Recent developments of Russian law
November 2011

This edition includes topics of interest to the corporate, insurance and construction sectors.

Igor Orlov writes on the changes in Russian law on foreign investments in sectors of strategic importance, including a change in the law on foreign investment in business entities of strategic importance for national defense and security. The principal effect of the changes is to simplify the procedures required when concluding transactions with foreign investors.

Dmitry Milyutin introduces us to the law on insider information signed on 27 July 2010 and came into effect on 27 January 2011. Because of the complexity of the subject it has already resulted in a plethora of acts of clarification from the Federal Financial Markets Service.

Polina Kondratyuk adds her voice to the debates on mandatory professional liability insurance and provides an insight into the diversity of liability insurance, the regulatory framework into which professional liability insurance fits and court practice on liability insurance.

Yulia Babkina considers migration law in connection with the work permit requirements under Article 13.4 of the law governing the legal status of foreign citizens in Russia and what foreign manufacturers/suppliers of equipment who undertake to install or service the equipment need to do to avoid the risk of prosecution by the Federal Migration Services.

Contents
Changes to Russian legislation on foreign investments Page 2
Law on insider information Page 3
Legal framework and application of professional liability insurance Page 4
Obviating the necessity to obtain work permits for foreign workers employed to install/commission/repair in Russia of equipment manufactured or supplied by a foreign country Page 6

Máire Ní Aodha
Head of the Moscow Office

The merged firm of Clyde & Co and Barlow Lyde & Gilbert

This document introduces considerable changes to both the main federal laws specifically related to activities of foreign investors in Russia and, according to commentators, these changes simplify the procedure of concluding transactions with such investors.

First, in accordance with similar changes introduced to both laws, prior approval (according to the procedure stipulated by articles 9-12 of the Law “On the procedure for foreign investments in business entities of strategic importance for national defense and security”) is no longer required for transactions involving international financial organizations established in accordance with international treaties to which the Russian Federation is a party or international financial organizations with which the Russian Federation concluded international treaties. The list of such organizations is approved by the Russian Government. According to press reports, this list has already been prepared and is being approved by departments at the moment. It is likely to be approved by the Russian Government in the near future.

Furthermore, such preliminary approval will no longer be required for transactions involving foreign companies controlled by Russian owners, more specifically, by the Russian Federation or Russian citizens being tax residents of the Russian Federation in accordance with the Russian law (except those with dual citizenship).

Secondly, changes concerning the procedure of transaction approval are introduced to the Law “On the procedure for foreign investments in business entities of strategic importance for national defense and security”.

On the one hand, the procedure is simplified. Thus, if earlier the transaction was approved on condition of concluding an agreement with a foreign investor stipulating some obligations of the investor, the case materials were reviewed in a meeting of government commission after conclusion of such agreement, after which the commission made a relevant decision. Now the decision on transaction approval is made upon the fact that the agreement is made, without repeated submission of materials to the government commission. It is expected that this change will considerably reduce the time for reviewing investors’ applications.

On the other hand, there are changes that in some way make the procedure longer and more complicated. Thus, in certain circumstances not only federal security agencies take part in the process, but also the Ministry of Defense of the Russian Federation; furthermore, the time period for certain actions has been increased (e.g., the time for reviewing applications from authorized bodies by the above-mentioned federal executive authorities in the field of safety assurance and the Ministry of Defense has been increased from 20 to 30 days).

Thirdly, some types of activities have been excluded from the list of activities strategically important for national defense and security, such as deployment, construction, operation and decommissioning of nuclear plants, radiation sources and nuclear and radioactive materials storages, radioactive waste storages, carried out in the civilian sector of the economy by business entities for which such activity is not a main activity; as well as activity of banks, the charter capital of which does not include a share held by the Russian Federation, related to the distribution and technical maintenance of encryption (cryptographic) tools and rendering services in the field of information encryption.

Finally, the minimum share of a foreign investor in Russian business entities of strategic importance, defined as a share granting control over such entity, has been increased from 10 to 25 percent. Accordingly, the minimum share of a foreign investor in subsoil user companies (exploiting subsoil sites of federal importance), where transactions for the purchase of such share are subject to approval, has also been increased from 10 to 25 percent. It is expressly stated that transactions for the purchase by a foreign investor of stocks (shares) in the charter capital of such companies are not subject to approval if, as a result of such transactions, the participation interest of such foreign investor in the charter capital of the company is not increased.

The Law was first introduced to the State Duma in 2010 and has been expected by the members of Russian stock market for a long time. In spite of the fact that the Law concerns many members, its enactment was not followed by an active information campaign.

