

exchange rates, interest rates, levels of inflation, or parameters calculated based on an aggregate of such indicators, or on the occurrence of another circumstance is provided by law and relative to which it is unknown whether it will occur or not”, provided that one of the parties to the transaction holds a license for banking operations or a license of a professional market participant. Since then, there have been a number of court precedents in which non-deliverable derivatives have been granted judicial protection.

4.11.2. The ISDA Master Agreement in Russia

The ISDA Master Agreement is often used by foreign companies in contracting Russian counterparties. Such agreements are typically governed by non-Russian law. If Russian law were to apply to the ISDA Master Agreement (for instance, if in the opinion of the respective court the parties did not rightfully choose foreign law to govern their relationship), some of the agreement’s provisions may not be enforceable, while in general the contract would be valid. Russian law does not require a license or similar authorization of any party for derivative contracts governed by foreign law.

4.11.3. Netting

It is unclear whether the netting mechanism would stand in a Russian bankruptcy scenario, since netting is not expressly dealt with by Russian law and Russian court practice has not yet considered it as distinct from set-off of claims. This may lead by analogy to application of the rules for set-off of claims to netting. Set off is not possible after instituting bankruptcy proceedings or if such set off, made within 6 months prior to a bankruptcy petition being filed with the court, led to the preferential treatment of the claims of one creditor¹.

5. COMPETITION PROTECTION LAW

The basic law for antimonopoly regulation in the Russian Federation is the *Federal Law on Protection of Competition* (the “*Competition Law*”), adopted on 26 July 2006, effective as of 26 October 2006. Antimonopoly issues in the Russian Federation are under the auspices of the Federal Antimonopoly Service (the “FAS”).

The Competition Law regulates competition in both the commodities market and the financial services market and includes seven main areas of particular interest to foreign investors:

¹ See Article 103.3 of the Bankruptcy Law

- Abuse of a dominant position;
- Agreements limiting competition;
- State aid;
- Establishment of companies;
- Mergers and acquisitions;
- Unfair competition; and
- Requirements for tenders and selection of a financial organization by subjects of natural monopolies and various state and municipal bodies for provision of financial services under government tenders.

Please note that the regulations outlined in this chapter are effective as of the date of this guide, however, a number of amendments to the Competition Law are expected to be adopted in the next several months, and therefore it is recommended to reconfirm with Baker & McKenzie lawyers whether the regulations of interest to the reader contained herein have undergone any significant changes.

5.1 Abuse of a Dominant Position

Dominant entities are subject to certain restrictions on their activities. Determining whether a particular entity enjoys a dominant position involves a complex evaluation of various factors, the most important of which is the entity's market share.

For entities with a market share of 50% or greater, there is a presumption of market dominance.

Entities with a market share of between 35% and 50% are deemed dominant, provided their dominant position has been established by the FAS.

For entities with a market share of 35% or less, there is a conclusive presumption of non-dominance, with a few exceptions provided by the Competition Law.

The FAS deems a financial organization to be a dominant entity according to the criteria/thresholds set down by the Russian Government together with the Russian Central Bank. A financial organization whose share in any single market in the Russian Federation does not exceed 10%, or whose share does not exceed 20% in a commodity market where the commodity also circulates in other commodity markets in the Russian Federation, may not be deemed dominant.

When determining market share, the FAS may take into account not merely one company in isolation but also the group of companies to which it belongs. The “group” will include all persons/legal entities related by a common controlling share ownership, contractual or other de facto management control.

In addition to the term “dominant position” the Competition Law introduced a new concept of “collective dominant position”, i.e. the collective domination of the market by between three and five independent companies. According to the Competition Law, a participant in this collective domination can occupy only 8% of the market and will be viewed as a violator in case it, together with one or two other participants jointly have more than 50% of the commodities’ market share, or, together with up to four other participants jointly hold more than 70% of the commodities’ market share, and such entities meet certain criteria specified in the Competition Law.

For those in a dominant position, the Competition Law prohibits any of the following activities:

- Setting and/or maintaining of monopolistically high or low prices;
- Withdrawal of goods from circulation if the result of such a withdrawal is a rise of the price of the goods;
- Creation of conditions that place one or more business entities in an unequal position as compared to other entities in their ability to access the market for particular goods (creation of discriminatory conditions);
- Imposition of contractual terms that are disadvantageous to the other party or do not relate to the subject matter of the contract on a contracting party (and which are not economically or technologically substantiated);
- Discontinuance or reduction of production of goods for which there is a consumer demand if it is possible to produce them on a profitable basis;
- Unjustified refusal to enter into a contract with particular customers if it is possible to produce or deliver the relevant goods to such customers;
- Setting different prices on the same goods where it is not economically or technologically substantiated;
- Creation of barriers for market entry or market exit for other business entities; or
- Violation of pricing rules established by legislation.

