

RUSSIA

LEGAL DIGEST

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ARBITRATION/LITIGATION

Provisional injunctions accepted to carry out rulings of international courts of arbitration

The London Court of International Arbitration in 2009 began reviewing a case filed by Edimax Ltd. (the “**Plaintiff**”) against Russian businessman Shalva Chigirinsky (the “**Respondent**”) to recover payment on approximately USD 32 mln in debt owed by companies under the control of the Respondent, based on the Respondent’s personal guarantee of the companies. The Plaintiff also applied to the Arbitration Court of Moscow for interim relief in the form of an attachment over Chigirinsky’s Moscow apartment.

The Court has upheld a decision to forbid the unauthorised import of Evian mineral water.

The case reached the Supreme Arbitration Court of the Russian Federation (“**SAC**”), and the SAC confirmed that a Russian state arbitration court may seize the assets of individuals in Russia in order to secure the enforcement of an international arbitration award.

The Presidium of the SAC’s eventual ruling confirms that Russian commercial arbitration courts may provide interim relief, such as the possibility of seizing the property of an individual in Russia.

This case makes it possible to protect the rights of international creditors through interim proceedings in Russia and could attest to a change in the SAC’s approach.

[Presidium of the Supreme Arbitration Court Decree No. 17095/09, dated 20 April 2010; Federal Arbitration Court of the Moscow District Decree No. KG-A40/14698-09-B-N, dated 28 September 2010; Federal Arbitration Court of the Moscow District Decree No. KG-A40/14698-09-B-N, dated 29 October 2010]

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BANKING & FINANCE

Compulsory online sale of bankruptcy assets could impact secured lenders

Companies going through bankruptcy proceedings are now subject to the compulsory online sale of certain assets, particularly pledged ones. The Ministry of Economic Development clarified the practicalities of e-trading in an order (the “Order”) that came into force on 14 October as part of improvement of the bankruptcy law.

The practicalities cover:

- the procedure for holding a public sale in electronic form;
- the requirements for the e-trading platforms;
- the requirements for e-trading platform operators; and
- the procedure for confirming adherence to these requirements.

At present, only three trading companies are certified, while another nine operators are waiting to receive permission from the Ministry of Economic Development. The new system is having difficulties coping with the compulsory e-sale requirement because of the large number of liquidations.

As a result, the interests of secured lenders are adversely affected, and it is not clear how long it will take for the situation to normalise.

This element should therefore be taken into consideration within the context of secured lending arrangements currently under negotiation.

[Ministry of Economic Development of the Russian Federation Order No. 54, dated 15 February 2010, “On Approving the Procedure for Conducting Public Sales in Electronic Form when Selling the Property (Enterprises) of Debtors during Bankruptcy Proceedings and the Requirements for Electronic Trading Platforms and the Operators of Electronic Trading Platforms when Conducting

Public Trading in Electronic Form when Selling the Property (Enterprises) of Debtors during Bankruptcy Proceedings, as well as the Procedure for Confirming the Adherence of the Electronic Trading Platforms and Operators of the Electronic Trading Platforms to the Established Requirements”]

Money transfers by mobile phone under consideration

The State Duma, in the first reading on 6 October, approved a draft law that would make it possible for mobile phone subscribers to make money transfers from their mobile phone accounts via a credit institution without having to open a bank account. This would apply to sums up to RUB 15,000 (approx. EUR 350) transferred for non-commercial needs.

If the bill becomes law, telecoms operators who wish to offer this new service will have to negotiate and sign relevant agreements with credit institutions.

[Federal Draft Law No. 405325-5 “On Amending the Federal Law ‘On Banks and Banking Activity’” and article 45 of the Federal Law “On Communications”]

MICEX permits the trading of foreign-issued securities

When the MICEX Stock Exchange (“MICEX”) first began operations, only Russian securities could be listed and traded.

As of 18 October this year, securities of foreign issuers can be listed and traded on the MICEX. The listing rules have been amended as follows:

- a new type of foreign issuer is specified – foreign organisations (previously only the listing and trading of securities of international financial organisations and those of foreign countries was permitted);
- the list of requirements to authorise the trading of foreign issuers’ securities on the MICEX has been expanded and updated;

- the list and format of documents that foreign issuers are to present to the exchange has been amended; and
- foreign issuers are now required to present documents and information in Russian to the exchange.

