

# **1. RUSSIA - AN OVERVIEW**

## **1.1 Geography**

The Russian Federation stretches across Eurasia from Eastern Europe to the Pacific coast. After the collapse of the Soviet Union, Russia became the largest country in the world in terms of territory.

## **1.2 Population**

The population of the Russian Federation is approximately 143 million. Although approximately 80% of the country's population is ethnically Russian, the Russian Federation is a multinational state and is home to numerous ethnic minority groups, including sizeable Tatar (3.8%) and Ukrainian (2%) populations. Roughly 73% of the population lives in urban areas, and 13 cities have a population of over one million. The largest city in the Russia is Moscow, with a population of approximately 10.4 million, followed by St. Petersburg, with a population of approximately 4.5 million.

## **1.3 Political System**

The Russian Federation is a federal republic consisting of 83 constituent entities. There are six categories of federal constituent entity which, while subtly different in classification, are constitutionally defined as equal members of the federation. The 21 republics (corresponding to the homelands of various ethnic groups) enjoy a certain degree of regional autonomy. The federation is further divided into 47 oblasts (regions), one autonomous oblast (autonomous region), and nine krais (territories) in which four autonomous okrugs (autonomous districts, also delineated for various ethnic groups) are located. Moscow and St. Petersburg are classified as cities of federal significance. In 2000, Russia was further delimited into seven federal super-districts (circuits) with the aim of ensuring federal supervision over regional affairs.

Each constituent entity of the federation possesses its own charter, political institutions and local legislation. Approximately half the constituent entities have signed bilateral treaties regulating the relationship between the regional and federal governments. Significant progress has been made towards greater consistency between the regional and federal legal systems. However, when conducting business transactions at the regional level treaty stipulations should be carefully reviewed as they may assign slightly different rights and privileges to the constituent entity in question.

Constitutionally, the President of the Russian Federation is elected for a four year term (limited to two terms in succession) and is vested with extensive powers, serving as the head of state, the commander-in-chief of the armed forces, and the highest executive authority of the federation. The office of the President also includes the powers of decree and legislative veto, and the power to appoint and dissolve the Government. The President is primarily responsible for domestic and foreign policy and represents Russia in international relations. Furthermore, as of December 2004 the President was granted the authority to directly appoint Russia's regional leaders, subject to confirmation from the regional legislature. The procedure was amended in December 2008: according to the new law, the political party that obtains the majority of mandates in the regional legislature submits three candidatures for the President's consideration.

The Prime Minister oversees the activities of the government and serves as the acting President if the President becomes ill and is unable to carry out the functions of that office. The Prime Minister's authority as acting President expires upon the election of a new President, which would normally be three months after the former President's authority expires.

Since the election of Vladimir Putin to the Russian presidency in May 2000, the country has undergone a number of sweeping political reforms aimed at centralizing power within the federal executive. Mr. Putin was re-elected in March 2004. In March 2008 Putin's designated successor, Dmitry Medvedev, won the general election with an overwhelming majority. In May 2008 Vladimir Putin was appointed Prime Minister.

Legislative power is exercised by a bicameral Federal Assembly, which consists of the Federation Council (upper house) and the State Duma (lower house). Since January 2002, the Federation Council has consisted of two representatives from each federal constituent entity, one from the executive branch appointed by the regional governor, and one from the legislature nominated by the regional assembly. This is different to the previous system, where leaders of the regional legislative and executive branches served on the council *ex officio*. The State Duma consists of 450 members elected nationwide by proportional representation through party lists. Previously 225 of the 450 members were elected in single member constituencies; however, in December 2004 these seats were abolished. The first election under the new rules was held in December 2007. In addition, new rules were introduced governing national political parties, increasing both the minimum number of party members required for registration (from 10,000 to 50,000) and the threshold to secure Duma seats (from 5% to 7% of the national vote).

The lowest governmental level in the Russian Federation is local self-government. Reformed in September 2003, bodies at this level remain relatively new and untested. Current law distinguishes between community-level government and the governments of towns and villages, reforming the roles and responsibilities of each level. However, the overall influence of local self-government depends on how much authority has been delegated to the local level by the regional government. Foreign investors should be aware of the position of local bodies in regions where they conduct business since these bodies may possess limited powers of taxation.

At the top of the Russian judicial system are three high courts: the Constitutional Court, Supreme Court and Supreme Arbitrazh (Commercial) Court. The 19 justices of the Constitutional Court review all constitutional disputes. The Supreme Court reviews civil, criminal, and administrative disputes involving private individuals, while the Supreme Arbitrazh Court reviews commercial disputes and administrative disputes involving legal entities and individual entrepreneurs. Judges for all these courts are appointed for life by the Federation Council on the recommendation of the President.

## **1.4 International Relations**

Russia is still in the process of defining its position in the post-Cold War world. One of the primary accomplishments of Russian foreign policy has been an improved relationship with Western Europe and the United States, although this bond has been severely tested on several occasions. In the past few years Russia has been re-evaluating its foreign policy agenda in response to increased Western involvement in both Eastern Europe and Central Asia.

