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RUSSIA

Government and State Duma Introduce Competing Bills to Liberalize Currency Controls

The process of liberalizing existing currency control regulations, one of the most controversial areas of Russian law, has recently led to a conflict between the Russian Federation ("RF") Government and the RF State Duma (the "Duma"). Currency rules in Russia have long been criticized for the bureaucratic restrictions imposed on business, as well as for their failure to combat capital flight. Business lobbies have pressured the RF Government and the Duma to loosen currency restrictions that have been in force since 1992, and further toughened after the August 1998 financial crisis. Currently, Russian companies must obtain a permit from the RF Central Bank to carry out a wide range of capital operations, repatriate convertible currency export proceeds within 90 days, and convert 50% of the export proceeds into Rubles.

Although President Vladimir Putin generally supports a much more liberal currency control system, various interest groups, legislators and governmental agencies have been debating the nature and degree of such liberalization for over a year. With support from the Russian business community, liberal Duma deputies have insisted upon full liberalization of the currency system in order to improve the investment climate. However, the RF Central Bank and the RF Ministry of Finance have argued against the elimination of all currency restrictions, and instead have sought to retain certain powers to limit capital transactions in the event of a financial crisis. These alternative approaches to currency control reform are reflected in the recent bills introduced by the RF Government and the Duma.

Under the bill prepared by the Duma (the "Duma Bill"), the mandatory sale of convertible currency export earnings on the domestic market would be abolished. The Duma Bill eliminates differential treatment of residents and non-residents, including legal entities, and treats Rubles and foreign currency on an equal footing, with the aim of increasing the much needed flow of foreign investment. The Duma Bill grants residents the right to open bank accounts with foreign banks in countries that are members of the Organization for Economic Cooperation and Development (the "OECD"). Further, the Duma Bill does not provide for a separate currency control body (*i.e.*, previously, there had been a currency control committee) and leaves currency regulation as the responsibility of the RF Central Bank and other existing federal executive bodies.

Under the bill proposed by the RF Government (the "Government Bill"), the proportion of export proceeds subject to mandatory conversion would be reduced from 50% to 30%, and businesses would only have to notify the RF Central Bank of certain capital transactions, as

opposed to obtaining a permit. Like the Duma Bill, the Government Bill would allow residents, including legal entities, to open bank accounts with foreign banks in OECD member countries, but all transactions through such accounts would have to be reported. In terms of deferral of payments for exported goods beyond 180 days, the Government Bill requires exporters to maintain in reserve, for the period of deferral, but not in excess of two years, up to 50% of the value of such transactions. The reserve and other requirements with respect to a transaction providing for an installment sale may be varied by the Government, depending on the type of product subject to such transaction (but generally, within the 50% reserve limit). Predictably, business groups have been critical of such provisions in the Government Bill. Moreover, in the case of a financial crisis, the RF Government would have two special powers – first, to require that businesses reserve 20% of all incoming investments or payments for one year, and second, that a reserve equal to 100% of all capital transferred abroad be maintained for two months.

Given the conflicting provisions of the two bills, the Duma decided to postpone consideration of the matter from mid-December 2002 to the Spring of 2003. /N. *Menshikova*

Currency Control Regime Relaxed Further

As a part of the ongoing effort to reform Russia's restrictive currency control regime, the RF State Duma recently adopted RF Law No. 192-FZ, dated December 31, 2002, which amends Article 5 of the RF Law "On Currency Regulation and Currency Control" (the "Amendments"). The Amendments release Russian residents from certain currency repatriation and conversion requirements when repaying loans from non-residents acting as agents for governments of member countries of the OECD ("OECD Agents").

Although limited to loans from OECD Agents, the Amendments address two of the most fundamental issues under Russian currency regulations, namely (i) the ability of Russian residents to open and maintain accounts with banks located abroad; and (ii) mandatory conversion rules for foreign currency export proceeds.

The Amendments provide that a Russian resident who has entered into a loan agreement with an OECD Agent is entitled

to receive export proceeds in foreign currency to its account abroad on the basis of a permit issued by the RF Central Bank. This element constitutes a departure from the general rule that such proceeds must be repatriated within 90 days of receipt and then converted into Rubles at a rate of 50%. The resident will be required to use these export proceeds solely to satisfy its loan obligations to the OECD Agent, otherwise, these funds must be transferred to the resident's account in Russia with an authorized bank.

The Amendments were officially published on December 31, 2002, and became effective immediately upon their publication. /E. *Abrossimova*

New Bankruptcy Procedures Introduced

On October 26, 2002, President Putin signed the new RF Law "On Bankruptcy" (the "Bankruptcy Law"). As we reported in the August 9, 2002, issue of the *CIS Legal Newswire*, President Putin previously vetoed the draft of the Bankruptcy Law approved by the State Duma on July 1, 2002. After considering the President's veto, the Duma adopted an amended Bankruptcy Law in accordance with the President's comments.

