19. Natural Resources (Oil and Gas/Mining)

Today Russia is one of the largest mineral producers in the world. Russian mineral resources are an important component of its wealth.

19.1 Introduction

Russia differs from other countries where the private ownership of minerals in the ground exists and where land owners have title to all mineral resources located below their land plots. All Russian subsoil resources in the ground, including oil, gas, gold and other minerals, unless extracted, are owned by the Russian state, irrespective of who holds the title to the relevant land plot or holds the relevant subsoil license. Rights to extract subsoil resources can be granted under subsoil licenses which, as a rule, provide that ownership rights to the extracted resources belong to the holder of the relevant license.

19.2 Subsoil Legislation

The Constitution of the Russian Federation stipulates that subsoil-use legislation falls within the joint competence of the federal and regional state authorities. However, in practical terms the regional authorities have competence over deposits of certain commonly occurring mineral resources and insignificant subsoil plots.

The core legal act in the mining and oil and gas domain is the Russian Federation Law On Subsoil Resources dated 21 February 1992, as amended (the “Subsoil Law”). The Subsoil Law provides the general legal framework for the use of subsoil resources in Russia and covers almost all principal issues connected with geological survey, exploration and production/mining of underground resources.

The other principal law governing the use of subsoil resources in Russia is the Federal Law On Production Sharing Agreements dated 30 December 1995, as amended (the “PSA Law”). The PSA Law sets forth the legal framework for Russian and foreign investments in the geological survey, exploration and production of subsoil resources.
The principal piece of legislation regulating operations with precious metals and gem stones in Russia is the Federal Law On Precious Metals and Gem Stones dated 26 March 1998, as amended (the “Precious Metals Law”). The Precious Metals Law provides the general legal framework for the processing, use and disposal of precious metals and stones, and has specific provisions on geological survey, exploration and mining of such metals and stones.

19.3 Subsoil Users

Under the Subsoil Law both Russian and foreign companies may hold subsoil licenses in the Russian Federation, save for licenses for strategic deposits, which may be held by Russian companies only. The licenses for offshore fields may be held only be a Russian company that is at least 50% owned by the Russian state and which has at least five years’ experience of development of offshore fields. Although foreign companies are allowed to hold subsoil rights in respect of non-strategic deposits, in practice there are only a few cases where a foreign company directly holds subsoil rights in Russia. Therefore, foreign companies usually hold subsoil rights to Russian deposits indirectly through their Russian subsidiaries which are allowed to hold subsoil rights to on-shore strategic deposits.

19.4 Licenses

Russia, similarly to many other countries, has adopted a licensing system. Subsoil licenses in Russia include: geological survey licenses, exploration and production/mining licenses and combined licenses (geological survey, exploration and production/mining licenses).

A geological survey license may be granted for a maximum period of 5 years (7-year geological survey licenses can be granted in certain Russian regions) and for 10 years for off-shore fields and can be extended if needed for completion of the works. Exploration and production/mining licenses and combined licenses can be issued for a term equal to the life of the project, however in practice they are usually granted for 20 or 25 year terms and can generally be extended.
provided there are no violations of the license terms and conditions by the license holder.

Geological survey licenses are issued without a tender or auction based on an application of the interested party. Unlike geological survey licenses, production/mining licenses and combined licenses can be granted only through a tender or auction, except (i) when a production/mining or combined license is issued to a holder of geological rights that made a commercial discovery under a geological survey license and (ii) with respect to strategic deposits (subsoil plots of federal significance) included by the Russian Government into the list of strategic deposits to be licensed by decision of the Government without a tender/auction.

Subsoil licenses are issued by the Federal Agency for Subsoil Use (Rosnedra). Rosnedra is in charge of granting subsoil rights with respect to all onshore deposits, except for strategic deposits. Rights to strategic deposits (which include all offshore deposits) may only be granted based on a decision of the Government of the Russian Federation.

19.5 Transfer of Subsoil Rights

Subsoil rights in Russia are not freely transferable. This means that they cannot be sold, pledged or otherwise encumbered. However, the Subsoil Law permits the transfer of subsoil rights in certain instances (except for the transfer of rights to strategic deposits to companies with foreign participation), which makes such rights transferable to a limited extent. Such instances include: (i) transfer of subsoil rights from a parent company to its subsidiary and vice versa and transfer between the subsidiaries of the same parent company; (ii) transfer following a merger of the license holder with and into another company; (iii) transfer following a consolidation of the license holder with another company; (iv) transfer following a spin-off or split-off of a new company. Any such transfer of subsoil rights requires a special decision of Rosnedra. Rights to strategic deposits are not transferrable.
to companies with foreign participation unless otherwise is determined by the Russian Government for a specific deposit.

