

Practical advice on developing your business on the territory of the Russian Federation

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Nowadays Russia is one of the most promising markets in the world. More and more foreign companies invest into Russia and successfully conduct their business here. Official representative offices of Mitsubishi, Toyota, Ford, Honda and many other well-known companies have been opened in St. Petersburg. Other companies continue expansion on Russia's territory. For instance, the Italian holding «Prysmian Cables & Systems» acquired the plant «Rybinskelektrokabel». The well-known German company «HOCHTIEF Russia» is building objects all over Russia including the dam in St. Petersburg and the airport in Vladivostok. The rules of the Russian market have become closer to foreign investors since Russia joined World Trade Organization.

For successful investment in Russia it is necessary to consider local specificity. It does not mean that one should regard Russia as a «wild» and «uncivilised» market. To our country (like any other) the following proverb is applicable: when in Rome, do as the Romans do. The set of rules of «Romans» in Russia is not worse than that of original Romans.

The Russian legislation establishes not too burdensome order of creating business. Time and money expenditures for organising business in Russia are not so high. For example, the authorised capital for creating a new company in Russia is only 10,000 roubles (about EUR 250) while, for example, in Turkmenistan the authorized capital must not be less than USD 10,000 and registration here will take about half a year; in Estonia the minimal authorised capital is EUR 2,700; in China, except for free economic zones, the authorised capital of a new company with participation of foreigners will be hundreds of thousands of dollars. In Russia the process of setting up a business organisation will not take much time either: a tax authority will need 5 working days to register a new company, within 18 working days an authorised body will issue permission for opening a representative office of a foreign company in Russia.

With proper control it is possible to conduct successful business anywhere including Russia. In this article we will outline the main moments that a foreign investor should pay attention to when organising his business in Russia.

In order to start business it is necessary to create a structure able to represent interests of a foreign investor in Russia. There exist several variants of its creation.

How to create a legal basis for business in Russia?

To begin with, let us consider legal regulating of this question in Russia. Types of Russian legal entities and their subdivisions are listed in the Civil Code of the Russian Federation. In Russia there are special laws dedicated to forms of a legal entity, for example, Federal law No.14-Φ3 of 08.02.1998 «On limited liability companies». It also would be useful for a foreign company to get acquainted with Federal law No.160-Φ3 of 09.07.1999 «On foreign investments in the Russian Federation» establishing guaranties for foreign investors. The information of forthcoming taxes and dues, the order of their calculation, tax privileges and deductions, and other questions of taxation can be found in the Tax Code of the Russian Federation. Federal law No. 129-Φ3 of 08.08.2001 «On state registration of legal entities and individual entrepreneurs» is also important for the procedure of registration. This is, probably, the minimum legal basis necessary to get an idea of available opportunities how to organise business in Russia. There exist several possible variants.

Firstly, a foreign company may create its *representative office* in Russia. The distinctive feature of a representative office of a foreign company is the prohibition for engaging in any commercial

activities¹. The main function of representative office is to represent interests of a foreign company in Russia. The representative office is convenient because its foreign employees are not required to obtain permission for work in Russia. In order to create official representative office it is necessary to obtain accreditation from an authorised body. It is possible to apply to the state body having issued accreditation of representative office for accreditation of its foreign employees. Accreditation or state permission for carrying out activity by a representative office is issued for a definite term.

A *branch office of a foreign organisation* has wider opportunities. A branch office of a foreign organisation in Russia carries out the same activity as the head organisation abroad. A branch office is convenient for realising projects in the sphere of construction due to considerable tax privileges. For opening branch office as well as for creating a representative office it is necessary to obtain accreditation.

Thirdly, an investor may create a new *legal entity* in Russia. Such an organisation obtains the status of a daughter or dependent company. When a foreign organisation decides to create in Russia a new legal entity, it is better to involve lawyers for professional assistance. But before getting professional assistance it is necessary to solve a number of organisational questions.

What should a foreign founder decide before registration of a new company?

Before proceeding to open a legal entity in Russia a foreign investor should solve a number of important questions.