Now, arbitration courts must apply the Bankruptcy Law to all bankruptcy proceedings (or parts thereof) initiated after December 2, 2002, which is the date on which the majority of the provisions of the Bankruptcy Law became effective. For example, once, upon completion of the external management stage of a bankruptcy proceeding commenced in accordance with previous bankruptcy legislation, an arbitration court initiates the final bankruptcy stage, the provisions of the new Bankruptcy Law will become applicable to such final stage.

Among the most important consequences of the Bankruptcy Law is that authorized government bodies may now vote at all meetings of a creditors' committee and are entitled to receive payments on account of the debtor's liabilities together with miscellaneous creditors, whereas previously, government bodies could vote only at the first meeting of the creditors' committee and could receive such payments ahead of miscellaneous creditors as a creditor of a separate priority category. Thus, even though government bodies have lost one level of priority with respect to the distribution of the

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debtor's assets in settlement of the debtor's liabilities, they have gained access to all stages of bankruptcy proceedings by being granted the right to vote at all meetings of the creditors' committee. It should be noted that notwithstanding the elimination of a separate priority category for government bodies' claims under the Bankruptcy Law, corresponding amendments to the RF Civil Code have not been made, thus creating an inconsistency between the Bankruptcy Law and the RF Civil Code. The legal implications of such inconsistency presently remain unclear.

Among other changes introduced by the Bankruptcy Law, the sale of a debtor's business or assets with a balance sheet value in excess of 100,000 Rubles (approximately US \$3,000) may now be effected only through a public auction, whereas, previously, the creditors' committee could choose a different method of disposition of the debtor's assets. This is a significant development and should help to eliminate frequent abuses in the bankruptcy process by members of the creditors' committee. The starting auction price must be determined by the creditors' committee on the basis of a price established by an independent appraiser, provided that the starting auction price may not be lower than the price approved by the appropriate governing body of the debtor. The creditors' committee may decide to sell the debtor's assets directly to third parties only if the debtor's assets were not sold at a second auction, but, even in this case, the direct sale price may not be lower than the price approved by the debtor's appropriate governing body. /E. Abrossimova

New Civil Procedural Code Completes Reform of Russian Procedural Law

On November 15, 2002, President Putin signed the RF Law "On the Entry into Force of the Civil Procedural Code of the Russian Federation." According to this law, the new RF Civil Procedural Code (the "New CPC") became effective on February 1, 2003, replacing the outdated Civil Procedural Code, which was adopted in 1964. The approval of the New CPC represents the culmination of a series of initiatives to reform Russia's procedural laws, which included the adoption of the new Criminal Procedural Code in 2001 and the new Arbitration Procedural Code in 2002 (the "New APC"), as we reported in

the October 9, 2002 issue of the *CIS Legal Newswire*.

The necessity of the New CPC was acknowledged in 1993 by the Special Presidential Council on Judicial Reform, and, since that time, various State bodies have been working on a draft of the New CPC. The New CPC eliminates jurisdictional gaps which existed in the 1964 version of the code, under which it was possible to bring commercial disputes before courts of general jurisdiction if a party to the dispute was an individual not registered as an entrepreneur (*e.g.*, a dispute between an individual shareholder and a joint stock company). Now, under the New CPC and the New APC, depending on the subject matter of the dispute, and whether such dispute is of a commercial or economic nature, the authority of courts of general jurisdiction and State arbitration courts has been strictly separated. The New CPC provides that courts of general jurisdiction may consider all types of disputes with the exception of those which fall under the jurisdiction of State arbitration courts.

Furthermore, the New CPC has eliminated the institution of public assessors (lay judges) -- private citizens who were resolving cases together with professional judges. Under the New CPC, all cases must be decided by a single professional judge, except for certain special cases in which a panel of professional judges is necessary according to the law (*e.g.*, cases concerning the dissolution of an election committee or a referendum committee, as well as all cases in courts of appeals, cassation courts and courts of supervision). As a general rule, though, all cases in courts of the first instance will be considered by one judge.

The reform of the court system is intended to ensure that all controlling power is vested with the highest court and State judicial bodies; consequently, the role of public prosecutors has been considerably limited. Accordingly, prosecutors under the New CPC are now prohibited from interfering in disputes between individuals and legal entities, unless the interests of the public are involved or the rights of individuals with disabilities or minors have been violated. In addition, the New CPC provides for a limited list of disputes in which a prosecutor may participate in court hearings in order to issue an opinion. Prosecutors have also lost their authority to lodge so-called "protests" in courts of appeal, courts of cassation and courts of supervision; upon receiving such protests, the courts had been required to consider them. In contrast to the provi-

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sions of the New APC, the New CPC does not limit the courtroom representation of companies to registered "legal advocates" only. As in the past, companies may be represented in court by any individual.

