RUSSIA

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1. What is the role played by the Russian government in regulating foreign direct investment?

Foreign direct investments in Russia are generally regulated by federal laws passed by the federal legislative body – the Federal Assembly. The main legal act in this sphere is the *Federal Law "On Foreign Investments in the Russian Federation" No. 160-FZ of 9 July 1999* (Investments Law). However, the Russian Government also plays a significant role. In particular, the Government:

- has a right of legislative initiative (*inter alia*, in the investments sphere) and uses this right very often;
- develops state supervision and control measures in respect of foreign investors;
- approves the list of high-priority investment projects, develops federal programs aimed at attracting foreign investments and ensures their fulfillment;
- issues other regulations in the sphere of direct foreign investments within its competence that shall not conflict with federal laws and international treaties entered into by Russia.

Efforts of various Russian federal executive bodies relating to attraction of foreign direct investments to the Russian economy are coordinated by the Ministry of Economic Development of the Russian Federation (paragraph 5.3.7 of the *Regulation on the Ministry of Economic Development of the Russian Federation approved by the Resolution of the Russian Government No. 437 of 5 June 2008*). In addition, there is the Governmental Commission for Control over Foreign Investments in the Russian Federation, headed by the Prime Minister, that is empowered to approve foreign direct investments in Russian strategic companies (see Questions 3 and 4 below for more detail).

Meanwhile, Russia is a federal state, and its regions may pass regional laws and acts of secondary legislation (the latter are usually issued by respective regional governments) regulating foreign investments that shall not intervene in issues that are described by the Russian Constitution as falling within the exclusive competence of the federation, and shall not conflict with federal laws. In addition, regional and municipal bodies within the framework of their powers may provide foreign investors with various privileges and guarantees, financial resources and other support measures (Art. 3(2) and 17 of the Investments Law).

In practice, special investments laws and other legal acts exist in many Russian regions. Typical instruments used by regional legislative bodies and governments to attract internal and foreign investments include:

- temporary or partial tax exemptions in respect of taxes payable to regional budgets;
- grace periods for payment of taxes payable to regional budgets;
- provision of investments tax credits;
- provision of guarantees by regional governments for the benefit of investors;
- discounted rental fees in respect of land plots and other property owned by respective Russian regions;
- support in creating favorable business infrastructure, in renting and purchasing land plots and other real estate objects owned by respective Russian regions.

2. What are the most common legal structures used by foreign investors when doing business in Russia?

Generally there are three main legal structures that the majority of foreign investors use when doing business in Russia. They are:

- Limited Liability Companies (LLC);
- branches; and
- representative offices (rep. office) of foreign companies.

The said structures may be registered/accredited for an unlimited term. There is also such legal structure as a joint stock company, but, historically, foreign investors tend to prefer LLCs when they establish subsidiaries in Russia, since Russian legislation applicable to LLCs is much more flexible as compared to the same governing joint stock companies.

It should be pointed out that branches and rep. offices are not separate legal entities. An establishing foreign company itself is a legal entity, while the branch or rep. office is a department of the foreign company situated in Russia. Meanwhile, the LLC is a fully-fledged legal entity separated from its mother-company or establishing natural person. The LLC may be established by any foreign natural person(s) and/or legal entity (entities). The LLC may have only one shareholder (natural person or legal entity). The only limitation is that the LLC may not be solely established by a company that, in turn, only has one shareholder (Art. 7(2) of the *Federal Law "On Limited Liability Companies" No. 14-FZ of 8 February 1998* (LLC Law)).

In addition, it is a foreign company that is responsible for all obligations of its rep. office or branch, while the LLC has its own rights and obligations. The foreign mother-company may become responsible/liable for acts of its Russian subsidiary only in circumstances strictly limited by applicable legislation.

The rep. office or branch does not have its own share capital and/or its own property; a foreign company provides its rep. office or branch with required funds and property. LLC has its own share capital (minimum amount prescribed by Art. 14(1) of the LLC Law – RUB 10,000) and may have its own property.