Some of the above activities may be allowed if the dominant entity is able to prove that the positive effects of a particular activity outweigh its negative consequences pursuant to the criteria set in the Competition Law.

5.2 Agreements Limiting Competition

The Competition Law prohibits agreements, transactions, or other business activities of business entities that lead or may lead to the following:

- Control or fixing of prices, discounts, bonus payments, or surcharges;
- Increase or reduction of prices or the manipulation of prices at tenders;
- Division of the market by reference to territories or according to the volume of sales/purchases, the range of marketable goods, or the range of sellers or buyers;
- Refusal to enter into a contract with particular sellers or customers without economic or technological justification;
- Imposition of contractual terms that are disadvantageous to the other party or do not relate to the subject matter of the contract;
- Setting different prices on the same goods without economic or technological justification;
- Discontinuance or reduction of production of goods for which there is a consumer demand if it is possible to produce them on a profitable basis;
- Restriction of access to the market or the removal from the market of other entities that sell or purchase particular products; etc.

The Competition Law further prohibits other agreements if such agreements lead or may lead to limitation of competition, with the exception of “vertical agreements” (agreements between economic entities not competing with each other, one of which acquires goods or is the potential acquirer, while the other supplies goods or is the potential seller) which are permitted by the Competition Law (“vertical agreements” between economic entities where the market share of each one is less than 20% or “vertical agreements” in written form which are commercial concession agreements).

In certain cases, some of the above-mentioned activities may be permitted if it can be proved that the positive effects of the action, including effects in the socio-economic sphere, outweigh its negative consequences pursuant to the criteria set in the Competition Law, or if it can be proved that federal laws permit such agreements or business activities.

The Competition Law prohibits the so-called “*coordination of economic activities*” by economic entities, if such coordination may lead to restriction of competition. “Coordination of economic activities” is understood as coordination of the actions of economic entities by a third person who does not belong to the “group of persons” at such economic entities.

5.3 State Aid

State aid is new to Russian competition legislation and was introduced by the Competition Law of 2006.

In accordance with the Competition Law, state (or municipal) aid consists in granting an economic entity certain privileges over other market participants, ensuring more favorable conditions for their activity in the relevant market by transferring property and (or) civil rights or providing priority access to information.

The Competition Law regulates the procedure of providing state (or municipal) aid for the following purposes:

- ensuring life activity of the population in Arctic regions and equivalent areas;
- carrying out fundamental scientific research;
- environmental protection;
- cultural development and conservation of the cultural heritage;
- agricultural production;
- support of small businesses engaged in high priority activities;
- rendering social services to the population; and
- rendering social support to unemployed citizens and facilitating employment of the population.

State (or municipal) aid shall be granted with the preliminary written approval of the FAS unless such aid is directly granted by a federal law, a law of a Russian Federation constituent entity or a regulatory act of the local government on the budget for the following year, or is granted from the reserve funds of the executive body of a constituent entity of the Russian Federation or the reserve funds of the local government.

In order to provide state (or municipal) aid, the authority intending to grant the aid submits an application to the FAS for approval to grant such state (or municipal) aid together with (a) a draft act which provides for the granting of the state (or municipal) aid with an indication of the goals and amounts of the aid; (b) a list of the beneficiary entity's activities over the two years preceding the date of the FAS application; and other information as provided for by the Competition Law.

The FAS shall make a decision on the application within two (2) months from the moment it is submitted together with all necessary documents. The FAS may extend the period for its review of the application for a term of up to two (2) months. If the FAS approves the granting of state (or municipal) aid, the authority granting the aid must submit documents confirming observance of the restrictions as indicated in the FAS approval within one (1) month after the aid has been granted.

5.4 Establishment of Companies

The founders of a new company must notify the FAS prior to the establishment of a company only if the charter capital of the company being established is paid by shares and/or property of another legal entity and the company acquires (as payment of the charter capital) more than 25%/50%/75% of such shares or more than $\frac{1}{3}$ / 50% / $\frac{2}{3}$ of such participatory shares, or where the company acquires more 20% of the main production facilities and (or) intangible assets (exclusive of most types of buildings and land plots) of another legal entity, and where the thresholds provided in the Competition Law are met.

