

Russian Law

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In the first month of 2002, the Russian Federation enacted several amendments to the Joint Stock Companies Law and the Profit Tax Chapter of the Tax Code. During the last days of the year, the Russian Federation enacted the new Bankruptcy Law and adopted several amendments to the Trademarks Law. From beginning to end, 2002 was an active year for legal reform in the Russian Federation. This article highlights some of the principal legal developments for the year 2002.

I. Company Law

As the amendments to the Joint Stock Companies Law entered into force in January 2002, Russian company law underwent significant reform throughout the remainder of the year.¹ The amended law grants shareholders preemptive rights at both open and closed subscriptions for additional issuances of securities.² The amendments also allow shareholders to proportionately retain their current shareholding in any new company that is formed as a result of the reorganization of a joint stock company through a division or split-off.³ Furthermore, the amendments no longer allow forced shareholder buy-outs as a result of fractional shares created during a merger or consolidation.⁴

The year 2002 also witnessed the introduction of the Code on Corporate Governance, a comprehensive set of recommendations aimed at protecting the interests of shareholders by promoting responsible corporate governance standards.⁵ Although the code is not legally

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1. SOBR. ZAKONOD. RF, 2001, No. 120- FZ

2. SOBR. ZAKONOD. RF, 2001, No. 208-FZ, art. 7.

3. SOBR. ZAKONOD. RF, 2001, No. 208-FZ, arts. 18(3), 19(3).

4. SOBR. ZAKONOD. RF, 2001, No. 208-FZ, art. 25(3).

5. The final version of the Russian Code of Corporate Conduct (Corporate Governance Code) was presented on April 4, 2002 at the IV Coordination Council for Corporate Governance. Russian Institute of Directors, *Russian Code of Corporate Conduct* (Apr. 4, 2002), available at http://www.rid.ru/db.php?db_id=516&l=en.

binding, it acts as a “how-to guide” for Russian stock exchange rules. The Federal Commission on the Securities Market recommended that all joint stock companies operating in Russia provide a section in their annual reports detailing their level of compliance with the code.⁶

II. Labor Law

A new Labor Code also came into force in February 2002.⁷ The new Labor Code represents a more realistic balance between the rights of employees and the needs of employers in a market-oriented economy. The code extends the grounds for unilateral termination of employment agreements by the employer, significantly curtails the powers of trade unions, allows greater use of fixed-term contracts and extended probation periods for certain categories of employees, and introduces new procedures for collective labor disputes. For the benefit of employees, the Labor Code provides new security for the timely payment of wages,⁸ greater protection of employee personal data, and more detailed regulation of workplace health and safety.

The Labor Code applies to nearly all employment relationships within the Russian Federation, including those created by subsidiaries, branches, and representative offices of foreign legal entities.⁹

III. Tax Reform

Effective January 1, 2001, the tax on personal income was changed to a flat tax and decreased to a rate of only 13 percent,¹⁰ which replaced the previous progressive rates that scaled as high as 30 percent. Administration of the flat tax was fine-tuned in 2002 with the focus of reform shifting to the taxation of business. The new Profit Tax chapter of the Tax Code, which became effective January 1, 2002,¹¹ modernized the way business operations were taxed in Russia. The new profit tax regime brought the focus of profit taxation closer to the concept of real economic gain and away from the poorly defined target of residual earnings. The new provisions now permit businesses to use the accrual method of accounting, which recognizes income and expenses when they are earned, rather than when cash is exchanged. It also contains improved rules regarding allowable deductions, depreciation, investment financing, and leasing. General profit tax rates dropped significantly, by roughly a third, to just 24 percent.¹²

6. FSCM Resolution of April 4, 2002, *On Recommendations with Respect to Application of the Code of Corporate Conduct*, Directive No. 421/r.

7. SOBR. ZAKONOD. RF, 2001, No. 197-FZ.

8. Wages must be paid every two weeks. Employees may seek compensation for any delay and if salary is delayed more than fifteen days, employees can refuse to work until paid in full. SOBR. ZAKONOD. RF, 2001, No. 197-FZ, arts. 136, 142.

9. The Code does *not* apply to military servicemen, members of boards of directors (unless there is a corresponding employment agreement), people working under civil law agreements, or other persons as established by law or an international agreement. SOBR. ZAKONOD. RF, 2001, No. 197-FZ, arts. 10, 11.

10. SOBR. ZAKONOD. RF, 2001, No. 117-FZ, ch. 23, art. 224.

11. *Id.* at ch. 25.

