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Establishing a Legal Presence in Russia

Establishing a Legal Presence

In Russia, foreign investors may:

- Establish a representative office or a branch of a foreign legal entity
- Establish a Russian legal entity in the form of an enterprise with foreign investment, which is either entirely foreign-owned, or co-owned as a joint venture with a Russian partner(s)
- Act directly as a foreign investor

Representative Office or Branch

Legal Status

A representative office or a branch of a foreign legal entity is not considered to be a Russian legal entity, but rather a body representing the interests of a foreign legal entity in Russia.

A representative office is entitled to carry out liaison and ancillary functions in order to promote the business of its foreign founder. Representative offices are not permitted to engage in commercial activities in Russia. Consequently, most representative offices are not subject to profits tax, unless their activities give rise to a "permanent establishment" for tax purposes, i.e. when a foreign legal entity engages in regular commercial activity through its representative office (for example, through the sale of goods or the provision of services).

A branch is a subdivision of a foreign legal entity, which may fulfill all or part of the functions of its foreign founder. These functions include the repatriation of management fees earned in foreign currency, contracting with Russian entities for payment in foreign currency and rubles, and the appointment of a sales force.

The obligations imposed on a branch may include the same obligations as imposed on a representative office. However, a branch has less flexibility in selecting an accrediting authority in Russia than a representative office. This can sometimes affect certain issues such as the effectiveness of visa support.

Registration

An appropriate accrediting body must approve representative offices. There are numerous accrediting bodies authorized to grant such accreditation, including those responsible for the accreditation of representative offices in a particular industry - representative offices of foreign banks, for example, are accredited by the Central Bank of the Russian Federation. The bodies most frequently charged with the accreditation of foreign entities are the Chamber of Commerce and Industry of the Russian Federation (the CCI) and the State Registration Chamber at the Ministry of Justice of the Russian Federation (the SRC).

Accreditation is usually granted for a period of up to three years, with the right of extension. An application letter for the accreditation of a representative office should be submitted to the appropriate accrediting body and must be accompanied by the following documents:

- The Charter (Articles of Association, By-laws) of the foreign legal entity
- The registration certificate (Certificate of Incorporation, an excerpt from the trade register, certificate of good standing of the foreign legal entity)
- The resolution of the foreign legal entity to establish the representative office in the Russian Federation and to appoint the chief representative(s)
- The regulation of the representative office
- A bank letter confirming the good credit standing of the foreign legal entity
- A document confirming coordination with the regional authorities of the Russian Federation on establishment of a representative office (not required for representative offices to be located in Moscow)
- General Power of Attorney issued to the chief representative(s)
- Power of Attorney for filing the application for accreditation in behalf of the foreign legal entity
- The Accreditation Card containing information on the representative office, completed in accordance with a sample form of a particular accrediting body and signed by a representative of the foreign legal entity
- The Certificate from the tax authorities in the country of the foreign legal entity's incorporation confirming that the foreign legal entity is registered as a taxpayer and specifying the taxpayer identification code
- Two letters of recommendation from Russian trading partners (preferably government bodies, social organizations, or 100% Russian-owned entities) on the official letterhead of the recommending organization
- A copy of a lease agreement or landlord's guarantee, together with a document confirming the landlord's right to the property to be leased by the representative office
- Certificate of payment of the applicable accreditation fee

Branch offices must be accredited by the SRC in accordance with the 1999 Law on Foreign Investments. An application letter for the accreditation of a branch should be submitted to the SRC and should be accompanied by the following documents:

- The Charter (Articles of Association, By-laws) of the foreign legal entity
- The registration certificate (Certificate of Incorporation, an excerpt from the trade register, certificate of good standing of the foreign legal entity)
- The resolution of the foreign legal entity to establish the branch office in the Russian Federation
- The regulation of the branch office
- A bank letter confirming the good credit standing of the foreign legal entity
- A document confirming coordination with the regional authorities of the Russian Federation on establishment of a branch office (not required for branches to be located in Moscow)
- General Power of Attorney issued to the General Manager of the branch office
- Power of Attorney for filing the application for accreditation on behalf of the foreign legal entity
- The Accreditation Card containing information on the branch office filled in accordance with a sample form of a particular accrediting body and signed by a representative of the foreign legal entity
- The Certificate from the tax authorities in the country of the foreign legal entity's incorporation confirming that the foreign legal entity is registered as a taxpayer and specifying the taxpayer identification code
- Expert opinions from the respective ministries of the Russian Federation (the Ministry of Energy, the Ministry of Natural Resources etc.) if provided for under the statute
- Certificate of payment of applicable accreditation and registration fees

All documents from a foreign legal entity must be notarized and apostilled/legalized in the country of execution. Any document supplied in a language other than Russian must be accompanied by a notarized translation.