The key difference between the rep. office and the branch is the scope of their possible activities. In terms of strict compliance with applicable Russian legislation, the rep. office may only represent interests of the respective foreign company in Russia and be involved in advertising or marketing its products and/or services. Branches (unless otherwise directly limited by applicable legislation) may carry out in Russia those commercial activities that the respective foreign company carries out in its own jurisdiction (for example, sales, distribution, sale support services, and so on). LLCs may carry out in Russia the commercial activities that the mother-company carries out in its own jurisdiction or any other commercial activities, unless otherwise directly restricted by applicable legislation or the respective LLC's articles of association.

As to further restructuring of business, an investor should take into account that the rep. office or branch may be closed, but there is no possibility to reorganize (such as convert, merge or divide) or sell (transfer) the rep. office or branch. The LLC may be reorganized (through a merger, consolidation, split-up, spin-off or conversion) and/or liquidated. Shares in the LLC may be sold either to another participant (shareholder) or to a third party in the order specified in applicable laws and regulations.

3. Are there specific industries or parts of the economy in Russia which are barred or highly restricted for foreign investors?

There are a number of industries in Russia which are barred or restricted for foreign investors, as follows.

Restrictions based on national importance of certain strategic activities

The *Federal Law "On Foreign Investments in Companies of Strategic Importance for Defense and National Security" No. 57-FZ of 29 April 2008* (Strategic Investments Law) imposes certain limitations for foreign investors and groups of persons, including foreign investors owning shares in companies of strategic importance for defense and national security, as well as in respect of transactions leading to control over the such companies.

A company is deemed strategic, if it carries out business in one or more areas specified in Art. 6 of the Strategic Investments Law. The list of such activities includes, for instance, activities relating to nuclear materials and radioactive technologies, encryption and cryptographic means, military equipment, ammunition and weapons, space, communication services, geology and mining and aquatic biological resources production.

Restrictions on banking and insurance activities

The Russian legislation contains a limitation of foreign capital investments into the banking system according to the provisions of the *Federal Law "On Banks and Banking Activities" No. 395-1 of 2 December 1990* (Banking Law). Foreign banks may not open branches in Russia. The Bank of Russia (Central Bank) is entitled to impose additional requirements on Russian credit institutions (including banks) with foreign shareholders (for example, filing of additional reports, adoption of guidelines and presentation of a banking operations list). The special procedure for registration of credit institutions with foreign investments is prescribed by the Banking Law.

In addition, according to the *Law "On Organization of the Insurance Business in the Russian Federation" No. 4015-1 of 27 November 1992* there are certain limitations and restrictions relating to foreigners owning (or co-owning) Russian insurance companies and types of insurance products that may be offered by such Russian insurance companies to their clients.

Restrictions of the land legislation

According to the Art. 15(3) of the *Russian Land Code, Federal Law No. 136-FZ of 25 October 2001* foreign individuals and legal entities as well as stateless persons may not own land plots located at state border areas and other specially assigned territories of the Russian Federation.

Foreign individuals and legal entities, stateless persons, as well as Russian legal entities with a share of foreign individuals/legal entities or stateless persons in the share capital exceeding 50% may possess agricultural lands only on the basis of a lease (Art. 3 of the *Federal Law "On Turnover of Agricultural Lands" No. 101-FZ of 24 July 2002*).

Foreign individuals, legal entities, and stateless persons may not own land

plots located within the borders of Russian sea ports (Art. 28(2) of the *Federal Law "On Sea Ports in the Russian Federation and Amending Certain Laws of the Russian Federation" No. 261-FZ of 8 November 2007*).

Restrictions in the sphere of mass media

As a general rule, a foreign individual and legal entity, as well as a Russian legal entity with a foreign participatory interest in the share capital, are not entitled to establish Russian mass media, act as editorial bodies of mass media or broadcasting organizations according to the *Law "On Mass Media" No. 2124-1 of 27 December 1991*. Very strict limitations on direct/indirect owning of shares in Russian mass media by foreigners are also imposed by the above-mentioned law.

Restrictions in the sphere of air transport

Establishment in the Russian Federation of an aviation company with foreign investments is allowed, if:

- the share of the foreign capital does not exceed 49% of the share capital of the aviation company;
- its director is a Russian citizen; and
- the number of foreign citizens in the management body of the aviation company does not exceed 1/3 of the management body.