Like the New APC, which is designed to reduce court bureaucracy, the New CPC has increased the significance of the introductory phase of court proceedings, providing, for instance, a range of steps which are to be carried out by the court and by the parties to the dispute. One important addition to this process is a preliminary court hearing aimed at expediting consideration of cases by courts of general jurisdiction by resolving many issues prior to court hearings.

The role of courts of cassation has become more important. Cassation courts now may not only consider the explanations of parties to a dispute, but may also investigate other evidence (e.g., interview witnesses), including new evidence that was not considered by the court of first instance. Previously, cassation courts could only consider the explanations of the parties, unless there was new evidence which the parties were unable to submit to the court of first instance.

Major changes have also been implemented with respect to the supervisory courts. Now, proceedings in the supervisory instance may be initiated by the parties or by other persons whose rights are affected by the court's decision, and not by judges and prosecutors, as under previous legislation. A supervisory appeal must be brought before the court within one year after the court's decision has entered into force. The supervisory appeal is first considered by a judge, and if he or she finds that there is a sufficient basis for hearing the appeal, then it is passed on to a panel of judges, who ultimately decide the matter.

Unlike the 1964 Civil Procedural Code, which contained only seven articles regulating court proceedings with the participation of foreign citizens and legal entities, the New CPC regulates such procedure in detail, and determines the jurisdiction of courts of general jurisdiction (including a list of disputes which fall under the exceptional competence of these courts), and the procedure for the recognition and enforcement of decisions of foreign courts and independent arbitration tribunals. However, it should be noted that enforcement of foreign court decisions and arbitral awards rendered in disputes related to "entrepreneurial and other economic activity" falls within the jurisdiction of State arbitration courts under the New APC. /A. Kelina, E. Abrossimova

Government Clarifies Issuance of Labor Permit for Foreign Employees

On November 1, 2002, the new RF Law "On the Legal Status of Foreign Citizens in the Russian Federation," dated June 21, 2002 (the "Foreign Citizens Law"), became effective. Since that time, foreign citizens working in Russia, as well as the companies that employ them, have been troubled by a number of issues introduced by the Foreign Citizens Law. The requirement that foreign employees obtain work permits has been one of the primary reasons for concern since its application was not entirely clear. On December 30, 2002, the RF Government issued Regulation No. 941 "On the Procedure for Issuance of Labor Permits for Foreign Citizens and for Individuals Without Citizenship" (the "Regulation"), which clarifies the issue of work permits.

The Regulation provides that the RF Ministry of Interior Affairs (the "MVD") is responsible for the issuance of work permits for foreign employees. Under the Foreign Citizens Law, in order to invite foreign citizens to Russia for the purpose of employment, an employer must first obtain a permit to invite and employ such foreign employees. Having obtained such permit, the employer may proceed with obtaining a work permit for each particular employee. As a general rule, the Regulation provides that the employer must file an application for a work permit with local branches of the MVD, along with a color photograph of the prospective employee and a copy of his or her passport. The Regulation does not list labor contracts among the documents that must be submitted to the MVD. However, according to unofficial information obtained from the Department of Migration of the Moscow Branch of the MVD (the "Migration Department"), the list of documents to be submitted will be expanded in the near future to include, among other things, labor contracts. In addition, employers must deposit to a special bank account of the MVD sufficient monetary funds to ensure the costs of departure of the foreign employee from Russia upon the expiration of employment or expulsion from the country.

Within thirty working days after all of the relevant documents

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have been filed, the MVD must either issue the work permit or reject the application. A rejection may be based either on the grounds that the information submitted by the employer is inadequate or false or on certain other limited grounds established under Section 9 of Article 18 of the Foreign Citizens Law.

The Foreign Citizens Law specifies certain categories of foreign employees that are exempt from the requirement to obtain work permits. Such exempt categories include temporary or permanent resident foreign citizens, teachers invited by Russian educational institutions to lecture, and employees of foreign producers or suppliers which are in Russia to install or service technical equipment imported into Russia. The exemptions granted by previous legislation to foreign highly qualified employees of Russian companies (e.g., a company's general director) have been abolished.

Neither the Foreign Citizens Law nor the Regulation clarifies the status of foreign employees of representative offices of foreign companies accredited in Russia. However, according to unofficial information received from the Migration Department, it is likely that personal accreditation of foreign employees of representative offices of foreign companies will remain sufficient for their employment in Russia, although this issue remains far from clear. /E. Abrossimova

Secured Creditors May Benefit from New Legislative Initiatives

Two new legislative initiatives, one enacted and one under consideration, have the potential to improve the status of secured creditors under Russian law. First, priority rights of secured creditors in bankruptcy proceedings have been improved by certain provisions of the new Bankruptcy Law, as discussed in the July 15, 2002, issue of the *CIS Legal Newswire* (additionally, see above "New Bankruptcy Procedures Introduced"). Such benefits for secured creditors include improving the priority rights of secured creditors (including those holding mortgages) by permitting them to receive proceeds arising from the sale of their secured property ahead of payments to creditors of the same or lower priority class.