12. SOBR. ZAKONOD. RF, 2001, No. 117-FZ, art. 284(1).

IV. Banking & Currency Control

In July 2002, the Russian Federation enacted a new law regarding the Central Bank.¹³ This law brought the Bank under closer government scrutiny by introducing a new management structure. Basically, the Central Bank's board of directors is divested of certain governing functions, which are assigned to the National Banking Council (Council).¹⁴ The Chairman of the Central Bank along with appointees of the President, Cabinet, State Duma, and Federation Council comprise the Council. The Council's decision-making powers include the Central Bank's expenditures and profit distribution. Also, the new law significantly reduces the scope of the Central Bank's profit-oriented activities by curtailing its participation in credit organizations and other legal entities.

Relaxation of currency controls continued in 2002. New amendments to the Central Bank directives allow Russian resident individuals to transfer foreign currency to and from the Russian Federation to cover current expenses not related to business activity.¹⁵ Additionally, transfers of funds by Russian residents to foreign accounts can now generally be conducted without opening a current foreign currency account with a Russian bank.¹⁶

Following court proceedings in which one of its instructions was declared unconstitutional,¹⁷ the Central Bank issued a new Directive that authorized residents to sell the compulsory portion of their export proceeds (currently 50 percent), not only on the Interbank Currency Exchange, which is partially owned by the Central Bank, but also to authorized banks or on the over-the-counter Interbank market.¹⁸

Since the 2001 ratification of the 1990 Strasbourg Convention on Laundering, Search, Seizure, and Confiscation of the Proceeds of Crime, Russia has continued to implement legislation giving it control over monetary operations. Demonstrating the continued effort to further develop controls over money laundering in Russia, numerous laws and regulations were enacted during 2002, including legislation that outlined the powers of the Ministry of Finance's Financial Monitoring Committee,¹⁹ the internal control requirements for securities brokers,²⁰ and the internal control requirements for money funds.²¹

13. SOBR. ZAKONOD. RF, 2002, No. 86-FZ.

14. The Council was formally established back in 1994, but had no real powers.

15. Central Bank Directive No. 1188-U, *On Amending Normative Acts of the Bank of Russia in the Sphere of Currency Regulation and Currency Control*, issued Aug. 20, 2002, effective Oct. 6, 2002.

16. *Id.*

17. Decision of the Supreme Court of April 1, 2002, No. GKPI 01-1709, *affirmed by* Decision of the Cassation Division of the Supreme Court No. KAS 02-230. The Supreme Court's decision invalidated provisions of Central Bank Instruction No. 7 from 1992, "On the Procedure for Mandatory Sale by Enterprises . . . of a Portion of the Foreign Currency Proceeds. . ." The Central Bank appealed this decision to the Cassation Chamber of the Supreme Court. The Cassation Chamber rejected the Central Bank's appeal, leaving the original decision unchanged.

18. Central Bank Directive No. 1192-U, *On the Procedure for Sale of Foreign Currency on the Domestic Market of the Russian Federation*, issued Sept. 5, 2002, effective Dec. 1, 2002.

19. Government Resolution No. 211, *On Approval of the Regulation on the Committee of the Russian Federation on Financial Monitoring*, issued Apr. 2, 2002, effective Apr. 10, 2002.

20. Federal Commission on the Securities Market Regulation No. 613/p, *On Methodical Guidelines to Follow by Participants on the Securities Market to Meet the Requirements of the Federal Law 'On Countermeasures with respect to Laundering Revenue Derived from Criminal Activity'*, dated June 3, 2002, effective June 28, 2002.

21. Government Resolution No. 983-p, *On Developing of Internal Control Rules by Organizations Operating with Monetary Funds or Other Property to Meet the Requirements of the Federal Law 'On Countermeasures with respect to Laundering Revenue Derived from Criminal Activity'*, dated July 17, 2002, effective July 30, 2002.

V. Bankruptcy Law

In December 2002, the Russian Federation enacted a new Bankruptcy Law.²² This law provides a more reasonable balance between the interests of creditors and their insolvent debtors and should make certain abuses that had occurred under the previous 1998 Bankruptcy Law more difficult.

The new Bankruptcy Law significantly increases the minimum threshold for a creditor's bankruptcy claim to RuR100,000 by requiring that the debt be at least ninety days overdue. Creditors are now required to send a copy of their claim to the debtor, thus giving the debtor earlier notice of the action. Bankruptcy procedures may be terminated at any time if the debtor pays all claims of record. Equally important, the new law establishes a financial rehabilitation procedure,²³ which, in certain cases, will allow the debtor's governing bodies to maintain control of the debtor during bankruptcy proceedings. The financial rehabilitation procedure is initiated by a court order, which sets out the conditions of the rehabilitation regime. The regime will prescribe a repayment schedule, which is not to exceed two years.

The new law also readjusted the priority of creditors' claims. Unsecured claims are now subject to satisfaction in the following order of priority: (1) personal tort claims; (2) claims for outstanding wages, severance pay, and authors' royalty; and (3) claims from other creditors.²⁴ Supporting the development of mortgage lending in Russia, the law now carves out secured claims, which were ranked in the 1998 Bankruptcy Law as third priority, and provides that they shall be satisfied out of the pledged assets' value before any other creditors' claims.