4. In merger and/or acquisition deals in Russia, what legal issues are most critical for foreign investors?

Russian law restricts the sale or change in control of what it refers to as strategic companies (see also Question 3 above). Transactions resulting in the establishment of control (over 50% of voting shares) over strategic companies by foreign investors are only allowed subject to prior approval of such transactions by the Governmental Commission for Control over Foreign Investments in the Russian Federation.

In addition, according to the *Federal Law "On Protection of Competition" No. 135-FZ of 26 July 2006* (Competition Law), a transaction aimed at acquisition of more than 25% shares in a joint stock company, more than 1/3 shares in a limited liability company, or acquisition of production assets of a legal entity with the value exceeding 20% of the total production assets value of that legal entity shall be subject to prior approval of the Federal Antimonopoly Service of the Russian Federation (FAS), if the specific criteria relating to the total assets value and (or) total turnover of the group companies are met. The prior approval shall be required if:

- the summarized amount of total balance value of the worldwide assets of the acquirer and the target company (and their groups of persons) is more than RUB 7 billion, and the summarized amount of total balance value of the worldwide assets of the target company (and its group of persons) is more than RUB 250 million; or
- the summarized amount of annual worldwide sales of the acquirer and the target company (and their groups of persons) is more than RUB 10 billion, and the summarized amount of total balance value of the worldwide assets of the target company (and its group of persons) is more than RUB 250 million.

According to Art. 31 of the Competition Law acquisition of shares in a Russian company, and/or acquisition of control over its parent company, is not subject to preliminary approval but is subject to post-completion notification of FAS if:

- the transaction is implemented by entities (parties of the transactions) which belong to the same group of persons, and the group of persons is formed on the basis of direct or indirect shareholding of more than 50% of voting shares (subsidiary, parent, sister companies);
- the transaction is implemented by entities which belong to the same group of persons, and information regarding the group of persons, which has not since then changed, has also been provided to the FAS no later than one month before the transaction (such information is to be disclosed at the official website of the FAS); or
- the transaction is implemented according to the legal acts of the Russian President or Government.

The term "group of persons" used for the purposes of calculating thresholds is defined very broadly in Art. 9 of the Competition Law and includes affiliates, parent companies and subsidiaries, companies controlled by other companies and companies with "cross-management" (that is, one person being a director in more than one company).

Failure to obtain a prior approval of the FAS where it is required may result in the imposition of an administrative penalty and (or) the invalidation of the respective transaction by a court.

The administrative penalty may be imposed within one year from the date of the transaction. The amount of administrative penalty (fine) may be in the range of RUB 150,000 to RUB 500,000.

A transaction executed without prior approval of the FAS may be invalidated in a court on the basis of a claim filed by the FAS, only if such transaction has led or may lead to restriction of competition. The FAS may request the transaction be declared invalid by a judgment within one year from the date when it knew or should have known of its execution.

5. Describe how the repatriation of profits, loans between related companies, or the return capital of foreign investors in Russia is/are structured.

Generally, the structure of repatriation of earnings and income (profits) out of Russia depends significantly on, and correlates with, applicable tax rules. Typical repatriation mechanisms include (without limitations):

- dividends;
- interests;
- return of investments in capital; and
- repatriation of income (profits) of a permanent establishment (PE).

As a general rule, foreign investors that are not Russian tax residents are taxed in Russia in respect of their income from the "Russian sources" (withholding tax, (WHT)). The taxable income includes mainly "passive income" such as

dividends and interests received from Russian companies, royalties paid for use of intellectual property in Russia. Services rendered by a foreign investor in Russia are not subject to taxation unless such activity forms a PE in Russia.

Dividends

The following WHT rates on dividends are applicable to foreign investors (Art. 284 of the *Russian Tax Code, Part 1 – Federal Law No. 146-FZ of 31 July 1998, Part 2 – Federal Law No. 117-FZ of 5 August 2000* (the Tax Code)):

- 15% for income received by a foreign investor in the form of dividends in respect of shares in Russian companies;
- various tax rates (for example, they are very often reduced to 10% or 5%; in certain cases even to 0%) and specific provisions concerning tax calculation and payment may be stipulated by relevant double tax treaties signed between Russia and other states (DTT).