The new rules are expected to have a positive effect on the continued development of Russia as a centre of international finance, thus supporting President Dmitry Medvedev’s numerous statements to this effect.

[Rules on listing, authorising and trading securities in ZAO FB MICEX, approved on 26 August 2010 by the Board of Directors of ZAO FB MICEX]

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CORPORATE

Draft bill on distribution of profits clears first hurdle

At present, implementing the decision of a general shareholders'/participants' meeting to pay dividends can prove to be problematic for various practical reasons, particularly when shareholders/participants have died or cannot be contacted because of a change in address.

As a result, dividends accumulate and joint-stock companies ("JSCs") and limited liability companies ("LLCs") cannot distribute these funds. In turn, this may have adverse consequences for companies, such as:

- having to pay profit tax on the unpaid funds if they are considered as taxable, undistributed profit; and
- JSCs not being able to reduce the share capital of the company until declared dividends have been paid in full.

Consequently, the draft bill to address these issues passed its first reading by the State Duma at the end of September 2010. It applies to both JSCs and LLCs, although it will predominantly affect JSCs that have large numbers of inactive minority shareholders who do not collect their dividends.

Once the new law comes into effect, JSCs and LLCs will have a single 60-day limit to pay declared dividends to their shareholders/participants.

Additionally, shareholders/participants will have five years to request that a company pay out dividends, although a company's charter can stipulate a longer period. Once the specified period has expired, shareholders/participants lose their right to claim the funds. At this point, the funds are considered to be net profit for the company to use at its own discretion.

No date has been set for the second reading of the draft law. Given the importance of this proposed legislation,

we would expect that the law is very likely to be adopted in the near future.

[Federal Draft Law No. 271397-5 "On Amending Several Legislative Acts as Part of Improving Corporate Management". Approved in the first reading by the State Duma on 21 September 2010]

Burden of information disclosure increases for securities issuers

The list of information that issuers are required to disclose will increase significantly from 7 April 2011. The following information will specifically have to be disclosed by issuers on their websites and be published by the news agencies authorised by the Federal Financial Markets Service ("FFMS"):

- details of the organisations controlling the issuers as well as the details of the organisations under the control of the issuers;
- details of cross-shareholdings of the subsidiaries and the issuer; and
- details of listed securities on the Russian and/or foreign stock markets.

Additionally, issuers will be required to disclose accounting as well as financial statements based on International Financial Reporting Standards (IFRS). Every issuer will be required to attach an auditor's report to the accounting and financial report.

Under certain conditions, JSCs with less than 500 shareholders may apply to the FFMS to obtain an individual exemption from certain disclosure requirements.

The provision for the exemption of issuers having to disclose information will come into force on 1 January 2011. Given this fact, it is time for securities issuers to think whether the exemption may be applicable to them.

[Federal Law No. 264-FZ, dated 4 October 2010, "On Amending the

Federal Law 'On the Securities Market' and Separate Legislative Acts of the Russian Federation" came into force on 8 October 2010]

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PHARMACEUTICALS

New procedures for import of medicines open to interpretation on clinical trials

The new “Rules for the Import of Pharmaceuticals for Medical Use on the Territory of the Russian Federation” (the “**Rules**”) have been in force since 29 September 2010.

The Rules stipulate that the import of pharmaceuticals into Russia must be licensed by the Ministry of Industry and Trade of the Russian Federation. In order to receive this licence, an applicant is required to present a certificate issued by the Federal Service for the Supervision of Health and Social Development (“**Roszdrazhnadzor**”).