One of the key pillars of Russian foreign policy has been the Commonwealth of Independent States (CIS), whose membership is comprised of most of the former Soviet republics. Since 1991 the CIS has struggled to establish itself as an effective and integrated body. In August 2008, following the escalation of hostilities between Russia and Georgia over the separatist region of South Ossetia, Georgia announced its intention to withdraw from the CIS.

Recently, Russia has been very active in various Western programs, including the strengthening of the International Non-proliferation Initiative as well the formation of a joint Russia-NATO action plan on international terrorism, which envisages the exchange of confidential information, joint exercises and anti-terrorism training. Internationally, Russia continues to be an active member of all bodies of the United Nations, and retains a permanent seat on the Security Council with veto rights.

Russia has always had close ties with its neighbour and major trading partner, Belarus. In 1997 a supranational entity, the Union of the Russian Federation and the Republic of Belarus, was formed. However, since then the initial enthusiasm for integration has waned and a Union with a single currency remains at the planning stage.

## **1.5 Economy**

The eight years of Vladimir Putin's presidency from 2000 to 2008 coincided with an era of rapid economic growth fuelled by sky-high commodity prices and accompanied by a significant increase in living standards. The government's devaluation of the rouble during the 1998 financial crisis gave local producers significant advantages over their foreign competitors. Local consumption was boosted by the introduction of consumer loans and mortgages. Among the other drivers of economic growth was an increase in the utilization of industrial capacity constructed in the Soviet period. Between 1999 and 2007 GDP rose by an average of 6.8% annually. Real fixed capital investments increased by an annual average of 10% between 2000 and 2007, while real personal incomes rose at an average annual rate of 12%.

Over these years Russia successfully paid off a substantial portion of its foreign debt. In March 2008 the country's gold and foreign currency reserves surpassed US\$500 billion, giving Russia the third largest reserves in the world after China and India. These achievements, in conjunction with prudent macroeconomic policies and renewed government efforts to advance structural reforms, raised business and investor confidence, with new business opportunities emerging in such sectors as telecommunications, retail, pharmaceuticals and the power industry in particular.

However, shortly after Vladimir Putin was appointed Prime Minister, the country's economic fortunes changed. Russia has been badly hit by the international financial crisis in 2008-2009. A slump in commodity prices, collapse of the financial markets, restricted access to external financing, rising unemployment and a consequent drop in internal consumption have shaken the foundations of the Russian economy. Among the industries most seriously affected were the financial services, B2B, IT, real estate & construction, mining & metals and automotive sectors. Experts have voiced concerns as to the soundness of the Russian banking sector given the apparent growth in the percentage of non-performing loans. In 1Q 2009 GDP fell by 9.5 % year on year. The IMF forecasts that Russian GDP will contract in 2009 by 6%.

Since the outbreak of the crisis the government has increased its efforts to safeguard the economy. By April 2009 approximately a third of Russia's foreign currency reserves had been spent on implementing a step-by-step rouble devaluation, which prevented panic and an inevitable run on the banks. The Central Bank has provided commercial banks with liquidity through REPO mechanisms in an attempt to unfreeze the credit market. However, as of April 2009 short-term financing at reasonable rates was still unavailable for most small and medium-sized enterprises. The government has proposed bail-out initiatives for the economy's largest companies with a view to limiting the negative social impact of massive lay-offs. Some banks and financial services companies have been acquired by government-controlled organizations. The authorities have come up with a multi-billion dollar rescue plan for the automotive sector and are subsidizing rates on car-loans for cars produced or assembled domestically. A package of tax initiatives encouraging economic activity has been adopted.

The Economist Intelligence Unit mentions that among the strong points of the Russian economy are comfortable savings levels, very limited exposure to the stock market (less than one million Russians own shares) and low exposure to the mortgage market compared to the US, the UK and the Central and Eastern European countries. On the downside are the drops in real income, real wages, disposable income and retail sales, and the increasing unemployment, which currently stands at between 7 and 8%.

The prospects for an upturn in the Russian economy remain unclear and largely depend on how long the recessions in the US and world economy last. According to the Economist Intelligence Unit, if global demand shrinks and oil prices in 2009 fall below 45-53 USD per barrel (seen as the critical level for the state budget), the rouble will come under more pressure and the recession in the Russian economy may last until Autumn 2010 or beyond.

## **2. PROMOTING FOREIGN INVESTMENT IN RUSSIA**

### **2.1 The Foreign Investment Law**

#### **2.1.1. General Provisions Regarding Foreign Investments.**

The *Constitution of the Russian Federation* (the *Constitution*), the *Civil Code of the Russian Federation* (the *Civil Code*), and other legislation on joint stock and limited liability companies and their insolvency provide the general legal framework for trade and