



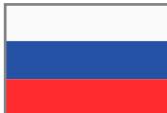
Games Industry Law Journal

Issue 1 (2017/04)



Russia Legal Update

Arseny Seidov



Arseny Seidov is a partner in the Tax law practice group of Baker McKenzie's Moscow office. He has been instrumental in developing optimal tax platforms and structures for various industries, and is consistently recommended by Chambers Global, Chambers Europe and International Tax Review.

Mr. Seidov co-chairs the tax subgroup of the US-Russia Bilateral Presidential Commission's Innovation Working Group, leading the work on drafting laws to remove obstacles and create incentives for businesses that promote R&D and innovation in Russia. For many years he has been a frequent speaker at key tax conferences and seminars organized by the American Chamber of Commerce and the Association of European Businesses. He has authored over 35 professional publications and, since 2007, has been a visiting professor of tax law at the Moscow State Institute of International Relations (MGIMO University).

Contacts

Baker & McKenzie

**Moscow,
Russian Federation**

Tel: +7 495 7872700
Direct: +7 495 7872737
Fax: +7 495 7872701
Cell: +7 903 1402435

**arseny.seidov
@bakermckenzie.com**

Personal data laws - changing interpretations and enforcement

As of September 1, 2015 the personal data of Russian citizens must be initially recorded, stored and updated on databases located in the Russian territory. Initially, Roskomnadzor, the Russian agency with regulatory authority over personal data (“RKN”), interpreted personal data as information relating to unambiguously identified individuals (e.g. information linked to passport details, full name and home address etc.). Thus, the newly introduced localization requirements did not significantly affect the video game industry, which only collected minimum data on Russian gamers. However, this started to change in mid-2016, when RKN started to opine, inter alia, that personal information collected through web analytics tools (such as IP addresses and other technical data) also qualified as personal data.

In 2016, RKN started the actual blocking of reputable multinational services on the grounds of violation of domestic personal data laws. It also dramatically extended its interpretation of personal data, which may require game companies to reconsider their personal data compliance measures in Russia. In particular, the agency sued LinkedIn, alleging violations of Russian personal data laws and, specifically, of the localization requirements. The lawsuit ultimately resulted in the blocking of www.linkedin.com and LinkedIn’s mobile apps in Russia.¹

The changing approach towards technical user data, together with RKN’s approach of blocking websites, may become a major issue for the video game industry in the long term.

¹One of the arguments made by RKN was that LinkedIn collects personal data without consent, particularly, by collecting information about the IP and MAC addresses of all website visitors, not just those who consented to its privacy policy during registration. The Russian courts neither supported nor expressly rejected these arguments, and granted the lawsuit on different grounds. However, the mere fact that RKN raised these arguments in court and subsequently re-affirmed its position in public speeches clearly demonstrates an important change in its interpretation of personal data, which should definitely be taken into account by the industry.

Restricted content, indecency and child protection

Games can contain content that is classified as either prohibited or restricted under Russian law. Prohibited content is not allowed to be distributed in Russia. Its inclusion in online games may lead to their blocking by the competent authorities in Russia, unless said content is deleted from the game. The distribution of restricted content without an appropriate age rating is generally prohibited. Online games may be blocked unless such content is deleted from the game or an age rating is assigned.

If a game contains depictions of homosexual relations, it is also recommended that the age of the person buying the game be verified (e.g., by publishing an age confirmation notice in relation to the online game). Public events relating to games that contain restricted content, and posters promoting such public events, are also subject to special age restriction rules.

Consumer protection and related enforcement practices

When existing or prospective Russian players are targeted, Russian consumer protection laws may apply even if the laws governing the game provide consumers with less protection.

Consumers may submit their claims with local state courts, and such courts normally accept and review these claims on the merits, irrespective of dispute resolution clauses in the terms & conditions and/or license agreement for the game. Furthermore, consumers may file a direct claim against the game's seller and manufacturer. Potential claims are not limited to common compensation of damages (if any), but may also include replacement of a defective game, rectification, refund and compensation for moral harm.

The video game industry nowadays does not have a significant flow of consumer claims. Typically, the compensation amounts awarded to consumers are fairly low (roughly the amount paid for the product and related services). Many claims are settled amicably. At the same time, the current trend in consumer protection enforcement practice is related to increases in compensation amounts and to the engagement of various law-enforcement authorities, especially for high-end and expensive products.

The amount of practical risk increases dramatically if a game is played with special equipment sold together with the game or separately. Irrespective of the limitations which may be listed in the sales contract or applicable terms of use, such equipment may be subject to mandatory Russian technical regulations, including health & safety, disclosure, and marking requirements.