Following accreditation, the representative office or branch office must carry out a number of post-accreditation procedures before it becomes fully operative, including registration with the State Statistics Committee of the Russian Federation, with the tax authorities of the Russian Federation, and with the Russian social benefits funds.

Legal Entities

Applicable Laws

The Civil Code of the Russian Federation recognizes the following most important types of commercial legal entities:

- General partnerships
- Limited partnerships
- Limited liability companies
- Additional liability companies
- Joint stock companies

The establishment of limited liability companies ("LLC") and joint stock companies ("JSC"), are governed by notably the Federal Law on Limited Liability Companies, dated Feb. 8, 1998 (the LLC Law), and the Federal Law on Joint Stock Companies, dated 26 December 1995 (the JSC Law). Since LLCs and JSCs are the corporate structures most often used by foreign investors, these are examined in detail below.

Limited Liability Companies

Number of Participants

A LLC may be established by one or more persons or legal entities (the "participants"). However, if the number of participants exceeds 50, the entity must be reorganized into an open joint stock company or a production cooperative within one year. Furthermore, a LLC may not have as its sole participant another business entity consisting of a single person. The Charter capital of a LLC is divided into participation interests held by its participants, as set forth in the Charter.

Rights of Participants

The participants in a LLC have the right to:

- Participate in the management of the LLC in accordance with procedures established by the LLC Law and the LLC foundation documents
- Obtain information concerning the activities of the LLC and have access to its accounting and other documents in accordance with procedures established by the LLC foundation documents
- Participate in the distribution of profits
- Sell or otherwise assign their participation interests in the LLC charter capital, or a part thereof, to one or more of the participants in the LLC in accordance with the procedure established by the LLC Law and LLC charter
- Withdraw from the LLC without first seeking the approval of the other participants
- Receive a portion of any assets remaining after settlement with creditors in the event of the liquidation of the LLC.

The participants in a LLC also have other rights under the LLC Law, and may have additional rights set forth during the establishment of the LLC under the LLC charter, or which are granted at a later date by a decision of the LLC's General Participants' Meeting. The following points should be noted with regard to the granting of additional rights to LLC participants:

- Where additional rights are granted by a decision of the LLC's General Participants' Meeting, such decision must be unanimous
- Additional rights granted to a particular participant in the LLC do not transfer to any party acquiring all (or a part) of such participant's ownership interest in the event of assignment thereof Obligations of Participants

The participants in a LLC are required to:

- Make contributions to the Charter capital as specified in the LLC Law and LLC foundation documents (or in the resolution on the establishment of the LLC, where there is only one participant in the LLC), and within the time periods specified in the LLC Law
- Keep confidential all information concerning the activities of the LLC

Participants in a LLC also have other obligations as provided for by the LLC Law, and may have additional obligations set forth during the establishment of the LLC under the LLC charter, or which are imposed on them at a later time by a decision of the LLC's General Participants' Meeting.

The following issues should be considered when imposing additional obligations on participants in a LLC:

- Where additional obligations are imposed by a decision of the LLC's General Participants' Meeting on all LLC participants, the above decision must be made unanimously
- If additional obligations are imposed by a decision of the LLC General Participants' Meeting on a particular LLC participant, such decision must be made by at least a two-thirds majority vote of the total number of votes held by the LLC participants, provided that the LLC participant on whom such additional obligations are imposed voted in favor of such decision or consented thereto in writing
- Additional obligations imposed on a particular participant(s) in the LLC do not pass to any party acquiring all (or part) of such participant's ownership interest in case of assignment thereof Charter Capital

The Charter capital of a LLC consists of contributions made by its participants. The initial charter capital may not be less than an amount equal to 100 times the statutory monthly minimum wage (the statutory monthly minimum wage used for the purposes of calculating the minimum charter capital of a LLC currently being RUR 100). As at the date of publication, with an exchange rate of approximately RUR 28 to the dollar, the minimum charter capital for a LLC is approximately US\$ 360.

At least 50% of the Charter capital amount must be paid by the date of the LLC's registration, and the balance must be paid in full within the first year of its operation. Contributions may be made in cash or in-kind, and certain customs benefits may be available for in-kind contributions made by foreign investors. The Charter capital may be increased only after the original charter capital has been paid in full.

