

Russia

Andrey Zelenin

Lidings Law Firm

Transfer of real estate

1 Legal system

How would you explain your jurisdiction's legal system to an investor?

Russian law is a civil law system. Therefore, the main regulations in the area of business and economic relations (including real estate) are stipulated in the Civil Code of the Russian Federation, which consists of four parts:

- part 1 (adopted in 1994) – general provisions, ownership, obligations;
- part 2 (adopted in 1998) – contracts;
- part 3 (adopted in 2001) – inheritance and international private law; and
- part 4 (adopted in 2007) – intellectual property.

Real estate issues are mainly covered in part 1 (section 2) and in part 2 (chapter 30 'sale' and chapter 34 'lease'). Part 3 contains provisions on conflict of laws regulations applicable when one party in a transaction is foreign or the object of the transaction is located outside the Russian Federation.

Additionally, relations between foreign investors and Russian legal entities, citizens, state authorities and institutions, with respect to issues related to real estate transactions, the registration of real estate, and the state registration of rights to real estate, are governed by the other specific codes, federal laws and other regulatory legal acts, in particular:

- the Russian Federation Land Code;
- the Russian Federation Tax Code;
- the Russian Federation City Planning Code
- the Federal Law 'On the State Registration of Rights to Real Estate and Transactions therewith';
- the Federal Law 'On the State Land Cadastre'; and
- the Federal Law 'On Transfer of Land or Land Plots from One Category to Another'.

State authorities of regions of the Russian Federation (regional authorities) may also adopt laws and other legal acts related to issues connected with investment activities in the real estate field. Such laws and other legal acts are effective only on the territories of the respective regions of the Russian Federation (for instance, Moscow, St Petersburg, Krasnodar Region, Republic of Tatarstan).

Any party is entitled to address a court to prevent an action by another party. To receive an injunction strong arguments shall be presented. Russian courts find themselves reluctant to impose restrictions in the absence of substantial proof of misconduct by another party. Courts rule only in accordance with relevant contract provisions, and applicable legislation, regulations, usages, etc. No equity judgments are available. Parol evidence is admissible though not very widespread in business litigation and arbitration.

Contracts between Russian and foreign counterparts as well as contracts related to real estate must be made in writing, or they are

considered to be void and invalid. Oral contracts are admissible only for minor transactions between Russian individuals. Oral contracts between Russian legal entities (in non-real estate issues) are restricted, though enforceable under certain conditions and limitations (for instance, a ban on using witness evidence in the event of a dispute).

2 Conveyance documentation

What are the legal requirements for documents recording conveyance?

Real estate (referred to as 'immoveable property' in law) includes land plots, subsoil plots, solitary water objects and everything that is securely attached to land, any objects that may not be relocated without incommensurate damage to their purpose, including forests, perennial plants, buildings and constructions. The main characteristic of real estate objects is inseparable attachment to land. However, regardless of existing attachment to land, by virtue of direct stipulation of the law, real estate also includes other property subject to state registration, namely aircraft, marine and river vessels and space objects. In the housing sphere real estate objects include apartments and elements of engineering infrastructure.

In the Russian Federation, real estate objects, rights thereto and transactions therewith are registered separately. Registration rules are the same throughout Russia.

Currently, registrations of land plots are performed by means of adding data on the land plots, including data on the real estate objects securely attached thereto, in the State Land Cadastre, which is formed in the course of cadastral registrations of land plots and cadastral and technical registrations of the real estate objects securely attached to such land plots. One of the main documents of the state land cadastre is the Unified State Register of Land. No transactions are allowed concerning a land plot (part of a land plot) until it has gone through such registration.

Objects of city planning activities, in particular buildings and constructions, are additionally described and registered in the system for state registration of objects of city planning activities.

The main information, namely the rights to each real estate object and data concerning restrictions on such rights, is still registered in the Unified State Register of Titles to Real Estate and Transactions Therewith (EGRP in Russian) during the process of state registration of rights to real estate and transactions therewith. On the basis of the data contained in the state register information on rights to land plots and restrictions thereon is inserted in EGRP.

Real estate objects are described and individualised upon cadastral and technical registrations. As a result of state registration of rights to real estate or transactions therewith, rights to individually defined real estate objects are acknowledged and confirmed by the state.