Companies (and sometimes also depositaries, fiduciaries, brokers and certain other organizations) paying dividends act as tax agents of the taxpayer (investor) and shall withhold payable taxes in respect of dividends and remit them to the Russian budget. If a reduced WHT rate is applied according to a respective DTT, the foreign investor is obliged to provide the Russian tax agent with its residence confirmation.

Interests

The following WHT rates on interest are generally applicable to foreign investors (Art. 284 of the Tax Code):

- 20% for income received by a foreign investors in the form of interest on loans previously provided to Russian companies;
- various tax rates (for example, they are very often reduced to 10%, 7%, 5% or 0%) and specific provisions concerning tax calculation and payment may be stipulated by a relevant DTT.

A company paying interest on a debt due to a foreign investor acts as a tax agent and shall comply with the following provisions of the Tax Code.

The general rule (Art. 269 of the Tax Code) is that interest on debt obligations (loans, credits, and so on) is treated as expenses/income that shall be calculated in accordance with a rate actually established by the parties. However, there are some exceptions described below.

In case of a controlled transaction (that is subject to transfer pricing rules) interest on debt obligations is treated as expenses/income for the profit tax purposes, if the interest rate falls within the interval set forth in Art. 269(1.2) of the Tax Code.

In case the interest rate does not fall within the indicated interval, the expenses/income from such controlled transactions are subject to transfer pricing rules (Section V.1 of the Tax Code), if such transactions do not comply with the "arm's length" principle.

In addition, there are specific provisions regulating interest deductibility caps with respect to "thin capitalization" cases. According to Art. 269(2) of the Tax Code such cases include debt relations between:

- a foreign investor (parent company) with more than 20% participation in a subsidiary and such subsidiary;
- such subsidiary and a Russian company affiliated with a parent company (foreign investor); and
- such subsidiary and another party, where obligations of such subsidiary are secured (guaranteed) by an affiliated company or a parent company.

The Tax Code stipulates specific debt-to-equity ratio to be complied with constituting 12.5 for banks and leasing companies and 3 in other cases. If the actual ratio exceeds the indicated one, the Tax Code limits the deductibility of interest paid on a debt obligation.

Non-deductible interest is qualified as a dividend payment and is subject to 15% WHT under the Tax Code for interests paid to a foreign company, unless otherwise stipulated in the respective DTT.

Repatriation of investments

As a general rule, repatriation of initial contribution through sale of shares in Russian companies is tax free. Pursuant to Art. 309 of the Tax Code the income of foreign companies, that do not act through a PE in Russia, from sale of shares in Russian companies is taxed at source only if more than 50 % of the Russian company's assets consists of immovable property situated in Russia.

Repatriation of profits of the PE

Profits of a PE are subject to profit tax in Russia. However, there is no standalone branch profits tax in Russia, and any profits after taxation in Russia may be transferred to the head office without paying the WHT in respect of the profit.

In addition, it shall be noted that the PE definition used in the Tax Code differs from the same used in the OECD Model Tax Convention on Income and on Capital of 2014. In particular, the Tax Code excludes delivery of goods from the list of preparatory or auxiliary activities.

6. How do local employment laws and regulations in Russia affect the activities of foreign investors? Are there any specific laws which make it difficult to relocate workers to the country where the business is located, or to terminate workers already employed at the time of acquisition?

The main legal act governing labor relations in Russia is the *Russian Labor Code, Federal Law No. 197-FZ of 30 December 2001* (the Labor Code).

As a general rule, in Russia, employment agreements shall be entered into for an indefinite term. However, the Labor Code includes the limited list of grounds for entering into fixed term employment agreements (Art. 58 and 59 of the Labor Code).

A normal business week may not exceed 40 hours (Art. 91 of the Labor Code). Some categories of employees (for instance, minors, handicapped persons, employees involved in hazardous works) shall have shorter working hours, but they shall be paid as if they have normal working hours.

An employer is obliged to grant an annual paid leave to an employee. As a rule, the annual leave shall not be less than 28 calendar days (Art. 115 of

the Labor Code). A longer annual leave or additional leave shall be granted to specific categories of employees (employees performing hazardous work, employees with non-standard working day, employees working in Far North regions, and so on).

