it co-finances and/or guarantees PPP projects. It also provides tax credits and other benefits

[1] Federal Law No. 44-FZ "On the Contractual System in the Sphere of the Procurement of Goods, Works or Services for State and Municipal Needs" dated 5 April 2013.

[2] At the notional exchange rate of RUB 63 = EUR 1, as used for convenience throughout this guide.

prescribed for special economic zones (please see the relevant section of the *Tax system* chapter on page 58).

Transport

The Ministry of Transport is the state body responsible for the development and investment policy in all areas of transport. Each means of transport (roads, airports, railways, etc.) is under its supervision and is managed by a specialised entity, which, in turn, reports to the Ministry of Transport.

Some PPP transport projects which will be implemented within the coming years in Russia include:

- the Moscow-Kazan high-speed rail link;
- the transport project Europe – West China;
- sections 3 and 4 of the Central Ring Road ("*TsKAD*") in the Moscow Region;
- road bridges in the Moscow Region;
- a private parking system in Saint Petersburg;
- a private tram in Saint Petersburg;
- a high-speed tram in Samara;
- a railway link from Saint Petersburg's centre to Pulkovo airport;
- a bridge over the Ob River in Novosibirsk; and
- the modernisation of Moscow's three existing airports (Sheremetyevo, Domodedovo and Vnukovo), as well as of the airports of Vladivostok, Irkutsk, Omsk and Oryol (Yuzhny).

Roads

The state company Russian Highways is responsible for, amongst other things, PPP projects in relation to federal roads. Under its activity programme for 2010-2020, as approved by the Government[3], Russian Highways will be allocated RUB 1.45tn (EUR 23bn) to (re)construct highways, develop new international routes and create a chain of multifunctional road service zones through PPP projects. Most PPP projects are planned to be implemented under long-term investment as well as concession agreements and operation & maintenance contracts.

Railway

JSC Russian Railways ("**RZD**") operates a monopoly in the Russian railway sector and is currently implementing a number of investment projects, such as the reconstruction of the Baikal-Amur and Trans-Siberian railway links (with a planned state financing of about RUB 260bn (EUR 4.13bn) and the Moscow-Kazan High-Speed Rail project (VSM-2) (with state financing of about RUB 190bn (EUR 3bn)).

The value of the design contract for the Moscow-Kazan High-Speed Rail project executed by RZD and financed by the state amounts to RUB 20bn (EUR 317.5m). After design is completed, a concession agreement for the construction and operation of the Moscow-Kazan rail link will be entered into, which alongside state financing will require a significant amount of private investment. This project will become part of the bigger "Silk Road Initiative" aimed at creating a high-speed rail link between Europe and China through Russia.

[3] Order No. 2146-r of the Government of the Russian Federation dated 31 December 2009.

RZD's new president Oleg Belozerov, who was appointed in 2015, has significant experience in PPP transport projects (as he was previously the head of the Federal Road Agency). It is therefore expected that RZD will now more actively use PPP mechanisms for its infrastructure projects, including for the construction of new railway links and the modernisation of existing railway links.

Communal utilities

Utilities have long been a successful and receptive area for private investment and are thought to offer a great potential for foreign investment. As an inheritance from the Soviet Union, Russia received a large number of publicly-owned housing and utility facilities, most of which are in poor condition, requiring urgent repair or modernisation.

The Government – and especially the Federal Ministry for Construction and Communal Utilities which is implementing a programme for the development of communal utilities by 2020 – is actively attracting private investment into the communal utilities sector. It is ensuring long-term commitments of the state towards investors and tariffs to cover both capital and operational expenses, as well as guaranteed profit. In some sectors where tariffs cannot cover both capital and operational expenses (e.g. waste management), additional state financing is available.

It is expected that by 2020 more than 80% of communal utilities companies will be operated by private operators based on concession agreements and other contractual arrangements with the state.

Waste management

In 2015, significant amendments to the law on domestic and industrial waste[4] came into force to introduce producer and importer responsibility for the recycling of their goods and packaging. Producers and importers can choose to fulfil this obligation by organising their own recycling infrastructure (by themselves or jointly with others), by contracting with waste management companies or by paying environmental fees to the Russian budget. This new development is aimed at increasing investment in waste management infrastructure on a long-term basis through:

- private investment in waste recycling infrastructure from producers and importers;
- investment from regional waste management operators which will be selected through tenders and will be awarded contracts with regions for a term of at least ten years; and
- applying the environmental fees collected to build new infrastructure.

The Concession Law was also amended in 2015 to include industrial waste facilities as potential objects of concession agreements (previously only facilities operating with household waste could be the subject matter of concessions).

Large projects in the waste management sector have already been announced in the Moscow Region and Tatarstan (five waste treatment plants with a total capacity of 3m ton/year and an investment volume at EUR 2.3bn).

[4] Federal Law No. 278-FZ "On the Production and Consumption of Waste" dated 21 October 2013.

Power (heating and electricity sector)

Tariffs in the heating sector in Russia are traditionally relatively high compared to those in other sectors, while the equipment used is old and inefficient which makes this sector attractive for private investors, including foreign investors and producers of modern equipment. As a result, there are currently many regional projects of different scale (from one to several districts) being at various stages of implementation.

Many of the existing plants are combined heating and electricity producing plants, which generates an additional source of income. Those projects which use renewable energy sources such as biogas, biomass and peat can further benefit from green tariffs granted by the state as an incentive for renewable energy, which can be three to five times higher than the standard market price for electricity.

It is anticipated that electricity produced by waste treatment plants to be constructed in Russia (five plants that will produce about 70MW each) will also be considered as renewable energy.