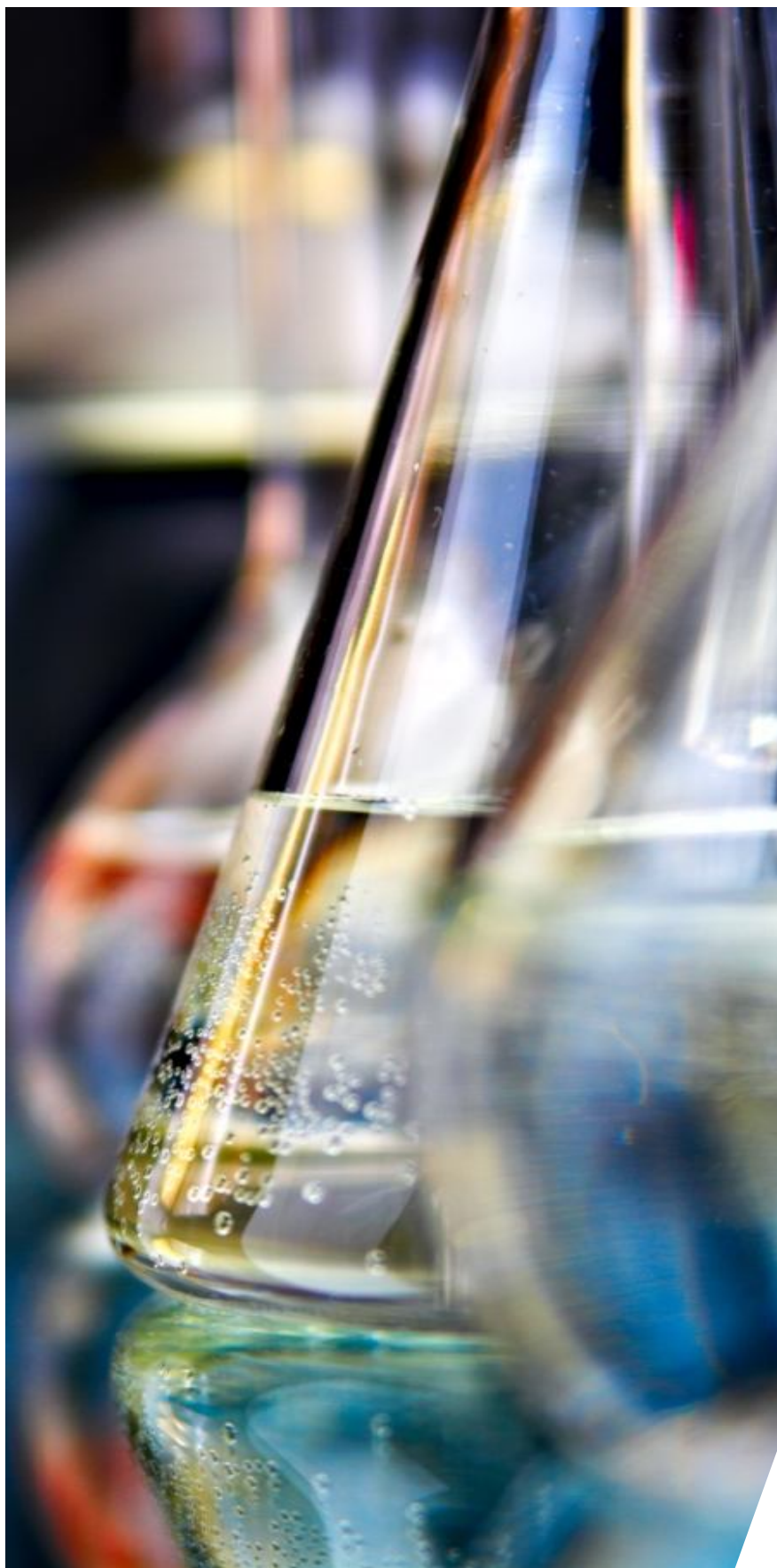
According to the wording of clause 11 of the Rules, an applicant must present a pharmaceutical licence or a pharmaceutical manufacturing licence in order to receive a certificate from Roszdrazhnadzor to import medicines intended to conduct clinical trials.

This wording does not permit the import of medicines intended to conduct clinical trials for contract research organisations (“**CROs**”) and the representative offices of companies sponsoring clinical trials, which have typically imported these goods into Russia.

However, according to a verbal explanation of the Ministry of Healthcare and Social Development, when CROs and the representative offices of companies sponsoring clinical trials import medicines to conduct clinical trials, applicants are not required to present a pharmaceutical licence or a pharmaceutical manufacturing licence.

[Government of the Russian Federation Decree No. 771, dated 29 September 2010, “On the Procedure for Importing Pharmaceuticals for Medical Use onto the Territory of the Russian Federation”]

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REAL ESTATE

Court rejects challenge to the General Plan for the development of Moscow

The adoption of the General Plan for the development of Moscow up to 2025 (the “**General Plan**”) gave rise to much public debate, and was subject to protests both during the drafting period and following its approval on 5 May 2010. Court proceedings challenging the General Plan reached the Moscow City Court, and, on 7 October 2010, the court ruled to uphold the validity of the General Plan.