Cadastral and technical registrations of real estate objects and the state registration of rights to real estate and transactions therewith are two closely interconnected procedures from the point of view of investment activities that involve concluding transactions aimed at

acquiring the rights to various real estate objects. The state registration of rights to real estate, which is required for acknowledgement and confirmation, commencement, termination and restriction of the respective rights, is performed on the basis of data received from state technical registration or inventory authorities.

Registration in the EGRP (either of the transaction itself or of the title transfer) is of vital importance for all of real estate-connected transactions.

3 Foreign investors

What other factors should a foreign investor take into account in considering an investment in your jurisdiction?

According to the general rule of the Russian Constitution, foreign citizens, legal entities, and Russian legal entities whose share capitals ownership interests are held by foreigners are entitled to acquire the same rights to land plots as Russian citizens and legal entities without foreign participation.

Agricultural land plots are the exception to this rule. Foreign parties (individuals and legal entities) and Russian legal entities with more than 50 per cent foreign share participation in their share capital are only entitled to have the right to lease agricultural lands.

In addition, pursuant to the Land Code of the Russian Federation, foreign parties may not have ownership rights to land plots located on border territories (the list of which is established by the president) and other specifically determined territories. The list of such territories has not yet been determined. Until such list is determined, granting any land plots located on border territories to the ownership of foreign citizens, individuals holding no citizenship or foreign legal entities is prohibited.

No special reporting from foreign investors is required (except for statistics filings).

A foreign investor should bear in mind that during its activities in Russia certain formal requirements for document signing, filing etc must be met (eg, at the moment of local company creation or real estate title registration). Though they are common to both Russian and foreign businesses, some peculiarities exist. For instance, documents originating from abroad must be accompanied by a certified translation into Russian, official documents shall carry an apostille, and the competence of the company's officials signing in its name shall be duly proven by a power of attorney or excerpt from a company register (or a similar document). Russian companies and state authorities also usually ask for a company stamp to be placed together with a signature in the documents.

Federal Law No. 57-FZ, 'On the Procedure for Foreign Investment in Commercial Organisations of Strategic Importance for the National Security of the Russian Federation' (the Strategic Enterprises Law), sets forth initial and ongoing notification obligations, and in certain cases requires prior approval by the government, with respect to foreign investments in strategic enterprises.

Strategic enterprises are companies that operate in 42 strategic sectors. Among others, strategic sectors include aviation, space exploration and technology, cryptography, certain activities involving use of subsoil resources, transportation, TV and radio broadcasting, certain telecommunication services, print publications with a circulation of 1 million copies or more and certain military-related industries. Investments in strategic enterprises that engage in geological study, exploration or production of natural resources on subsoil plots of federal interest (subsoil strategic enterprises) are subject to more onerous requirements.

4 Exchange control

If a non-resident invests in a property in your jurisdiction, are there exchange control issues? What about repatriation of capital?

Russian legislation that regulates operations performed in foreign currency is intended to protect the national currency and prevent

capital from being illegally exported. The main legislative act in this sphere is the Federal Law 'On Currency Regulation and Control', No. 173-FZ dated 10 December 2006 (hereinafter the Law on Currency Regulation). The regulatory instruments of the Central Bank of the Russian Federation are also of relevance, given that in accordance with the above-mentioned law the Central Bank is the main body for currency regulation in Russia.

Russia's currency legislation has recently undergone significant changes due to the overall liberalisation of the Russian economy as well as the intention of the government to ensure conditions for a freely convertible rouble. Starting from 2006, most restrictions connected with capital transfer transactions between Russian and foreign entities were abolished.

As a general rule, transactions between residents and non-residents as well as transactions between non-residents are conducted freely and without any restrictions. In particular, non-residents are entitled to transfer foreign currency without limitations to accounts opened in Russian banks or to transfer foreign currency from accounts opened in Russian banks to those opened beyond the borders of the Russian Federation. Also, non-residents have the right to freely conduct transactions with securities. Transactions between residents and non-residents will still require filing a special report (a transactional passport) with the Russian bank that is involved in the money transfer with regards to the amount of money transferred to or from abroad. If a foreign investor has created a subsidiary in Russia, such a subsidiary company is qualified as a resident. According to article 140 of the Russian Civil Code the transactions between such a subsidiary and other Russian companies must be conducted in roubles. Agreements may therefore refer to an amount expressed in a foreign currency, but the payment transfers are to be made in its rouble equivalent.

5 Legal liability

What types of liability does an owner of real estate face? Is there a standard of strict liability and can there be liability to subsequent owners? What about tort liability?