Cybersports regulation and esports benefits

eSports were recognized as official sports in Russia during the summer of 2016. However, the recognition of eSports is merely the first step in their incorporation into the Russian system of ‘traditional’ sports.² Official rules and detailed sports regulations will also need to be adopted.

As a result of this recognition, general rules for running sports events may also apply to eSports events if they are included in federal, regional or municipal calendar plans of official sporting events. The inclusion of an eSports event into the relevant calendar plan may have its benefits, e.g. budgetary financing at the federal, regional or municipal level, allowance for so-called perimeter alcohol advertising during official sporting events (only until January 1, 2019). If an eSports event is not included into any of the above calendar plans, the relevant rules do not apply to such event.

²This step must be followed by accreditation of an official all-Russian eSports federation by the Russian Ministry of Sports (the completion of this procedure is scheduled for spring 2017).

The principal question is whether professional eSports really need such recognition. Full incorporation into the state system of sports in Russia will most likely lead to a situation where major eSports events would be subject to detailed state administrative rules (e.g., construction requirements, safety and security rules, etc.), which could be highly unattractive from a legal and business point of view. However, having a state system of eSports in Russia with direct assistance from the all-Russian eSports federation may help to expand the popularity of a sport among amateurs, enlarge the target audience, and attract new sponsorship contracts into the industry.

Taxation of gaming revenues

There are no special tax rules relevant to the video game industry as such. Depending on where the publisher is located and how the relationships with consumers are structured, the relevant fees may or may not be subject to Russian 20% profits tax and 18% VAT.³

As of January 1, 2017, Russia has introduced a VAT regime on electronically supplied services (“ESS”). Whether the publisher receives licensing or service revenue from Russian sources, it may qualify as ESS for domestic VAT purposes. Under the new regime, foreign suppliers directly collecting such revenue from Russian individuals are required to register as taxpayers in Russia and pay the VAT themselves through a special e-office opened with the Russian tax authorities.

³In a cross-border context, license fees are generally subject to a 20% withholding profits tax (which can be reduced to 0% under many double tax treaties with Russia). However, if the licensor is located outside of Russia with no taxable presence in the country, and license fees are collected directly from individuals, there is no enforceable mechanism to withhold the tax, since regular consumers do not act as tax agents. If there are Russia-based corporate intermediaries or agents in the cash flow chain, e.g. payment aggregators (and provided they are not regular payment processors performing the technical function of card acquiring), then such businesses may be potentially required to act as such tax agents, and to verify whether the publisher is located in a treaty jurisdiction and eligible for double tax treaty benefits as the beneficial owner of a Russian source licensing income.

If relationships with gamers are structured, for example, as a free license with paid services for additional in-game features, then such service fees are not subject to withholding tax under the domestic tax rules. There would be no need to rely on a double tax treaty, if one exists.

At the same time, starting from 2008, under the Russian Tax Code software use licenses are exempt from VAT. In 2015 the Supreme Court ruled in its landmark case against Mail.Ru Games, the largest domestic online games company, that paid services for organizing in-game time where all the elements of the game have already been provided to the gamer under the free end-user license may not enjoy the VAT exemption.

At the beginning of 2017, the Federal Tax Service issued a guidance letter of a non-binding nature about additional in-game functionality and application of the VAT exemption to in-game currency. The FTS letter seems to support the idea that certain additional “sleeping” game functionality (described as “deactivated data and commands”), which only becomes operational subject to additional payment, can form the subject matter of a separate software license agreement and, thus, may be exempt from Russian VAT. However, the letter is silent on the actual scenarios in which the FTS would consider that certain functionality constitutes such “deactivated data and commands”. Whether a particular publisher may be eligible, in full or in part, to this VAT exemption needs to be carefully explored, keeping in mind the underlying facts specific to the game, its IT architecture, and its licensing terms.

Monetization and payment infrastructure, in-game currency and electronic cash registers

Gamers may place cash on their game accounts via payment terminals operated by different categories of payment agents. According to the Russian anti-money laundering laws, payment agents and other organizations must identify their clients if the latter make a cash payment in favor of a foreign entity or any payment in excess of RUB 15,000 (app. \$260).⁴

⁴ In practice, the identification process is unreasonably complex and makes smooth cash monetization directly by foreign publishers almost impossible. However, there are ways to structure relationships with consumers in such a way that this restriction can be legitimately circumvented.