The above options are often used by subsoil users for structuring their business, as well as for the “sale” of licenses, which is only possible through a sale of the licensee’s shares.

19.6 Strategic Deposits

In 2008 Russia introduced a long-discussed set of restrictions for foreign investors in respect of strategic subsoil plots (subsoil plots of federal significance). Strategic deposits include the following:

- Subsoil plots containing deposits and showings of uranium, diamonds, high-purity quartz, the yttrium group of rare earths, nickel, cobalt, tantalum, niobium, beryllium, lithium, or the platinum group of metals (irrespective of the size of the deposits);

- Subsoil plots containing the following reserves, as evidenced by the State Register of Reserves, starting from 1 January 2006:
  - Recoverable oil reserves equal to or exceeding 70 million tons;
  - Gas reserves equal to or exceeding 50 billion cubic meters;
  - Hard-rock gold reserves equal to or exceeding 50 tons; or
  - Copper reserves equal to or exceeding 500 thousand tons;

- Subsoil plots located in the inland sea waters, territorial sea waters, or on the continental shelf of the Russian Federation (the so-called offshore deposits);
• Subsoil plots that can only be developed using land used for defense and security.

The list of subsoil plots of federal significance is published by the Federal Agency for Subsoil Use and includes approximately 1,000 strategic deposits and is updated on a regular basis. It is noteworthy that the list is not exhaustive and any deposit that meets the above criteria will be deemed strategic irrespective of whether it is included into the list or not.

19.7 Production Sharing Agreements

In the Russian Federation production sharing agreements (PSAs) are used to provide a particular legal framework for foreign investors in the mining, oil, gas, and other extraction sectors. The main objective of the PSA legislation is to provide investors in these sectors with greater stability in fiscal and regulatory areas over the long term. The main legislation governing PSAs in Russia is the PSA Law.

Since 2003 subsoil plot development under the PSA Law has been available only if the subsoil plot was put out to auction and the auction failed. That is, only those plots that are not of interest to subsoil users on standard license terms and conditions may be developed under a PSA. Therefore the best deposits are distributed under subsoil licenses and the PSA regime is not very attractive to subsoil users.

Due to the above and to the PSA tax regime established at the same time (see Section 8.10), PSAs have, in practice, become largely ineffective in terms of attracting foreign investment into Russia.

19.8 Export of Gas and LNG

In late 2013 Gazprom’s monopoly on export of gas was abolished. Starting from 1 December 2013 access to the LNG export market was granted to the following categories of exporters in addition to Gazprom and its wholly-owned subsidiaries:
• subsoil users holding subsoil licenses for strategic deposits (see Section 19.6 above) if their subsoil license as of 1 January 2013 envisages either (a) development of an LNG plant or (b) recovery of natural gas for further liquefaction at an LNG plant;

• Russian companies meeting all of the following criteria:
  o more than 50% owned by the Russian Federation;
  o holders of subsoil licenses in respect of Russian offshore deposits; and
  o producers of LNG out of natural gas extracted from the deposits mentioned above or under product sharing agreements;

• 50%+ subsidiaries of the companies meeting the criteria set out in item 2 above, if such subsidiaries produce LNG out of natural gas recovered under product sharing agreements.

19.9 Precious Metals and Gem Stones

Under the Precious Metals Law precious metals include gold, silver, platinum, palladium, iridium, rhodium, ruthenium and osmium; and gem stones include natural diamonds, emeralds, ruby crystals, sapphires, alexandrites, and natural pearl and unique amber formations. Artificially created materials, even if they have the same properties as gem stones, are not subject to the Precious Metals Law. Both lists, of precious metals and gem stones, are exhaustive.

Precious metals, with the exception of native metals, may be refined by organizations included on a special list of companies authorized to do so, which is maintained by the Russian Government. Following the refining process, precious metals may be sold on the domestic market. Export requires a separate export license, which in practice is usually granted to banks and major producers.
It is important to note that the Russian authorities enjoy a right of first refusal to purchase precious metals and gem stones from mining companies. The prices for precious metals in such instances are based on world market prices. The pricing of precious stones is carried out by expert commissions on the basis of world market prices.