Participation Interests

A participation interest (i.e. an ownership share) in a LLC is not considered a security under current Russian legislation. Therefore, in contrast to the shares of a joint stock company, LLC participation interests do not need to be registered.

Participation interests in a LLC may be sold to third parties, but they are subject to the right of first refusal of other participants to purchase the participation interests at the price offered to the third parties. The participants in a LLC also have a unilateral right to withdraw from the LLC and to be compensated for their participation interests.

Finally, a participant (participants) with more than a 10% ownership interest in a LLC may demand the expulsion of any participant who grossly violates his obligations as a participant, or whose actions (or lack thereof) substantially hinder the LLC or make its activity impossible.

Management Structure

The General Participants' Meeting is the highest governing body of a LLC, and almost all matters fall within its exclusive competence. Even where the LLC participants choose to create a Board of Directors, the General Participants' Meeting may nonetheless only delegate a limited number of matters to the Board.

The General Participants' Meeting has exclusive rights to:

- Amend the Charter
- Amend the foundation agreement
- Define the basic goals of the LLC
- Delegate to a commercial organization or to an individual entrepreneur the authority reserved to the LLC executive body and approve the conditions of the agreements with such organizations or persons
- Assign supplemental rights and duties to the participants in the LLC
- Approve the annual financial report and the distribution of profits
- Alter the amount of the Charter capital of the LLC Approve the regulations governing the internal activities of the LLC
- Reorganize or liquidate the LLC, appoint a liquidation commission, and approve the liquidation balance sheet of the LLC

The daily management of a LLC is the responsibility of the Executive Body, which may be comprised of one person (the General Director) or may consist of both the General Director and the Management Council. The Executive Body is responsible for all matters which do not fall within the authority of either the Board of Directors or the General Participants' Meeting.

Registration

With effect from July 1, 2002, the new Federal Law on State Registration of Legal Entities (the Registration Law) entered into force, transferring authority for registration of legal entities in Russia to the local bodies of the Federal Tax Service of the Russian Federation. As a result, activities connected with the state registration of legal entities and with their registration as taxpayers are now under the auspices of the local tax inspectorates.

The following documents are required for registration purposes:

- The application for the state registration of the new entity
- The foundation agreement of the LLC (if the LLC has more than one founder/participant)
- The protocol of the founders' meeting or, if the LLC has only one founder, the resolution of the founder on the establishment of the LLC
- The Charter of the LLC
- A copy of the passport of the proposed General Director of the LLC
- Power of Attorney issued by the founder for establishment of the LLC
- Power of Attorney issued by the founder for filing the application for the state registration of the LLC
- The registration certificate, Certificate of Incorporation, an excerpt from the trade register, or certificate of good standing of the foreign legal entity
- The Charter (Articles of Association, By-laws) of the foreign legal entity
- Confirmation of payment of the state registration fee
- A tax registration certificate (required for opening of a bank account)
- A bank letter confirming the good credit status of the foreign legal entity
- Confirmation of the foreign legal entity's contribution to the Charter capital of the LLC

Any Russian founder participating in a LLC must also provide additional documentation. All documents from a foreign legal entity must be notarized and apostilled/legalized in the country of their preparation. Any document supplied in a language other than Russian must be accompanied by a notarized Russian translation.

Joint Stock Companies

Types of Joint Stock Companies

A significant number of commercial organizations have been established as joint stock companies since the JSC Law came into force on Jan. 1, 1996. While the adoption of the LLC Law in 1998 introduced another option for investors seeking to establish a corporate entity, the JSC Law represented one of the most significant pieces of civil legislation of the post-Soviet era, and JSCs remain among the most important commercial corporate forms and structures for doing business in Russia.

A JSC is a legal entity, which issues shares in order to raise capital for its activities. A shareholder of a JSC is not generally liable for the obligations of the JSC, and bears the risk of any such loss only to the extent of the amount paid by it for the shares.

Two types of joint stock companies exist in Russia:

- Closed joint stock companies
- Open joint stock companies

An open JSC may have an unlimited number of shareholders. Shareholders in an open JSC are entitled to freely dispose of their shares. The number of shareholders in a closed JSC may not exceed 50, and the JSC must be transformed into an open JSC within one year should the number of shareholders ever exceed this amount. As with participants in a LLC, shareholders in a closed JSC have a right of first refusal to acquire shares sold by other shareholders to third parties, at the price offered to the third parties. Shareholders in either an open or closed JSC have a preemptive right to acquire newly issued shares that are to be privately placed, in proportion to their existing shareholdings.