Water and wastewater

Under the law on water supply and wastewater treatment[5], infrastructure in this field must remain within the public property domain. That means that the new PPP Law is not applicable to this type of facility and instruments available for private investment into this sector are limited to concession agreements, long-term lease agreements and other alternative PPP models where ownership is not transferred to the investor.

In 2013, the Russian President instructed[6] the Government to ensure the transfer, in the coming years, of the management of facilities of all inefficient municipal and state utility companies in the water and wastewater sector to private operators under concession agreements. This has already given rise to an increasing number of regional infrastructure projects, including concessions in Volgograd, Elista, Ryazan, Voronezh, Saratov and other cities, some with a population of more than one million.

Amendments to the Concession Law effective from 1 January 2017 are expected to increase the number of concession projects in water and wastewater infrastructure.

The most significant and long-awaited projects that are expected to be implemented in the future are a concession over Saint Petersburg Vodokanal and the partial privatisation of Mosvodokanal, which are the largest Russian communal utilities companies.

Housing

In 2015 a law on capital renovation of housing[7] introduced a new fee for capital renovation of apartment buildings which must be paid by all urban population. The fees are accumulated either by state controlled regional funds responsible for the renovation of housing in specific regions, or by municipalities which contract

[5] Federal Law No. 416-FZ dated 7 December 2011.

[6] Instruction of the Russian President No. Pr-1479 dated 6 July 2013.

[7] Federal Law No. 271-FZ dated 25 December 2012.

directly with companies for renovation works with respect to particular housing objects.

Healthcare sector

The recent decrease of budget financing for medical equipment in Russia (which made it more attractive to sell equipment than to create the respective infrastructure) and the market's tremendous potential are factors that are potentially conducive of opportunities for market players in the healthcare sector, and in particular for foreign equipment producers and investors that have know-how in the operation of healthcare facilities.

Investment in healthcare infrastructure is actively supported by the Government through long-term commitments to buy the services of private operators of infrastructure facilities through state medical funds, as well as through the implementation of life cycle agreements (please see the *Alternative schemes for quasi-PPP* section above).

There are already a number of successful healthcare infrastructure projects in Russia, some of which are implemented by foreign investors. More projects are about to take off in the near future in Moscow, Saint Petersburg, the Leningrad Region, Vologda, Udmurtia, Ulyanovsk, Novosibirsk, Samara and other major regions of Russia, including a number of nuclear medicine projects in major Russian cities such as Moscow, Rostov, Tomsk, etc.

Social infrastructure

PPP projects in social infrastructure are primarily initiated in the regions, such as the construction of retirement homes in the Moscow Region and in Buryatia, two sport facilities in the Nizhniy Novgorod Region, a college for gifted children in Omsk, education facilities in the Pushkinsky District of Saint Petersburg and the construction of 25 kindergartens in Tomsk.

The main obstacles for investors in this field are the return on investment and available guarantees, as project cash-flow is based on the availability of payments made by the relevant state authorities.

Financing

Funding market players

The state corporation Bank for Development and Foreign Economic Affairs ("**VEB**") is the Russian development bank primarily responsible for developing and funding PPP projects in Russia. VEB provides financing for projects deemed to be of primary importance to the Russian Government and which are carried out on a PPP basis, including those partially financed by the Investment Fund of the Russian Federation. There are a variety of methods which allow VEB to participate in infrastructure projects, such as providing guarantees, suretyships and loans, as well as through equity finance.

Investment and commercial banks involved in PPP projects remain Russian for the most part, with Sberbank, VTB and Gazprombank (all of which are state-owned) leading the way, together with Russian pension funds, such as Leader. However, the new PPP Law that came into force on 1 January 2016 (which prohibits state-controlled entities from having

more than 50% control over a private partner) will require these major state-owned players to enter in consortia with private investors to implement PPP projects. This recent development is expected to benefit private investors in Russian infrastructure in view of the stable market position and resources of these major players.

Legal issues

Some of the innovations that have been introduced within the framework of the Civil Code reform in 2015 are likely to bring the PPP legal environment in Russia one step closer to international best practices in the fields of PPP and project finance. These include concepts such as:

- options;
- independent guarantee;
- security deposits;
- pre-contractual liability;
- the reimbursement of losses arising from the occurrence of certain events specified in a contract (the intended equivalent of the English law concept of an "indemnity"); and
- representations (in Russian – "*zavereniya ob obstoyatelstvakh*") (an intended equivalent of "representations" and "warranties" as used in contracts under English law).

Despite the legal developments in 2015, further amendments to the current legislation are still required in order to address the concerns of financing organisations and increase the bankability of PPP projects in Russia.

Prospects for infrastructure projects

A number of PPP projects in various sectors have already been announced or are expected in the coming years.

Russian federal and regional authorities have recognised the need to develop infrastructure projects on a PPP basis. These authorities have already taken some positive steps to create the legal framework necessary to attract both foreign and domestic investors to this type of projects, such as the adoption of the PPP Law and amendments to Concession Law enabling private finance initiatives. These factors will likely help support current initiatives and possibly create new opportunities in the Russian infrastructure market.

"The adoption of a new federal law on PPP in July 2015, which had been debated for several years, became a significant milestone in the development of the PPP legal framework in Russia."

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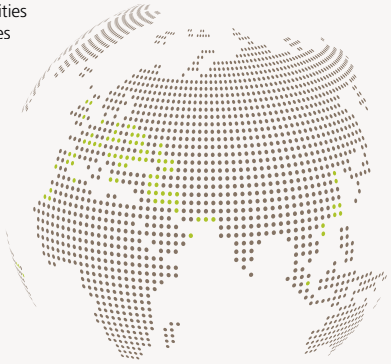

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