It is important to note that the General Plan separates the City into development and stabilisation zones. Reconstruction, demolition and new construction will be permitted in the development zones, such as industrial areas and districts with dilapidated housing. In the stabilisation zones, in the City centre and historic districts, only extensive repairs and site improvement will be allowed.

To read the General Plan, please click here: <http://gpinfo.mka.mos.ru/>

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TAX

Russia and Cyprus strengthen tax treaty ties

Russia and Cyprus signed the Protocol on Amending the Double Tax Treaty (the "Protocol") on 7 October, which is set to come into force once both parties have ratified it.

The main changes are the following:

- Cypriot companies that have shares in Russian companies whose assets comprise 50% or more in real estate will pay Russian income tax on the sale of these shares. This amendment will come into force four years after the Protocol has been ratified;
- When the Russian authorities request that Cyprus provide specific information on companies and contracts, the Cypriot authorities cannot deny the request based solely on commercial and banking privileges. This amendment will come into force when Cyprus implements the necessary legislation;
- If Russian and Cypriot authorities ascertain that a company has been established solely to obtain tax concessions, the company will be denied this privilege. This amendment will come into force upon ratification of the Protocol.

As a result, the attractiveness of Cyprus as a tax and asset haven will likely decrease as the amendments in the Protocol are enacted.

[Order of the Government of the Russian Federation No. 1431-p, dated 2 September 2010, "On the Signing of the Protocol Amending the Double Tax Treaty between the Russian Federation and Cyprus, dated 5 December 1998"]

On-site tax audits likely to increase

The Federal Tax Service (the "FTS") has amended some of the publicly available criteria in its Strategy of on-site audits

planning that it uses to trigger an on-site audit.

The FTS' key criterion is a company's tax burden, which is calculated as a ratio of the amount of tax paid over turnover. The degree of the various applicable tax burden ratios depends on the type of business activity of the company.

The FTS has increased the ratios for all types of business activity, except for the extractive industry which means that the risk of on-site audits for most companies is now increased.

Companies showing a loss for more than two consecutive years are likely to be audited. The FTS has announced that, in view of the economic crisis, it will not take into account 2008 losses. However, to benefit from this, companies will have to:

- prove that the losses were caused by objective reasons; and
- document this to the satisfaction of the tax authorities.

As objective reasons and necessary documents are not defined by law, it will be difficult for companies to counter-argue with the tax authorities without expert advice.

[Federal Tax Service Order No. MMB-7-2/461@, dated 22 September 2010, "On Amending FTS Order No. MM-3-06/333@, dated 30 May 2007, "On Approving the Strategy of Planning On-site Audits"]

Accrued VAT remains problematic, especially when retaining ownership

The Ministry of Finance has stated that VAT on goods is accrued upon delivery, irrespective of whether the seller has retained ownership of the goods.

This contradicts the provisions of tax legislation that stipulate goods are VAT taxable only upon being sold, i.e. when ownership passes to the buyer. Companies are therefore faced with a dilemma:

- apply the tax authorities' prescriptions; or
- be prepared to defend their position in court against the tax authorities.

[Ministry of Finance Letter No. 03-07-11/379, dated 8 September 2010]

Supreme Arbitration Court sides with right to deduct VAT in subsequent tax periods

Current legislation allows a company to deduct VAT when the company enters goods on its books. In practice, companies typically deduct VAT in tax periods following the one in which the goods are actually received.

The tax authorities, however, oppose this practice. The FTS of Moscow clearly states that a company may deduct VAT on goods only within the quarter when the goods are booked¹.

Contrary to this position, the Supreme Arbitration Court has ruled that companies may continue to deduct VAT in tax periods other than the one in which goods are booked, basing this decision on the fact that the Russian Tax Code does not contain restrictive provisions on this matter.

Consequently, if the tax authorities claim that a company has to deduct VAT in the same period that the goods are received, the company should challenge the claim in court.

[Ruling of the Supreme Arbitration Court of the Russian Federation No. BAC-9902/10, dated 2 August 2010, and Decree of the Presidium of the Supreme Arbitration Court No. BAC-2217/10, dated 15 June 2010]

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¹ Letter No. 16-15/128328, dated 4 December 2009, and Letter No. 16-15/130771, dated 9 December 2009, of the FTS for Moscow