There are specific rules in Russia for hiring foreign employees. As a general rule, an employer should obtain a permit to employ foreign employees. In order to do that the employer should be able to explain to competent authorities why Russian nationals cannot be hired to do this job. In addition, employers may hire foreign employees only within the limits of annual quotas set by the Russian Government. As a standalone obligation, the majority of foreign employees shall have a personal work permit to work in Russia. These issues are mainly governed by the *Federal Law "On Legal Status of Foreign Citizens in the Russian Federation" No. 115-FZ of 25 July 2002*.

The law stipulates the simplified procedure of obtaining a permit for a highly qualified foreign employee who meets the statutory requirements to a salary amount, as well as for foreign employees working on certain territories of Russia. Citizens of certain states that have special agreements with Russia are not required to have a work permit (for instance, citizens of the Eurasian Economic Union member states: Belarus, Kazakhstan, Armenia, and Kyrgyzstan).

When it comes to termination of an employment agreement, an employer should remember that the exhaustive list of reasons (grounds) for dismissal is specified in Chapter 13 and some provisions of the Labor Code. Meanwhile, as a general rule, an employment agreement itself may not indicate any additional reasons for a dismissal.

The Labor Code provides for several groups of grounds for termination of an employment agreement:

- at the initiative of an employee;
- at the initiative of an employer;
- upon mutual consent of the parties; and
- in circumstances beyond the reasonable control of the parties.

An employer may terminate an employment agreement with a chief executive officer (director) at any moment without specifying any reasons. If the termination does not relate to a willful misconduct of the CEO, the employer shall reimburse the CEO for not less than three monthly average wages. An employment agreement may stipulate a greater amount of compensation (Art. 278 and 279 of the Labor Code).

An employer may terminate an employment agreement due to a staff reduction (which falls within the group of grounds for termination "at the initiative of an employer"). In such circumstances, employees shall be given two months prior written notice, offered vacancies, including lower-ranking and lower paid vacancies and paid the compensation for one to six average monthly wages (the latter is for the Far North regions). There are certain categories of employees who may not be dismissed in the course of a downsizing (for instance, pregnant women, women with children under a certain age and other employees with family duties).

Agency work (work carried out by employees following instructions of their official employer for the benefit and under the direction and control of an individual or a legal entity other than the employer) is prohibited in Russia. On the other hand, personnel leasing is permitted under certain circumstances and may be performed by:

- private employment agencies; and
- other legal entities (including those owned by foreigners), if they direct employees to their affiliated persons or to other legal entities specified by law.

7. Are there any unique aspects to intellectual property protection in Russia of particular importance to foreign investors?

The legislation on intellectual property has been actively developing in Russia. It has become easier for the right holders to protect their exclusive rights due to efficient mechanisms established by law.

Depending on the nature of a particular IP object, the law provides for different ways of providing protection.

Objects of copyright, such as works of design, graphics, advertising claims and such like, are protected due to the fact of their creation; their registration or observance of any other formalities are not required (Art. 1259(4) of the *Russian Civil Code, Part 1 – Federal Law No. 51-FZ of 30 November 1994, Part 2 – Federal Law No. 14-FZ of 26 January 1996, Part 3 – Federal Law No. 146-FZ of 26 November 2001, Part 4 – Federal Law No. 230-FZ of 18 December 2006* (the Civil Code)).

According to Art. 1353 of the Civil Code, technical solutions can be protected by patents for inventions or utility models. The external shape of a product may also be protected by a patent for an industrial design. To ensure protection such objects should be registered with the Federal Service on Intellectual Property (Rospatent) or certified by patents valid in the Russian Federation in accordance with international treaties entered into by the Russian Federation (for example, the Patent Cooperation Treaty of 1970 or the Eurasian Patent Convention of 1994).