Real estate owners' liability regulation is quite superficial at present. Only general liability rules apply, stating that any personal or environmental damage shall be compensated by the violator. Additionally, administrative fines and penalties are imposed for certain offences (up to 100,000 roubles and suspension of the company's activities for up to 90 days).

While no broad court practice exists, the liability imposed on a real estate owner may be transferred to the subsequent owners.

6 Protection against liability

How can owners protect themselves from liability and what types of insurance can they obtain?

Not enough practice yet exists regarding protection from liability. Commercial insurance is available but not widespread. If the company is engaged in certain types of 'dangerous' activities (eg, mining or construction) special obligatory insurance with governmental agencies is required.

7 Choice of law

How is the governing law of a transaction involving properties in two jurisdictions chosen? What are the conflict of laws rules in your jurisdiction?

General conflict of law rule states (article 1211 of the Civil Code) that a contract shall be governed by the law of the jurisdiction that is most closely connected with the transaction (by default – the jurisdiction of the party of engaged in most significant performance under the contract). Contracts related to real estate are presumed to be most closely connected with the jurisdiction where the immovable

property is located. The parties are also free to choose the governing law for the transaction at their own discretion (article 1210 of the Civil Code). But notwithstanding this choice of law, contracts related to real estate located in Russia shall be imperatively governed by Russian law.

As to real estate rights, their occurrence and cessation, the rules of the jurisdiction where the real estate object is situated will apply independently of contract choice of law provisions.

8 Jurisdiction

Which courts have subject-matter jurisdiction over real estate disputes? Which parties must be joined to a claim before it can proceed? What is required for out-of-jurisdiction service? Must a party be qualified to do business in your jurisdiction to enforce remedies in your jurisdiction?

Russian courts are authorised to hear and make a determination in a court action regarding real estate claims. In the absence of forum choice provision, contract disputes are tried at the court of the region where the respondent is registered. For actions in rem only the court of the region where the real estate is located can resolve the case.

The claimant and respondent are the necessary parties, though personal presence in the court hearings is not usually required. For some disputes state authorities (eg, registration agencies) are required to participate.

A special court appointment is required for out-of-jurisdiction service to be carried out by one of the parties. Otherwise it is performed through state authorities themselves. There is no need to be qualified in any way to be able to enforce remedies in Russia.

When entering into contract relations with Russian businesses foreign investors should bear in mind that Russian state courts support a rather strict position that real estate claims are subject to their exclusive jurisdiction and cannot be submitted to arbitration either in Russia or abroad. This usually makes it impossible to enforce an arbitral award regarding Russian real estate in Russian state courts even in the presence of an arbitration clause in the contract. Accordingly, it is not recommended to use arbitration for Russian real estate disputes if the enforcement is likely to take place in Russia.

9 Investment entities

What legal forms can investment entities take in your jurisdiction? Which entities are not required to pay tax for transactions that pass through them and what entities best shield ultimate owners from liability?

The Civil Code of the Russian Federation provides for various legal forms – general partnerships, limited partnerships, additional (or unlimited) liability companies, limited liability companies (LLC or the Russian abbreviation, OOO), joint-stock companies (JSC or the Russian abbreviation, AO), and others. The Civil Code also provides for non-profit organisations of various types. The most common commercial organisations are joint-stock companies and limited liability companies.

Joint-stock companies

A joint-stock company has shareholders and may engage in any form of commercial activity envisaged by its charter documents provided such activity is not prohibited by Russian corporate law or other legislation, subject to licensing where applicable (see below). A JSC may contract, undertake legal obligations, acquire property and sue or be sued in its own name. A joint-stock company may be either ‘open’ (OJSC), meaning publicly held, or ‘closed’ (CJSC), meaning privately held. Both forms may issue common or preferred shares and debentures. Both forms are subject to statutory reporting requirements and regulatory restrictions, but the requirements for public disclosure are less rigorous for CJSCs.

No provision in the organising documents can be made to prohibit a JSC shareholder from selling its shares. The shareholders of a CJSC, however, have non-waivable pre-emptive purchase rights.

For an OJSC, the statutory minimum authorised capital is 100,000 roubles, and 10,000 roubles for a CJSC.

Different classes of shares are permitted; dividends and voting rights are equal for each share in a class. Shares in a joint-stock company are considered ‘securities’ under the Russian securities law and must be registered with the Federal Service for Financial Markets at the time of issuance.