According to specific conditions provided by the Competition Law the establishment of a company whose charter capital is paid by shares and/or property of a financial organization may be subject to a mandatory pre-establishment FAS notification. Such conditions are similar to those described above with respect to entities acting in the commodities market but contain certain differences that should be considered separately.

5.5 Mergers and Acquisitions

5.5.1 Mergers

Entities involved in a consolidation or a merger must obtain the prior approval of the FAS if the aggregate asset value of the entities exceeds 3 billion RUR or the aggregate revenue earned by the entities and their “group of persons” from sale of goods during the past calendar year exceeds 6 billion RUR or if either of the entities is included in the FAS Register of Entities with a market share exceeding 35% in the relevant market. The procedures for obtaining such approval are similar to the procedures used for acquisitions.

5.5.2 Acquisition of an Interest, Assets and Rights in a Russian Company

Acquisition of Shares/Participatory Interest in a Russian Company

When an individual, legal entity or group of persons acquires more than 25%/50%/75% of voting shares or more than $\frac{1}{3}$ / 50% / $\frac{2}{3}$ of participatory shares in an entity, such persons, entities or group of entities must receive prior approval from the FAS if:

- the aggregate book value of the assets of the acquirer and its “group of persons” plus the target and its “group of persons” exceeds 3 billion RUR and the balance sheet value of the total assets of the target and its group exceeds 150 million RUR; or
- the aggregate revenue earned by the acquirer and its “group of persons” plus the target and its “group of persons” from sale of goods over the past calendar year exceeds 6 billion RUR and the balance sheet value of the total assets of the target and its group exceeds 150 million RUR; or
- either the acquirer, or any of its “group of persons”, or the target, or any of its “group of persons”, is included in the FAS Register of Entities with a market share exceeding 35% in the relevant market.

Acquisition of Assets in a Russian Company

When an individual, legal entity or group of persons acquires the right of ownership or the right to use the main production (fixed) assets or intangible assets of an entity, if the acquired assets account for more than 20% of the book value of the main

production (fixed) assets and intangible assets of the selling entity, such persons, entities or a group of entities involved in the acquisition must receive prior approval from the FAS if:

- the aggregate book value of the assets of the acquirer and its “group of persons” plus the target and its “group of persons” exceeds 3 billion RUR and the balance sheet value of the total assets of the target and its group exceeds 150 million RUR; or
- the aggregate revenue earned by the acquirer and its “group of persons” plus the target and its “group of persons” from sale of goods during the past calendar year exceeds 6 billion RUR and the balance sheet value of the total assets of the target and its group exceeds 150 million RUR; or
- either the acquirer, or any of its “group of persons”, or the target, or any of its “group of persons”, is included in the FAS Register of Entities with a market share exceeding 35% in the relevant market.

The main production (fixed) assets or intangible assets of an entity taken into account for the purposes of the above calculation do not include land plots and non-industrial purpose buildings, constructions, premises and parts thereof or unfinished construction objects.

Acquisition of Rights in a Russian Company

When an individual, legal entity or group of persons acquires rights conferring the ability to determine the commercial behavior of the target company (including as a result of change of indirect control over a Russian target company) or of the right to perform the functions of its executive bodies, such persons, entities or group of entities involved in the acquisition must receive prior approval from the FAS if:

- the aggregate book value of the assets of the acquirer and its “group of persons” plus the target and its “group of persons” exceeds 3 billion RUR and the balance sheet value of the total assets of the target and its group exceeds 150 million RUR; or
- the aggregate revenue earned by the acquirer and its “group of persons” plus the target and its “group of persons” from sale of goods over the past calendar year exceeds 6 billion RUR and the balance sheet value of the total assets of the target and its group exceeds 150 million RUR; or

- either the acquirer, or any of its “group of persons”, or the target, or any of its “group of persons”, is included in the FAS Register of Entities with a market share exceeding 35% in the relevant market.

In practice, the FAS supervises those offshore mergers or other transactions involving the acquisition of shares, as a result of which indirect control over a Russian entity changes. It is presumed by the FAS that as a result of an indirect change of control of a Russian legal entity, the foreign entity acquiring the shares would obtain rights over the Russian entity which would allow it to determine the conditions of this Russian entity’s business activity.