The Law was signed by the President of Russia on 27 July 2010 and came into force from 27 January 2011. The Law defines insider information, determines the persons classified as insiders and the procedure for disclosure of information.

Insider information is defined by the Law as accurate and specific information that was not previously known and publication of which can have significant impact on the cost of financial instruments, foreign currency and goods. Such information includes commercial, official, bank secrets, secrecy of communication in relation to postal and money transfers.

The Law also determines actions which constitute market manipulation. Such actions include, among other things, intentional dissemination of deliberately misleading data which results in considerable change of cost, demand, supply or volume of bidding.

The Law defines insiders as a range of state bodies and organizations that should disclose or provide insider information on their websites – this concerns the Central Bank, federal and regional executive bodies, municipalities, etc.

In August 2011 the provisions which came into effect oblige organizations to maintain a list of insiders and provide the list to the securities exchange. However, the penalty for violation of insider legislation will be applied only after the transition period expires, i.e. from 1 January 2012. Until then market players have the opportunity and time to bring their activity into compliance with the requirements of the Law. During the transition period (until 31 December 2011) companies trading on the securities market should prepare the lists of insiders and provide them to the securities exchange. The securities exchange, in their turn, should inform the supervisor about insiders’ operations. All notifications should be sent to the Federal Financial Markets Service within the entire transition period, but not later than 31 December 2011.

The Law lists 13 insiders’ categories that include companies which issue securities, manage assets, major market members that dominate a market of certain goods. Of the market infrastructure, insiders include exchanges, clearing organizations, depositaries and banks via which settlements on exchange transactions are made. A separate category is professional stock markets members: brokers, dealers, managers, auditors, appraisers and insurers.

Persons who own blocking share holdings (25% + 1 share) are also considered to have access to insider information, as well as persons who are members of managing bodies (members of the board of directors, auditing committees, etc.)

Employees of state bodies and regulatory bodies are also considered to be holders of insider information – according to the Law, federal executive bodies and the Bank of Russia are included in a single category.

Separate category includes rating and information agencies that disclose information of issuers, professional market members, Central Bank of Russia.

The last category includes individuals who have access to financial information of previous insider categories on the basis of labor and civil law contracts, i.e. employees of organizations with insider information are classified as insiders (the Law does not specify the level of employee’s position).

It is obvious that in order for the Law to be efficient, a vast regulatory framework of bylaws to clarify and specify the provisions is needed. Currently the Federal Financial Markets Service has already produced about 20 statutory acts with clarifications. In particular, the orders specifying the list of information relating to insider information were elaborated, as well as disclosure requirements for issuers.

In conclusion, we note that the important criteria for the efficacy of the Law will be its application by market members, state bodies, law enforcement bodies and courts.
Debates about the necessity and practicality of certain types of mandatory professional liability insurance occur in Russia every once in a while. This is particularly so in connection with socially important spheres, such as realtors professional liability insurance on the issue of enforcement of citizens’ housing rights, or medical professional liability insurance in case of medical malpractice. The development of liability insurance involves not only broadening the range of mandatory but also voluntary insurance which are actively available abroad. This article analyses the diversity of types of insurance, the system of legal regulation and the court practice on professional liability insurance.

Professional liability insurance (PLI), or Errors and Omissions (E&O), is a relatively new insurance product for the Russian market. This type of insurance is widely used in Western Europe and USA and has been available for sometime now.

The object of liability insurance of a person engaged in a professional activity is, as a rule, monetary risks related to their liability for wrongful professional actions or harm caused by such actions.

Russian legislation does not classify PLI as a separate category. At the same time the Civil Code of the Russian Federation distinguishes between two types of liability insurance, namely:

1. liability insurance for causing harm (article 931 of the Civil Code); and
2. liability insurance for breach of contract (article 932 of the Civil Code);

Liability insurance in accordance with article 932.1 of the Civil Code for breach of contract is permitted only in cases prescribed by law.

As almost any professional activity is carried out on the basis of a contract for work performance or rendering services, the limitation stipulated by article 932.1 of the Civil Code is applied to PLI contracts. However, PLI contracts usually cover delict (tort) liability too. Therefore, the rules governing both types of liability may be applied to PLI contracts.

In practice we often see PLI contracts which cover both delict and contractual liability. When making such contracts it is important that the insured bear in mind the above-mentioned limitations for contractual liability, as the consequences of inconsistencies can be draconian, namely the PLI contract may be declared void in whole or in part.

Currently many insurers offer their clients different liability insurance products that allow both voluntary insurance and mandatory insurance of insured’s liability in accordance with the law. The most popular products in Russia are insurance of the liability of notaries, adjusters, court-appointed trustees, tour operators, advocates, medical professionals, auditors, directors and officers (D&O), builders, customs brokers, temporary storage warehouse and customs warehouse owners, and customs carriers.