The law in Russia also provides for the possibility of protecting almost any kind of information in the area of science and technology in the form of know-how (Chapter 75 of the Civil Code). The information eligible for protection should have current or potential commercial value by virtue of being unknown to third parties. Know-how protection is deemed established after a range of measures specified in the law have been taken by the owner of information (such as limiting access to the information by implementing procedures for handling the same, listing the individuals receiving access to the information and so on). The protection granted to know-how is similar to patent protection. However, it is not required to register know-how with state authorities. Therefore, the exclusive right to know-how originates as soon as the respective right holder establishes the protection regime and remains valid as long as the confidentiality of the information constituting know-how is maintained. As soon as the respective information is no longer confidential, that is, it becomes publicly available, the exclusive right of the right holder shall lapse.

Due to Art. 1479 of the Civil Code trademarks enjoy legal protection in the territory of Russia, if registered with Rospatent or pursuant to an international agreement effective in Russia (for example, the Madrid Agreement Concerning the International Registration of Marks of 1891 and Protocol Relating to the Madrid Agreement of 1996, Paris Convention for the Protection of Industrial Property of 1883).

If a third party infringes someone's exclusive right, the right holder, in order to exercise its right to remedy, will have to prove the existence of the respective IP right, as well as evidence of a breach of such right (unauthorized use of the IP) by a third party. For example, trademark certificates, patents, agreements, correspondence or witness statements may be presented as proof. Besides, a special certificate of registration and deposit of the work may prove one's copyright as of a certain date. Such registration is not mandatory, but it can be of help when bringing a matter before the court.

In order to do business in Russia under the brand of a foreign company, or use industrial property objects protected in Russia, it is necessary to enter into special agreements (licensing, franchising). The right to use the results of intellectual activity and means of individualization on the basis of such agreements is subject to registration with Rospatent (Art. 1235(2) of the Civil Code).

8. Are there specific laws in Russia regulating data exchange and privacy?

In Russia there is a system of detailed specific laws regulating data exchange and privacy that, *inter alia*, include:

- *Federal Law "On Information, Information Technologies and Protection of Information" No. 149-FZ of 27 July 2006*. It provides general legal guidelines for searching, collecting, transferring production and dissemination of information, use of information technologies and protection of information.
- *Federal Law "On Personal Data" No. 152-FZ of 27 July 2006* (Personal Data Law). This law was originally passed to implement the Convention for the Protection of Individuals with regard to Automatic Processing of Personal Data of 1981, but its current version is much more detailed compared to the above-mentioned convention. It governs principles of, and terms for, personal data processing, rights and obligations of personal data subjects and operators, state control and supervision over personal data processing.
- *Federal Law "On Commercial Secret" No. 98-FZ of 29 July 2004*. The law describes what information shall be treated as a commercial secret and provides legal guidelines for its protection.

Some other (general) legal acts shall be also taken into consideration. In particular, in accordance with Art. 23(1) of the *Constitution of the Russian Federation of 12 December 1993* everyone has the right to the inviolability of private life, personal, and family secrets.

Moreover, the inviolability of private life, personal, and family secrets is mentioned in Art. 150(1) of the Civil Code among nonmaterial values safeguarded by the Civil Code. The latest edition of the Civil Code has also been supplemented

with a new Art. 152.2 specifically devoted to the protection of private life, while Art. 152.1 of the Civil Code governs protection of a personal image.

Protection of the right to the inviolability of private life, personal, and family secrets is also governed through certain other legal concepts introduced by various legislative acts, including secrecy of adoption (Art. 139 of the *Family Code of the Russian Federation, Federal Law No. 223-FZ of 29 December 1995*), medical secrecy (Art. 13 of the *Federal Law "On Basics of the Legislation of the Russian Federation on the Citizens' Health Protection" No. 323-FZ of 21 November 2011*), secrecy of confession (Art. 3(7) of the *Federal Law "On Freedom of Conscience and Religion Unions" No. 125-FZ of 26 September 1997*), secrecy of will (Art. 1123 of the Civil Code), attorney-client privilege (Art. 8 of the *Federal Law "On Advocatory Activities and Advocacy in the Russian Federation" No. 63-FZ of 31 May 2002*), etc.

Certain acts relating to privacy violations are recognized as administrative offences by the *Russian Code on Administrative Offences, Federal Law No. 195-FZ of 30 December 2001* and as crimes by the *Russian Criminal Code, Federal Law No. 63-FZ of 13 June 1996*.

9. What is the best strategy for acquiring real estate and other tangible property in Russia? Is it different for foreign investors?