Shareholders in an open JSC also have a preemptive right to acquire newly issued shares that are to be publicly placed, in proportion to their existing shareholdings, but do not have a right of first refusal to acquire shares sold to third parties.

All JSCs are required to maintain a shareholders' register. The register includes information on each registered shareholder including the number, category, and classes of shares held. A JSC with more than 50 shareholders must delegate the maintenance and keeping of the shareholders' register to a licensed registrar.

Formation of a Joint Stock Company

Founders of a JSC may include individuals and/or legal entities. A company's foundation document, i.e. its charter, must include the following information:

- The name, address, and status of the JSC (i.e. open or closed)
- The size of the JSC's charter capital
- The quantity, nominal value, and categories (common or preference) of shares, as well as the classes of preference shares issued and distributed by the JSC
- The rights of the holders of shares of each category
- The structure and competence of the governing bodies of the JSC, and their decision making procedures
- The procedure for preparing for and holding of the General Shareholders Meetings, including a list of issues requiring either unanimous consent or a resolution adopted by a qualified majority of votes
- Information on branches and representative offices
- Information on the existence of any special right of participation in the management of the company (a "golden share") vested in the Russian Federation, a subject of the Russian Federation, or a municipality of the Russian Federation
- Other provisions required by law

The Charter may include other provisions, so long as these comply with applicable Russian legislation.

Charter Capital

The Charter capital of an open JSC may not be less than an amount equal to 1,000 times the statutory monthly minimum wage (the statutory monthly minimum wage used for the purposes of calculating the minimum charter capital of the JSC currently being RUR 100). As at the date of publication, with an exchange rate of approximately RUR 28 per dollar, the minimum charter capital for an open JSC is approximately US\$ 3,600. A closed joint stock company must have a minimum charter capital equivalent to at least 100 times the minimum monthly wage - currently approximately US\$ 360.

In contrast to LLC founders, the founders of a JSC must pay 50% of the JSC charter capital within three months of its state registration, with the balance payable in full within the first year.

Shares and Other Types of Securities

A JSC can issue securities in the form of shares, bonds, and issuer's options. In either case, such securities must be registered with the Federal Service for the Financial Markets of the Russian Federation (the FSFM), which replaced the former Federal Commission for the Securities Market (the FCSM) in March 2004. A JSC can issue common shares and/or several classes of preference shares. The total value of a JSC's preference shares may not exceed 25% of its charter capital.

The concept of a "fractional share" was introduced on Jan. 1, 2002. A fractional share is a share representing a portion of a whole share, which can come into existence where it is not possible to acquire the whole share during the consolidation of shares, where a shareholder exercises its preemptive right, or in the course of acquiring additional shares. A fractional share grants its owner the same rights as those granted by the whole share of the corresponding category or class, albeit on a pro rata basis.

Management Structure

Both open or closed JSCs must maintain two governing bodies: the General Shareholders Meeting and the Executive Body. An open JSC with more than 50 shareholders must also have a Board of Directors (sometimes called a Supervisory Board). An open JSC with less than 50 shareholders and all closed JSCs may have a Board of Directors, although this is not a requirement. The authority of the Board of Directors is defined by the Charter of the JSC and, where a Board is not provided for in the Charter, the corresponding authority must be vested with the JSC's General Shareholders Meeting by the Charter.

In addition to the foregoing governing bodies, a JSC must either establish an Internal Auditing Commission or elect an Internal Auditor to oversee its financial and economic activities, which must be elected by the shareholders.

The General Shareholders Meeting is the highest governing body overseeing the activities of a JSC. Its authority is outlined in the JSC Law and cannot be altered. Each common share carries one vote at the General Shareholders Meeting (except for cases of cumulative voting in cases provided for in the JSC Law), and most decisions are made by a simple majority vote, although for certain key decisions a supermajority of 75% is required.

The daily management of a JSC is the responsibility of the Executive Body, which may be comprised of one person (the General Director) or may consist of both the General Director and the Management Council.

The Executive Body is responsible for all matters which do not fall within the authority of either the Board of Directors or the General Shareholders Meeting. The General Shareholders Meeting may (by a majority vote), choose to delegate on the contractual basis the powers of the Executive Body to an external commercial organization or to an individual manager; however this decision may be taken only pursuant to a proposal of the Board of Directors.

Registration

With effect from 1 July 2002, the procedure for state registration described in Section 1.2.2 above in respect of LLCs is also applicable to JSCs: the only additional requirement in respect of JSCs being the registration of the issuance of the JSC shares with the FSFM.

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