According to statistical data from public sources, in Russia there are about 65,000 advocates, 8,000 notaries, 8,000 court-appointed trustees, 100,000 adjusters, 4,500 tour operators, 600,000 doctors, 6,000 auditing companies and 400 customs brokers. They are all potential clients for PLI.

As the market evolves, business entities require an increasing variety of types of insurance for different types of activity. In particular, the law does not prescribe the possibility of contractual liability insurance for carriers, forwarding agents, security guards, accountants, etc., and there is a need for such insurance.

Though many lawyers do not consider carrier’s and forwarding agent’s liability to be professional liability, we would like to mention this type of insurance in this article, as it is in highest demand on the market. Because of prohibition in article 932.1 of the Russian Civil Code such insurance contracts were, for a long time, declared void by courts. However, following the ruling of the Presidium of the Supreme Arbitrazh Court of 13 April 2010 No. 16996/09, the position on carriers’ and forwarding agents’ liability insurance contracts has changed. In this ruling the Supreme Arbitrazh Court concluded that the disputed contract of insurance of the insured’s monetary risks was related to the insured’s responsibility to compensate in accordance with the procedure stipulated by Russian civil law for actual damage inflicted to property interests of third parties during the performance of the insured activity, that it contained the elements of different property insurance types stipulated by article 929 of the Russian Civil Code and, therefore, did not contradict the law.

In fact, the Presidium of the Supreme Arbitrazh Court, taking into account the market interests, passed the ruling which circumvents the prohibition in article 932.1 of the Russian Civil Code. In doing so the Court brought carriers’ and forwarding agents’ liability insurance into the legal framework.
In relation to professions for which neither the law nor judicial law enforcement officials permit contractual liability insurance contracts, insured have to make insurance contracts for liability for causing harm and include contractual liability insurance terms, which may later be contested in court. Recently there has been extensive court practice on carriers’ and forwarding agents’ liability insurance contracts. However, as at present there are very few disputes before the courts concerning PLI, it is difficult to comment on court practice in this sphere of insurance.

We are aware of some court cases connected with notaries’ liability insurance. In one such case the insurer was a named defendant and the compensation was recovered from the insurer (Ruling of Moscow city court (MCC) of 8 September 2011 in Case No. 33-25471). In another case where the notary’s liability insurer was involved as a third party, the notary’s representative in court claimed that the notary was not the appropriate defendant and that the appropriate defendant was the liability insurer. In that case the court did not replace the defendant and ruled that the notary was liable to pay the damages (Ruling of Moscow city court (MCC) of 18 May 2011 in Case No. 33-14864).

As advocates we have come across cases where the advocates’ principals attempted to collect the insurance indemnity from the advocate’s liability insurer. In all the cases the principals sought to recover from the insurer unearned advances paid to the advocates. The courts dismissed these actions and ruled that the responsibility to return advance payments is not a liability measure and is not covered by the PLI contracts.

There are also very few court cases in the legal databases relating to court-appointed trustees’ liability insurers. At present amounts collected by courts in such cases from insurers do not exceed one million rubles.

There are a few court cases in relation to adjusters’ liability insurance. Most attempts to collect insurance indemnity have failed; the courts refused collection, usually because the connection between adjusters’ actions and loss occurrence could not be proved. There are far more cases concerning tour operators’ liability insurance than those mentioned above. Most such claims are determined by the courts of general jurisdiction as the claims are, in general, brought by individuals, and insurance indemnity is often collected.

Actual court cases in relation to doctors’ liability insurers are very few, notwithstanding information about tragic consequences of medical malpractice constantly appearing in media reports. The main reason for this situation is the lack of insurance contracts in this field. The reluctance of the medical profession to insure their liability is probably connected with the fact that insurance options in this sphere are considerably restricted by law (e.g. Russian law “Fundamentals of Russian legislation on citizens’ health care”), which provides that “medical and pharmaceutical employees have a right to insure professional errors which result in inflicting harm or damage to individual’s health, provided that this harm or damage is not connected with negligent or reckless performance of professional duty”, while most incidents of injury are due precisely because of the excluded “negligent or reckless” conduct.

Currently a draft law “On mandatory insurance of medical organizations’ civil liability to patients” is under consideration. Passing this law is planned for 2013. Entry into force of this law would significantly expand the market for medical negligence PLI and also increase the degree of protection of consumers of medical services.