The board of directors (often referred to as the supervisory council) of a JSC is responsible for the overall management of the company’s activities. The powers of the directors normally include all powers not specifically delegated to the realm of the general meeting of the shareholders or other management bodies. However, these powers may be specifically limited by the company’s charter document or other applicable laws. Directors have broad fiduciary duties, and may be held individually or jointly liable for damages to the company resulting from their misconduct.

Accounting records must be kept in roubles and according to Russian accounting rules (records may also be kept in parallel according to any other desired accounting standards, for example, IFRS). Dividends may be paid quarterly, semi-annually, or annually. The decision to pay dividends is made at the shareholders’ meeting, but the amount of dividends is recommended by the board of directors. Dividends are determined based on the financial statements prepared under Russian accounting and reporting standards.

Limited liability companies

Limited liability companies are also a popular form of corporate organisation. LLCs are often used by foreign companies to conduct wholly owned businesses in Russia. The minimum authorised capital for an LLC is 10,000 roubles.

The Limited Liability Company Law provides for many similar provisions to those in the Joint-stock Company Law.

A notable distinction between LLCs and JSCs is the division of the capital of a LLC into ‘participations’ or units that are not considered securities under the Russian securities law, unlike shares in a JSC, which are securities.

Unlike in a JSC, the sale of participations by a participant of an LLC can be restricted in the charter. Also unlike in a JSC, a participant may withdraw from an LLC at any time, requiring the LLC (or remaining participants) to provide it with a portion of the net assets of the LLC proportionate to its interest in the LLC.

Limitations on the sale of participation interests or preferential purchase rights or on the approval process for a transfer of a participation may be included in the charter of an LLC.

Dividends and voting rights are determined by the participants in the charter, although some restrictions on voting rights exist in the Limited Liability Company Law. Shareholders of a joint-stock company JSC (participants of a LLC) have the power to amend the company’s rules and by-laws, change its authorised capital, elect members of the board of directors, approve annual reports, and adopt decisions on reorganisation and liquidation.

In general, a shareholder’s or participant’s liability is limited to the extent of the capital it has invested in the company, including any unpaid amounts. However, in the event of the bankruptcy of a company, a ‘parent’ may be held liable by a company’s creditors if such parent’s actions caused the subsidiary to become insolvent.

A ‘parent’ is defined quite widely and includes control not only by reference to ownership, but includes contractual or other relationships that allow a person including a parent, to determine the decisions of the company. Application of these provisions is uncertain, which, in practice, often leads to investments in Russia being made through an offshore special purpose vehicle.

No Russian entities can be considered as pass-through for tax purposes – they are obliged to pay tax on income (24 per cent) from

the sources in Russia, value-added tax (18 per cent) on Russian operations and a property tax (up to 2.2 per cent of the asset value) even if no operations are carried out.

10 Foreign investors

What form of entities do foreign investors customarily use in your jurisdiction?

Foreign companies conducting Russian business operations increasingly view a wholly owned Russian subsidiary as a relatively quick and easy way of expanding their local businesses. Usually an LLC form is used as it is simpler for registration and management processes.

In certain cases when there is no intention to establish a local entity it is possible to conduct business directly from outside Russia by creating a local representative office, which is not regarded as a Russian legal entity.

11 Organisational formalities

What are the organisational formalities for creating the above entities? What requirements does your jurisdiction impose on a foreign entity? What are the tax consequences for a foreign investor in the use of any particular type of entity, and which type is most advantageous?

Registration of a legal entity usually takes three to four weeks, including one week after the submission for the registration of certain required documents with the (tax) authority. The tax authorities finalise the state and tax registration of a company and then forward the documents for registration with the social funds and Federal Service for State Statistics without the involvement of the company being registered.

When a foreign founder is involved, there is a need for a number of documents to be apostilled (or legalised), translated and notarised, which can mean that the period from commencing the process to its completion is significantly in excess of three to four weeks.

The state fee for registration of a LLC or JSC is 2,000 roubles, plus some other small amounts. The professional fees for the entire process of collecting documents, preparing organisational documents and presenting the documents to the Russian registration authorities typically range from €4,000 to €5,000.