In general the simplest strategy for acquiring tangible and/or intangible property is a direct acquisition. Such a strategy allows the foreign investor to refrain from conducting a full scale due diligence of a special company holding the respective property and will mitigate certain corporate risks relating to owning such company. It should, however, be noted that pre-transactional due diligence of the seller's ownership title to property is always highly recommended. A sale and purchase agreement regarding Russian real estate shall be governed exclusively by the Russian law due to applicable Russian conflict of laws rules, and this may be treated by some investors as a potential disadvantage of such strategy in respect of immovable property.

However, if the investor's intention is to acquire all (or a huge part of) property owned by a particular company, and the respective property complex includes many objects, the best strategy would be an acquisition of the company itself. If such a strategy is chosen, a pre-transactional full-scale due diligence of the respective company is of great importance. This should typically cover (apart from a check of the ownership title) such aspects as corporate issues, tax issues, litigation issues and so on.

The above strategies, in most cases, may be applied equally to domestic and foreign investors. However, there are certain limitations for direct/indirect acquisition of certain types of property by foreign investors. For example, a direct/indirect acquisition of a strategic company is subject to prior approval of such transaction by competent public authorities (see Questions 3 and 4 for more detail). There are also certain limitations relating to the purchase of land plots (located near state borders, agricultural lands, land plots located within the borders of Russian sea ports) by foreigners (see Question 3 for more detail).

Besides, there are general limitations applicable to all private investors (Russian and foreign). For example, certain types of land plots cannot be owned by a private investor (legal entity or individual) – lands of natural parks, forest areas, lands relating to national monuments, and so on.

Information on titles over immovable property and related transactions are subject to reflection (registration) in a special unified state register that is publicly available. It is a requirement to register transfer of title to immovable property from a seller to a buyer to affect validity and enforceability of such transfer. Mortgages, long-term leases and some other encumbrances created in respect of real estate objects are also subject to registration.

10. If a foreign investor in Russia decides to work with a local representative or distributor, what are the potential risks?

The major risks lie in the field of Russian antitrust rules. Potential supplier and distributor should draft a distribution agreement with due care to make sure that no Russian antitrust laws and regulations (in particular, the Competition Law) will be, or may be, potentially violated. Various "exclusivity" and "non-compete" clauses are typically the most vulnerable in this respect. This aspect is especially important for foreign investors, since Russian antitrust prohibitions are of super mandatory nature, which means that they apply even if a respective contract is governed by laws of a jurisdiction other than Russia, but affects the Russian market.

Another challenge is that distributorship contracts are not specifically regulated by Russian civil and commercial legislation. Russian court practice and legal science are not uniform in respect of this issue. There are at least two main points of view that should be taken into consideration prior to drafting a distribution agreement governed by Russian law:

- A distribution agreement should be treated as a "mixed" agreement, effectively combining various features of agreements that have special rules applicable to them prescribed by the Civil Code (supply of goods agreement, agreement on rendering paid services and other agreements depending on the exact terms and conditions of a particular distribution agreement). According to such an approach, mandatory rules of the Civil Code applicable to the respective "defined" agreements will apply to the distribution agreement as well.
- A distribution agreement is a so-called "non-defined" agreement. This means that only general rules of the Russian Civil Code regulating all commercial contracts shall apply to distribution agreements.

11. When resolving disputes, are foreign investors in Russia better advised to rely on local courts or to use arbitration for the resolution of commercial disputes?

In order to resolve commercial disputes arising in the course of doing business in Russia, foreign investors in respective dispute resolution clauses of commercial

agreements with trans-border elements typically choose either international commercial arbitration or the system of Russian state courts. However, it should be noted that sometimes there is actually no choice, since according to applicable provisions of Russian law, disputes of certain categories fall within the exclusive jurisdiction of Russian state courts (for instance, disputes relating to rights to real estate objects located in Russia, bankruptcy claims against Russian companies, certain corporate disputes relating to Russian companies, and so on; see Art. 38 of the *Russian Code of Commercial (Arbitrazh) Procedure, Federal Law No. 95-FZ of 24 July 2002*.