Depending on the asset value threshold, the acquisitions described above need to be either preliminarily approved by FAS or only notified to the FAS post-closing.

In determining the threshold for asset values, FAS takes into consideration not only the acquirer and the target company, but also all persons (individuals or legal entities) in the acquirer’s “group of persons.” The broad term “group of persons” includes all individuals or legal entities related to the acquirer as a result of controlling share ownership or through certain management contracts, familial relations, and/or other *de facto* control mechanisms.

Where a merger or acquisition takes place between entities in the same “group of persons”, and where preliminary approval by the FAS is required by law, the Competition Law permits the application for preliminary approval to make a post transaction notification to the FAS within 45 days after the transaction is completed. In this case the group structure must be submitted to the FAS no later than one (1) month prior to the transaction, and may not change until after the transaction is completed.

The Competition Law contains separate articles for the acquisitions of interest, assets and/or rights in *financial organizations* which are subject to a pre-acquisition FAS notification, and the articles contain specific conditions and thresholds applicable to such acquisitions concerning financial organizations that should be considered separately.

5.5.3. Procedures and Timing

If the FAS determines that an establishment, merger, or acquisition may restrict competition or strengthen a dominant position, it may request additional information and documentation. The FAS may also require the parties to take measures to ensure competition.

After all documents have been submitted, the FAS has thirty (30) days to review the application or notification. If the FAS believes that the transaction may lead to restriction of competition, the review period may be prolonged for an additional two (2) months, during which the FAS places information about the transaction on its official web-site and invites all interested parties to send their opinions to the transaction.

5.6 Unfair Competition

Unfair competition, namely any actions of commercial entities aimed at acquiring competitive advantages in commercial activity which contradict the Competition Law, business customs, the requirements of good-faith, reasonableness and fairness, which may or have caused losses to other competing legal entities, or damage their business reputation, is prohibited in Russia.

Types of activities, which constitute unfair competition, include:

- distribution of false, inaccurate or distorted information, which may cause losses to a commercial entity or damage this entity's business reputation;
- misleading consumers about the nature, methods and place of production, as well as consumer properties and quality of goods;
- incorrect comparison by a commercial entity of goods produced or sold by this entity with the goods of other commercial entities;
- sale of goods with illegal use of the results of intellectual activity (i.e., intellectual property) and of the means of individualization of a commercial entity, products, or services, such as trademarks, logotypes and other objects of intellectual property;
- receipt, use and disclosure of scientific and technical, production or trade information, including commercial secrets, without the consent of the commercial entity to which this information belongs, etc.

5.7 Requirements for Tenders and Selection of a Financial Organization by Subjects of Natural Monopolies and Various States and Municipal Bodies

The Competition Law provides for a list of actions in conducting tenders (including governmental tenders) which are prohibited if they lead to restriction of competition.

All federal and municipal bodies, bodies of Russian Federation constituent entities and subjects of natural monopolies shall select a financial organization by holding a public tender (in the procedures set down by other federal laws) to render certain number of financial services for them, a full list of which is provided by the Competition Law, and which includes granting credits, rendering services on the securities market and under leasing contracts, attraction of monetary funds of legal entities for deposits, opening and maintaining bank accounts of legal entities, and making settlements with these accounts, etc.

6. TAXATION

6.1 Introduction

Over the past 10 years, Russia has been engaged in a significant reform of its tax system, which has been implemented in phases. This reform has improved procedural rules and made them more favorable to taxpayers, has reduced the overall number of taxes, and has reduced the overall tax burden in the country.

Part I of the *Tax Code of the Russian Federation* (the “*Tax Code*”) came into effect in 1999, dealing largely with administrative and procedural rules. The latest significant amendments to Part I clarified certain administrative and procedural issues raised by over ten years of practice of the application of Part I of the *Tax Code* (in particular, regarding tax audit procedures, procedural guarantees for taxpayers, operations with taxpayer bank accounts and bank liability). Starting January 1, 2009, taxpayers are required to adverse appeal tax inspectorate decisions on a tax audit to a higher-tier tax authority before bringing a court claim. The provisions of Part II of the *Tax Code* regarding excise taxes, VAT, individual income tax, and the unified social tax came into force in 2001, followed by the profits tax and mineral extraction tax provisions of the *Tax Code* in 2002.