Second, the State Duma is currently considering the reduction

of notary fees for mortgages, which could potentially allow mortgages to serve as a more attractive form of security in Russia. A new chapter of the RF Tax Code (the "Draft Chapter"), which modifies the amount and payment of all State duties, has been prepared by the Duma's Budget and Tax Committee for its planned second reading. Among other important changes, the Draft Chapter envisages substantial reductions of notary fees for certification of mortgage agreements. If enacted as currently drafted, the Draft Chapter will: (i) reduce the notary fee rate from its current level of 1.5% of the total value of the mortgaged immovable property to a regressive scale from 0.5% to 0.15%; (ii) establish caps of 20,000 Rubles (approximately US \$625) on the total amount of notary fees for commercial immovable property and 500 Rubles (approximately US \$16) for residential immovable property; and (iii) become effective on January 1, 2004.

Unofficial sources in the Duma have indicated that this part of the Draft Chapter has been strongly opposed by notaries from the outset (having passed in its first reading on April 19, 2001) and continues to meet resistance. However, these same sources believe that it is unlikely that during further consideration of the Draft Chapter by the Duma, the proposed amount of notary fees for the notarization of mortgage transactions will be returned to the current rates. /E. Abrossimova

Law On Unitary Enterprises Adopted

On November 14, 2002, President Putin signed RF Law No. 161-FZ "On State and Municipal Unitary Enterprises" (the "Unitary Enterprises Law"), which had been approved by the Duma on October 11, 2002. The Unitary Enterprises Law significantly expands certain provisions of the RF Civil Code related to unitary enterprises, which are defined as wholly State-owned commercial organizations that lack the right to own the property allotted to them by their owners. The Unitary Enterprises Law amends and expands the three articles of the RF Civil Code that regulate the legal status of unitary enterprises, the rights and obligations of those with a proprietary interest in unitary enterprises, and the procedure for the establishment, reorganization and liquidation of unitary enterprises.

The Unitary Enterprises Law, as well as the RF Civil Code, es-

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establish that a unitary enterprise does not own the assets allotted to it by the enterprise's owner. Instead, the law provides that such an enterprise holds assets under the right of economic management (for both State and municipal unitary enterprises) or operative management (for State enterprises only), and that such assets may not be distributed among the participants, nor otherwise divided. The Unitary Enterprises Law forbids unitary enterprises from establishing another unitary enterprise through the transfer of a portion of its property (*i.e.*, establishing a subsidiary). A unitary enterprise has civil rights corresponding to the subject matter and goals of its activity. A unitary enterprise may participate in other commercial and non-commercial organizations, but may not act as a founding participant of a credit organization.

The Unitary Enterprises Law establishes a list of circumstances pursuant to which the establishment of a unitary enterprise is possible, including when it is necessary: (i) to use property that may not be privatized; (ii) in order to attain certain social goals; or (iii) to produce certain types of goods that are redeemed from turnover or restricted in turnover. Furthermore, the Unitary Enterprises Law states that the minimum amount of charter capital that a unitary enterprise may have is 5,000 times the minimum monthly wage (approximately US \$15,600) for State unitary enterprises, and 1,000 times the minimum monthly wage (approximately US \$3,120) for municipal unitary enterprises. There is no minimum charter capital for other State enterprises. The charter capital must be fully paid within three months after State registration of the unitary enterprise.

The Unitary Enterprises Law also regulates certain aspects of transactions involving unitary enterprises. State and municipal unitary enterprises may manage their movable property independently; however, the management of real property may be effected only with the consent of the property owner. The property owner's consent is also needed for transactions involving the grant of a loan or surety or receipt of a bank guarantee, or other encumbrances, as well as an assignment, a transfer of debt, and a general partnership agreement. The list of transactions that may be effected only pursuant to the property owner's consent can be expanded pursuant to the enterprise's charter. Major transactions, which must be approved by the owner, include those in which the value of the property to be purchased or alienated exceeds either 10% of the charter capital of the unitary enterprise or 50,000 times the minimum monthly wage (approximately US \$156,000).

The Unitary Enterprises Law became effective on December 3, 2002. The charters of existing unitary enterprises may now be applied only inasmuch as they do not contradict the Unitary Enterprises Law, and such charters must be amended to conform to the Unitary Enterprises Law before July 1, 2003. Companies that are subsidiaries of unitary enterprises must be reorganized by means of incorporation before June 3, 2003. /A. Kelina

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