Rouble and foreign currency accounts can be opened after registration. Prior to registration an 'accumulative' account is opened to pay up the charter capital. Certain requirements established by the government and specific requirements that may be established by each bank must be met. For an LLC, 50 per cent of the charter capital must be paid prior to state registration and the balance must be paid within the period established by the foundation agreement (but not more than one year from the date of state registration). For a JSC, 50 per cent of the charter capital must be paid within three months after state registration and the balance within the period established by the foundation agreement (but not more than one year from the date of state registration). Charter capital contributions can be made in monetary form or in kind. Debt may not be capitalised as a contribution to capital.

Generally, only one participant or shareholder is required. Under a special rule, if a sole participant or shareholder of a Russian company (LLC or CJSC) to be formed is itself a company owned by only one participant or shareholder, then the Russian company to be formed must have at least two participants or shareholders. A CJSC with over 50 shareholders must convert to an OJSC. An LLC with over 50 participants must convert to an OJSC or into a manufacturing cooperative.

12 Documentation

Is it customary in your jurisdiction to execute a form of non-binding agreement before the execution of a binding contract of sale? Will the courts in your jurisdiction enforce a non-binding agreement or will the courts confirm that a non-binding agreement is not a binding contract? Is it customary to take the property off the market while the negotiation of a contract is ongoing?

Non-binding agreements are usually structured as memorandums of understanding and letters of intent. They are not legally regulated and thus do not form an enforceable contract. They can gain legal effect only if they form a preliminary agreement signed by both parties, describing all the main features of the planned transaction, including an obligation to sign a principal agreement in the stipulated term.

The property may be taken off the market during negotiations subject to payment of a retainer by the buyer. Usually it is a question to be resolved at the parties' own discretion.

13 Contract of sale

What are typical provisions in a contract of sale?

Land plot sale and purchase agreements are concluded in writing by means of preparing one document to be signed by the parties thereto.

Land plot sale and purchase agreements must contain the essential conditions stipulated by Russian legislation (an agreement not containing such conditions shall be deemed non-concluded), in particular, the price of the land plot, any data that allow for unambiguously identifying the land plot. Sale and purchase agreements must also comply with other requirements for the execution and contents of sale and purchase agreements stipulated by current legislation.

It is necessary to note that Russian legislation stipulates certain special requirements for agreements for the sale and purchase of a land plot; namely, the following conditions are invalid when incorporated into land plot sale and purchase agreements:

- establishment of the seller's right to buy out the land plot at the seller's discretion;
- establishment of rights restricting the further management of the land plot including those restricting mortgage, transfer of the land plot for lease or the conclusion of other land transactions; and
- establishment of rights restricting the seller's liability in cases when third parties claim rights to the land plot.

The interests of a land plot purchaser are further protected by the requirement, established by the Land Code, for the seller to provide the buyer with all available information on the encumbrances on the land plot and the restrictions on its use. Should the seller provide the buyer with patently false information on encumbrances on the land plot and restrictions on its use, on the permit to construct thereon or on the use of neighbouring land plots, that significantly affects the use and price of the land plot being proposed for sale, or other information that may affect the buyer's decision to purchase such land plot, the buyer is entitled to require that the purchase price be reduced or that the land plot sale and purchase agreement be terminated and damages inflicted on the buyer be paid. If the buyer wishes to conduct more complex research it is usually done at its own expense.

The amount of the down payment is usually negotiated by the parties and it depends on the circumstances of a particular deal. As escrow services are still not widespread in Russia, the down payment is usually kept on the seller's account, or alternatively a system of letters of credit is used.

14 Environmental clean-up

Who takes responsibility for a future environmental clean-up? Are clauses regarding long-term environmental liability and indemnity that survive the term of a contract common? What are typical general covenants? What remedies do the seller and buyer have for breach?

Not applicable. Due to the lack of practice in the area of environmental damage the inclusion of covenants or representations regarding environmental matters has not yet become widespread. A very general rule of the Civil Code indicating that the seller is liable for latent defects of the merchandise is understood to cover consequent environmental and other damage.

15 Lease covenants and representation

What are typical representations made by sellers of property regarding existing leases? What are typical covenants made by sellers of property concerning leases between contract date and closing date? Do they cover brokerage agreements and do they survive after the property sale is completed?

Not applicable. Usually the seller is required to indicate all lease agreements relating to the sold property in a separate attachment to the acquisition agreement. Russian legislation and business practice does not recognise estoppel certificates.

16 Leases and mortgages

Is a lease generally subordinate to a mortgage pursuant to the provisions of the lease? What are the legal consequences of a lease being superior in priority to a mortgage upon foreclosure? Do lenders typically require subordination and non-disturbance agreements?