In summary, a brief review of court practice shows that at the moment only carriers’ and forwarding agents’ liability insurance really works and is widely used in Russia. Insurance policies for other PLI types, though they are available on the market, are not in great demand. As the court practice usually reflects topical problems of certain insurance types, the fact that there are almost no court disputes in relation to PLI unfortunately does not prove an absence of problems in this sphere but rather a lack of demand for such insurance products. Nevertheless, gradual expansion of mandatory liability insurance for different professions provides optimism for the future of PLI on the Russian market.
Obviating the necessity to obtain work permits for foreign workers employed to install/commission/repair in Russia of equipment manufactured or supplied by a foreign company

Yulia Babkina, Associate

Generally contracts for the design, manufacture and / or supply of technical equipment includes a provision that the manufacturer / supplier undertake the installation, commissioning (start up), integration into the technological process, testing and initial operation of the equipment. For such works the manufacturer / supplier invariably wishes to use its own resources, in particular its own employees.

For a foreign manufacturer / supplier to Russia which wishes to use its own employees or foreign independent contractors to implement the above processes, it will have to consider whether it is required to obtain work permits for such employees or independent contractors and whether Russian employment law will apply to such workers for the duration of their work in Russia.

Under Federal law No. 115-FZ dated 25 July 2002 “On The Legal Status of Foreign Citizens in the Russian Federation” (“Law No. 115-FZ”) an employer engaging foreign workers must obtain a permit to do so (Article 13.2 of Law No. 115-FZ) and the foreign worker engaged under an employment contract or civil law contract for services to perform the works also must have a work permit (Article 13.4 of Law No. 115-FZ)

However, there are exceptions to the general rule under Article 13.4 of Law No. 115-FZ requiring foreign workers to have a work permit, and one such exception is that foreign workers employed by the foreign manufacturer or supplier of the equipment to perform installation, etc of the equipment in Russia do not require a work permit (Article 13.4.4) of the Law No. 115-FZ


Thus, in order for the exception to apply the foreign worker must be employed by a foreign legal entity and that foreign legal entity must be the supplier or manufacturer of the equipment which is to be installed, commissioned, tested, etc., in Russia.

If the foreign manufacturer / supplier sends individual contractors to Russia to carry out the installation, etc, then such individual contractors will require a work permit as such workers will not fall within the definition of employee under the Russian Labour Code (i.e. an individual who is party to a labour contract, the subject of which is the personal performance of certain works on an ongoing basis for a named employer in exchange for a salary with the employer providing the working conditions).

A consequence of a foreign company sending to Russia its employee as opposed to an individual contractor to perform the installation, etc, is that Russian employment law will apply to the employee’s work in Russia, notwithstanding such work is performed under a contract of employment with the foreign company.

If, however, the foreign manufacturer / supplier sends its individual contractors (as opposed to employee), then Russian employment law would not apply due to the legal nature of its relationship with the contractor, but such contractor would need a work permit to perform the works in Russia and the Russian buyer or Russian Branch office of the foreign manufacturer / supplier would need a permit to engage foreign labour.

In order to ensure that any challenge by the FMS to the second part of Article 13.4.4) of Law No. 115-FZ (the foreign employer must be the manufacturer / supplier of the equipment), the contract between the Russian company using the foreign equipment and the foreign manufacturing / supply company should expressly state the obligation of the foreign company to install, or service, or warrant maintenance or perform post-warranty repair of the equipment (whichever is appropriate). Also, the contract should include a detailed list of the equipment, details of the manufacturer / supplier of the equipment and the production sites where the equipment is to be used. Russian courts often refer to formal deficiencies in such contracts (for example if the contract submitted to the court does not have the attachments referred to in its text or specify the equipment to be installed or the work sites where the equipment is to be installed), to uphold FMS rulings under Article 13 of Law No. 115-FZ.
Non-compliance with Law No. 115-FZ is an administrative offence under Article 18 of the Russian Administrative Offences Code (carrying out labour activity without a work permit).

Currently, the penalty for an employer for such an offence is an administrative fine between 250000 and 800000 rubles for each case of such engagement, or administrative suspension of activity for a period up to 90 days (Article 18.15 of the Administrative Offences Code), and for the foreign worker an administrative fine between 2000 and 5000 rubles with or without administrative deportation from the Russian Federation (Article 18.10 of the Administrative Offences Code).

In summary, Russian entities which import equipment for use in its business and plan long-term cooperation with the foreign manufacturer / supplier for the installation and operation of this equipment should take particular care to ensure its paperwork is in order to avoid the risk of an administrative prosecution with financial consequences of payment of a fine and suspension of activities or having to obtain a permit to engage and use foreign workers and a permit for the foreign workers.