It is also theoretically possible to indicate in a contract a state court of a foreign jurisdiction as a body that shall resolve disputes between parties. But due to existing Russian legislation and court practice there may be substantial problems with recognition and enforcement of a judgment of a foreign state court in Russia, unless there is an international treaty between Russia and the respective state on mutual recognition and enforcement of judgments.

Arbitral awards made in the territory of the Russian Federation and abroad may be recognized and enforced in Russia, since the latter is a party to the UN Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958.

As an alternative to the international commercial arbitration (and as indicated above, sometimes without any alternative), commercial disputes may be submitted to the Russian state courts. In Russia there is a special system of state courts created to resolve commercial disputes – commercial (*arbitrazh*) courts.

Commercial (*arbitrazh*) courts are located in the territory of almost each Russian region (federation subject). Each commercial (*arbitrazh*) court typically has special judicial divisions focused on resolving certain categories of disputes (corporate disputes, disputes arising out of investment relations, disputes relating to the construction, insurance, and so on).

We may note the following advantages of Russian commercial (*arbitrazh*) courts:

- comparatively low (as compared to international arbitration) legal costs, expenses and disbursements;
- electronic document management system that allows to monitor the progress of the case, submit documents to the court in electronic form, get access to the audio records of court hearings;
- possibility of participating in hearings by video conference; and
- very detailed and codified dispute resolution procedure.

12. What are the three most important legal issues for a foreign investor to understand before doing business in Russia?

1) Regional variations of the legal environment regarding investments

A foreign investor should be aware that the investments legal environment in Russia varies from one region to another. This is caused by the federal nature of the Russian state, in which regional public authorities are empowered to

pass regional legal acts aimed at attracting foreign investors to their particular regions (see Question 1 above for more details), and by efforts of the federal public authorities aimed at boosting economic development of particular regions and cities. For instance, a number of special economic zones of different types and free ports are created in certain Russian regions, residents (investors) of which enjoy various privileges and exemptions (see the *Federal Law "On Special Economic Zones in the Russian Federation" No. 116-FZ of 22 July 2005*, federal laws devoted to specific special economic zones, the *Federal Law "On Vladivostok Free Port" No. 212-FZ of 13 July 2015*, and so on). Therefore, it would be recommended that a potential new investor conduct research of investments legal environment of various Russian regions and cities prior to entering the Russian market to make sure that a "right" place for investments is found.

2) Russian personal data protection rules

Relatively new Russian data protection rules should the taken into consideration and reviewed with due care, especially by foreign investors aiming at the consumer market and anticipating interaction with many Russian citizens (individuals). In particular, a number of amendments were introduced in the Personal Data Law, according to which, starting from 1 September 2015, operators processing personal data are obliged to initially store and process personal data of Russian citizens using databases located in Russia (Art. 18(5) of the Personal Data Law). Cross border transfer of such personal data is still possible, but only after the data is firstly processed using a primary database located in Russia and subject to strict compliance with applicable Russian rules for cross border personal data transfer (Art. 12 of the Personal Data Law).

3) Employment and migration laws regarding senior foreign staff

It is important to understand that, under Russian law, a chief executive officer (director) of a Russian company (including Russian subsidiaries of foreign companies) and the head of a branch or rep. office of a foreign company in Russia are treated not only as officers authorized to act on behalf of the company, but also as employees (Chapter 43 of the Labor Code). It effectively means, *inter alia*, that if a foreign citizen is appointed the CEO/head, he or she, as a general rule, shall have a valid work permit issued in accordance with applicable Russian migration rules (*Federal Law "On Legal Status of Foreign Citizens in the Russian Federation" No. 115-FZ of 25 July 2002*). One of the problems here is that the subsidiary / branch / rep. office in most cases shall itself apply for getting a work permit for a foreign citizen and/or for getting a permit to employ foreign citizens, and such steps may not be taken before the respective subsidiary / branch / rep. office is formally registered in Russia. Therefore, if a foreign investor is willing to open a new Russian subsidiary / branch / rep. office and appoint a foreigner its CEO/head, in most cases such investor will have to find a reliable individual who is a Russian national or may work in Russia without getting a work permit on legal grounds that will act as a first (provisional) CEO/head until all migration formalities are fulfilled in respect of appointing a foreigner.

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