As a rule, a mortgagee's rights are subordinate to those of the prior mortgagee. No special subordination concept exists in Russian legislation relating to leases. Subordination and non-disturbance agreements are not enforceable.

17 Delivery of security deposits

What steps are taken to ensure delivery of security deposits to a buyer? How common are security deposits under a lease? Do leases customarily have periodic rent resets?

Security deposits are widespread. Usually they are transferred in cash to the lessor's account. Rent resets are rarely used in lease agreements in Russia.

18 Due diligence

What is the typical method of title searches and are they customary? How and to what extent may acquirers protect themselves against bad title? Does your jurisdiction provide statutory priority for recorded instruments?

Due diligence is usually performed by both legal and non-legal counsel (accountants, management and marketing consultants). Legal due diligence is performed through a search in public registers as well as through a review of documents represented by the seller. As a result a due diligence report is prepared. Opinion letters are not widespread because regulations on lawyers' liability for professional misconduct or mistakes is quite uncertain.

19 Structural and environmental reviews

Is it customary to arrange an engineering or an environmental review? What are the typical requirements of such reviews? Is it customary to get representations or an indemnity? Is environmental insurance available?

To arrange or not arrange an engineering or an environmental review is a business issue. No customary practice exists in relation to these processes.

20 Review of leases

Do lawyers usually review leases or are they reviewed on the business side? What are the lease issues you point out to your clients?

Leases are usually reviewed both from business and legal sides. The following issues are usually covered by a legal review: validity of lease, term of lease, possibility for a pre-term dissolution or termination, possibility to increase rental payments, rights to sublease, etc.

21 Other agreements

What other agreements does a lawyer customarily review?

Usually any and all agreements related to the real estate at hand are reviewed. The scope of analysis can be narrowed by the concept of materiality.

22 Closing of transaction

How does a lawyer customarily prepare for a closing?

As no customary practice exists the list may vary from time to time. In any case special attention is paid to registration and authorities of the counterparty, title to the property and provisions imperative according to law (form of contract, registration, price, etc).

Financing**23 Form of lien**

What is the method of creating and perfecting liens?

Liens are created through a written agreement between the creditor and the debtor (mortgage) or through a court decision (arrest).

24 Legal requirements

What would be the ramifications of a lender from another jurisdiction making a loan secured by collateral in your jurisdiction? What is the form of lien documents in your jurisdiction? What other issues would you note for your clients?

No special ramifications are provided by the law. Any lien documents must be in writing. Mortgages are registered with the EGRP. The fee for the registration is quite modest (ranging from 2,000 to 7,500 roubles).

25 Loan interest rates

How are interest rates on commercial and high-value property loans commonly set? What rate of interest is unreasonably high in your jurisdiction and what are the consequences if a loan exceeds the reasonable rate?

LIBOR and Euribor are broadly used in large international finance transactions. Small and mid-sized deals usually refer to a fixed amount of interest. As guidance on the acceptable interest rate in Russia, one can refer to the Central Bank refinancing rate, which is currently 10 per cent.

26 Default and enforcement

How are remedies against a debtor in default enforced in your jurisdiction? Is one action sufficient to realise all types of collateral? What is the time frame for foreclosure and in what circumstances can a lender bring a foreclosure proceeding?

Enforcement is always done through a judicial procedure. Only if a special agreement is signed between the debtor and the creditor at foreclosure may it be performed through a public order. A bailiff service at the Ministry of Justice is addressed after a judgment or a notary act is received.

Update and trends

Real estate legislation is considered one of the most conservative areas of law in Russia. The downturn in the market has also negatively affected its development, and therefore not many new updates have occurred recently. From the market standpoint, while the acquisition prices of real estate are quite stable (especially for residential properties in major cities), there has been a substantial decrease in lease prices, which in turn caused a lot of office moves to take place.

From a legal viewpoint, there has also been no substantial change in regulations. However, one fundamental review of the system of government regulation of construction works took place at the beginning of 2009. From January 2010 the system of state licensing of construction activities will be completely abolished; instead, a new system of self-regulating organisations (SROs) will be introduced. From then on it will be required that all construction business be conducted only by members of SROs that possess admission certificates issued by the respective SRO.

To become a member of an SRO and receive an admission

certificate, an applicant first must submit certain payments to an SRO. Payments include contributions to the compensation fund of the SRO, an admission fee and a membership fee. For the purpose of becoming a member of an SRO, an applicant is obliged to pay a monthly or annual membership fee as well.