The new Bankruptcy Law has empowered the debtors' shareholders by allowing them to participate in both the creditors' meetings as an observer and also in the rehabilitation, restructuring, and amicable settlement procedures that attempt to avoid bankruptcy liquidation. Previously, shareholders had no rights during the bankruptcy proceedings.

VI. Agricultural Land Reform

Russia's new Farmland Law was adopted in July 2002 and came into force in January 2003.²⁵ For the first time since Soviet collectivization, the Farmland Law will enable the acquisition of full private rights to Russian agricultural land.

The Farmland Law also provides terms and conditions for the transfer of state and municipally owned farmland into leaseholds and private ownership by Russian individuals and legal entities. Under the law, foreign individuals and legal entities with more than 50 percent foreign participation will only be able to acquire leasehold interests in farmland.²⁶ The law defines the specific requirements for a transfer of interest in farmland and expressly allows farmland to be mortgaged.

22. SOBR. ZAKONOD. RF, 2002, No. 127-FZ.

23. *Id.* ch. V.

24. *Id.* art. 134(4).

25. SOBR. ZAKONOD. RF, 2002, No. 101-FZ.

26. *Id.* art. 3.

VII. Intellectual Property Protection

Intellectual property legislation was further revised throughout 2002. New amendments to the Trademarks Law²⁷ introduced a definition of counterfeit goods²⁸ and provided new remedies for trademark infringement, including the destruction of infringing products and packaging.²⁹ In December 2002, technical changes were also made to the laws relating to the Legal Protection of Software and Databases.³⁰ Equally significant, the assignment of software property rights no longer requires State registration; however, the parties may still agree to register such assignment.³¹ In addition, a new Code of Administrative Offences introduced for international property infringers harsher sanctions.³²

VIII. Judicial Reform

Significant judicial reform also took place in 2002. The Russian Government is now in the first stages of its "Federal Program for Development of Judicial System in Russia 2002–2006."³³ This program is designed to bring the Russian court system into compliance with the Russian Constitution, international law, and the standards of the Council of Europe.

The new Arbitrazh Procedure Code entered into force in September 2002.³⁴ The code clarifies the jurisdiction of arbitrazh (commercial) courts by specifying special jurisdiction over legislation involving corporations and, consequently, over disputes between companies and their shareholders or participants. The jurisdiction of the arbitrazh courts, however, does not include labor disputes, which are to be heard by the general jurisdiction courts. Also, Arbitrazh courts are now specifically empowered to decide matters pertaining to the enforcement of foreign court decisions or arbitral awards related to commercial matters. The code introduces numerous rules relating to the proceedings themselves. For example, the code extended the scope of permissible evidence and also empowered the courts to award new interim measures pending a final decision.³⁵

In November 2002, the new Civil Procedure Code was adopted.³⁶ It entered into force in February 2003. The code grants the general jurisdiction courts jurisdiction over disputes arising out of civil, family, inheritance, labor, housing, land, ecology, and certain other legal relationships. It also introduces changes to procedures governing the burden of proof, the rights and obligations of witnesses, and the conduct of judicial examinations. The code curtails the right of prosecutors to participate in the proceedings by limiting their involvement to cases concerning the public's interest.³⁷

27. SOBR. ZAKONOD. RF, 2002, No. 166-FZ.

28. *Id.* art. 4(2).

29. *Id.* art. 46(2).

30. SOBR. ZAKONOD. RF, 2002, No. 177-FZ.

31. *Id.*

32. SOBR. ZAKONOD. RF, 2001, No. 195-FZ, art. 14(10).

33. SOBR. ZAKONOD. RF, 2001, No. 805.

34. SOBR. ZAKONOD. RF, 2002, No. 95-FZ.

35. SOBR. ZAKONOD. RF, 2002, No. 138-FZ art. 91.

36. SOBR. ZAKONOD. RF, 2002, No. 138-FZ.

37. SOBR. ZAKONOD. RF, 2002, No. 95-FZ, art. 45.

The new Criminal Procedure Code,³⁸ which took effect in July 2002, replaced the 1960 Soviet code. Adoption of a new code was a condition to Russia's membership in the Council of Europe, which it joined in February 1996.³⁹ At the expense of the prosecutor's office, the code gives greater power to the courts and defendants in an attempt to institute a balanced adversarial system. For example, the new code allows defense attorneys to question individuals, to request documents from various institutions, and to invite experts to court.⁴⁰

38. SOBR. ZAKONOD. RF, 2001, No. 174-FZ.

39. EUR. PARL. OPINION, No. 193 (1996), *available at* <http://assembly.coe.int/Documents/AdoptedText/ta96/EOP193.HTM> (last visited Mar. 6, 2003).

40. SOBR. ZAKONOD. RF, 2001, No. 174-FZ, art. 53.