E-commerce payment processing companies doing business in Russia may be subject to special regulations concerning the national payment system and payment agents. Such regulations might require the publisher to operate special accounts with Russian banks, and to perform other activities. Therefore, it is advisable that publishers perform at least some basic due diligence of their Russian intermediaries providing payment collection and processing services.

Payment structures involving in-game currency, gift cards and vouchers are restricted to those issued by game publishers, Russian banks or other licensed credit organizations in Russia. If they are issued or operated by a third party, or used outside of the game to pay for products (e.g. game-related merchandise) and/or services, then these payment structures could be in breach of financial regulations enforced by the Russian Central Bank.⁵

Starting from July 2017, all Russian game publishers collecting payments with the use of e-commerce payment systems must use electronic cash registers for processing payments online. Such cash registers allow the issuing of electronic receipts to consumers, transmitting all payment data to special processing centers accessed by the Russian tax authorities. All new electronic cash registers must be certified in Russia and registered with the Russian tax authorities.

Branded merchandize market and co-branding programs

As game publishers explore alternative revenue streams, branded merchandise and co-branding of services are becoming more common for the Russian video game market. These include co-branded payment card programs with Russian banks, special cash back and discount programs, branded promotional life insurance offers, and even branded soft drinks and promotional burgers.

⁵ While it is unlikely that this position would be enforced against companies located outside of Russia, it should be taken into account for the activities of Russian distributors, since local payment recipients operating the said in-game currency may be held liable for performing an activity for which they do not have proper authorization.

Launching both licensed merchandise and co-branding programs has become much easier in the last couple of years, thanks to the recent trademark law reform and relatively flexible Russian trademark and copyright laws. At the same time, Russian legislation retains several challenges that should be taken into account.

Although trademark license agreements now become effective upon execution, the relevant trademark licenses still need to be registered with the Russian patent and trademark office (“Rospatent”). Legally structuring such license arrangements may also become an issue for game publishers that do not have trademark protection in the relevant classes of goods or services, or whose trademark applications have not matured to registration yet. Mandatory provisions of Russian trademark and copyright law should also be taken into account, in particular, to avoid license validity issues, to mitigate the trademark licensor’s joint and several liability for licensed products, to have the trademark smoothly recorded with Rospatent, etc.

Game publishers who are considering such options may also wish to extend their Russian trademark coverage in advance, as it takes roughly a year to register a trademark in Russia. Such protective trademark registrations would also be helpful for potential enforcement, as both counterfeit merchandise and the practice of ‘free-riding’ on the reputation of third-party brands appear to be on the rise.

IP enforcement against counterfeit merchandise and unauthorized mods

As game franchises attract new fans, counterfeit merchandise tends to flood local markets. The three most rapidly developing offerings are (i) low-quality imported goods, (ii) online printing platforms that produce merchandise on demand, often using a library of user-generated prints and designs, and (iii) online stores operated by fan communities. These are actively promoted via search engine ads, and social media may supplement or even replace traditional online storefronts for such products.

Another dark and increasingly popular area in Russia is unauthorized mods and cheats. They are frequently distributed on a paid basis in a similar manner via social media, third party platforms, marketplaces, etc.

At least some infringers are potentially friendly and can be persuaded by a plain cease and desist letter. If an infringer cannot be persuaded this way, Russia has a broad set of remedies, including many basic remedies available in the EU: notices of infringement to operators of marketplaces and hosting providers; UDRP proceedings with respect to new generic top-level domains⁶; suspension of new generic top-level domains by registrars or registries in certain cases; etc.

In comparison to the EU, there are a number of tools which are specific to Russia. Despite recent amendments to legislation on attorney activities, which have made the procedure less binding for service providers, most local registrars and hosting providers respond to requests from licensed attorneys to disclose an infringer's identity (i.e. name and residential address). The Court for Intellectual Property Rights and a judge of the Supreme Court have also recently confirmed that in order to benefit from safe harbor provisions, hosting providers need to cooperate with rights holders in identifying the infringers upon their request. Such information proves helpful when seeking to persuade infringers or when taking subsequent enforcement steps.

Another important tool is a court injunction issued by the Moscow City Court in an expedited manner, which may subsequently lead to the permanent blocking of an infringing website.⁷ One AAA game developer has recently used this tool to permanently block an unauthorized online store that was selling game license codes, but it may also be used against various forums containing links, torrent files and file-sharing platforms.

⁶However, Uniform Domain-Name Dispute-Resolution Policy is not available for country code .RU and Cyrillic .RF domain names.

⁷There also is a pending bill aimed at facilitating the blocking of derivative versions of permanently blocked websites and delisting them from search engines.