Upon receipt of payments, an applicant must secondly submit documents to the SRO that confirm the compliance of the applicant with requirements for issuance of an admission certificate. The SRO must within 30 days make a decision on whether to accept the applicant or whether to decline the applicant. If the SRO makes a positive decision, it must in three days issue an admission certificate to the member. An admission certificate is issued for an indefinite term and is valid on all territory of the Russian Federation.

While the switch from government regulation to self-governance is generally regarded as positive, there is still no specific understanding of how the system will work and what impact it will have on the quality of construction.

27 Protection of collateral

What actions can a lender take to protect its collateral until it has possession of the property?

No special protective actions in connection with collateral are provided by Russian law. The mortgaged property can be left either with the mortgagee or with the mortgagor.

28 Recourse

May security documents provide for recourse to all of the assets of the borrower? Is recourse typically limited to the collateral and does that have significance in a bankruptcy filing?

The recourse for a secured lender is limited to the collateral. If the amount of money received after the sale of collateral is not enough to cover the debt, then recourse to all other assets can be utilised. Bankruptcy proceedings bring a significant change to the order of recourse.

29 Cash management systems

Is it typical to require a cash management system and do lenders typically take reserves?

No particular requirements for a cash management system are common in Russia.

30 Credit enhancements

What other types of credit enhancements are common? What about forms of guarantee?

Guarantees of different kind (payment guarantees, banking guarantees) are the most widespread methods of credit enhancement. Letters of credit are successfully used for large-scale transactions. Holdbacks and carve-back guarantees are not commonly used.

31 Loan covenants

What covenants are commonly required by the lender in loan documents? What is the difference depending on asset classes?

Russian law makes no provision for covenants, but business practice successfully employs concepts from English law, which are usually acceptable under Russian legislation.

32 Financial covenants

What are typical financial covenants required by lenders?

Russian law makes no provision for financial covenants, but business practice successfully employs concepts from English law, which are usually acceptable under Russian legislation.

33 Bankruptcy

Briefly describe the bankruptcy system in your jurisdiction.

Relations connected to the insolvency of legal entities in Russia are governed by the new Federal Law 'On Insolvency (Bankruptcy),' No. 127-O3, which has recently undergone a major change.

Insolvency is understood as the debtor's inability, as recognised by a state arbitration court, to fully satisfy creditors' claims regarding monetary obligations or to fulfil its obligations to make mandatory debt payments.

A legal entity is recognised as being unable to satisfy creditors' monetary claims or fulfil its mandatory payment obligations if its outstanding liabilities have not been met within three months as of their due dates.

The consideration of bankruptcy cases falls within the jurisdiction of the commercial courts.

Commercial courts initiate bankruptcy proceedings against legal entities when the sum of creditors' claims exceeds 100,000 roubles.

The right to initiate a bankruptcy suit for recognising a debtor as bankrupt is vested in the debtor, the creditor, and authorised persons, for example, tax authorities.

When particular signs of a debtor's insolvency become apparent, the debtor's authorised body is obligated to bring a bankruptcy suit to a commercial court for the commencement of bankruptcy proceedings aimed at adjudicating the debtor a bankrupt within one month from the date when the relevant circumstances occurred.

In cases of fraudulent and deliberate bankruptcy, the law provides for measures of civil and criminal responsibility of the founders and employees of legal entities. During consideration of bankruptcy suits, the following main bankruptcy procedure are applied to debtor legal entities:

- surveillance;
- financial recovery;
- external management;
- bankruptcy proceedings; and
- settlement agreement.

Following the submission of an application for commencing bankruptcy proceedings and the acceptance of such by a commercial court, the commercial court places that debtor under surveillance for the time required for preparing for hearing the bankruptcy case (which usually takes several months).

34 Secured assets

What are the requirements for creation and perfection of a security interest in non-real property assets? Is a 'control' agreement necessary to perfect a security interest and, if so, what is required?

Lockbox services are not yet offered by Russian banks.

35 Single purpose entity (SPE)

Do lenders require that each borrower be an SPE? What are the requirements to create and maintain an SPE? Is there a concept of an independent director of SPEs and, if so, what is the purpose? If the independent director is in place to prevent a bankruptcy filing, has the concept been upheld?

No requirements for an SPE exist in Russia. The concept of an independent director exists, but only for matters of corporate governance and not real estate or loan issues.