Firstly, it is necessary to decide on the name and legal form of the future company. The most popular forms of commercial organisations in Russia are a limited liability company (hereinafter LLC) and an open joint-stock company (hereinafter OJSC). A LLC is the most convenient from the point of view of day-to-day management.

Secondly, it is necessary to solve the question of personal presence of the founder while creating a new company. It is possible to open a company in Russia without physical presence here. An authorised person may solve all questions of business organisation on behalf of the founder. For this purpose a properly completed power of attorney is necessary to make. Power of attorney may be made both in Russia as well as in any other country participating in the Hague Convention of 1961. In the latter case the power of attorney should be attested with an Apostille.²

Thirdly, it is necessary to solve the question of personnel. In the first place it concerns the management personnel of the new company and the office of the accountant. The director general may be a foreigner. However, at the moment of creating a new legal entity it is expedient to appoint as a director general a lawyer or another authorised person – a citizen of the Russian Federation - and later replace him with a general director - a foreign citizen. The authorised person will perform all necessary formalities on opening the company and obtaining permission to work for a foreign director general.

If a citizen of Russia is appointed as a director general, it will be expedient to form the board of directors. This allows to divide competence and responsibility between director general and collective body. Thus, the freedom of action of the director general will be limited.

As to accounting, it may be carried out not only by a member of the staff but also by a separate company specialising in this field.

Fourthly, it is necessary to define the order of financing of the organisation on the initial stage: the amount of the authorised capital and the order of its payment; to choose a bank for opening the settlement account of the organisation.

Fifthly, an address for the registering company and a postal address should be found; an agreement of lease of the office should be concluded. One should not forget that state bodies will sent

¹ Certainly, some business activity is possible and follows the law but it should not to be a main activity of a representative office.

² It is worth noting that Russia's state bodies accept foreign documents only with authentic marks of consular legalisation together with certified (notarially or in a consular institution abroad) translations into Russian. At the same time, consular legalisation of documents is not needed if the foreign state is a participant of the Hague Convention of 1961. In countries participating in the Hague Convention of 1961 only Apostilles are required on documents.

all correspondence at the registration address of the company. Non-receipt of official letters may cause unpleasant surprises.

Interaction with state bodies demands extreme caution. Such interaction is inevitable during the process of registration of a new company. In this situation it is very important to observe all formalities. Non-observance of the term for presenting a document, non-enclosing of a needed document with an application, an incorrect filling of an application – all these small mistakes cause retardation and additional trouble. Such problems can be easily avoided if you resort to assistance of professional lawyers. They will perform the procedure of registering a new company in a short time period.

What should not be forgotten after creating a new company?

After creating a legal entity in Russia it is necessary to build up a scheme of work with the head organisation, particularly, to decide how *financing of the new company* will be conducted, what agreements with the head organisation should be concluded for this purpose: loan, credit, transfer of non-property rights (for example, know-how) etc. When solving this question it is necessary to be guided by the Russian Federation's Civil Code and Tax Code. Provisions of these codes should be taken as the basis for developing a financing scheme convenient from the point of view of taxation and corporate management.

Questions of personnel will arise as well. In Russia they are regulated mainly by the Russian Federation's Labour Code. On the whole, the Russian labour legislation meets standards of the International labour organisation. The status of a foreign employee in Russia is regulated by Federal law No. 115-Φ3 of 25.07.2002 «On legal status of foreign citizens in the Russian Federation». It should be kept in mind that there is a difference between status of foreign employees in representative or branch offices and in subsidiary company. In a branch or representative offices foreign employees undergo the procedure of accreditation. In subsidiary company its foreign employees must obtain *permission to work in Russia*. The requirements of labour law should be observed. It is necessary to conclude labour contracts with all employees immediately. Labour contracts protect interests of not only employees but of employers as well. Otherwise the company will not be able to avoid liability for violations of the labour legislation.

The company has been created. The personnel have been employed. The first clients have been found and first agreements have been signed. On this stage it is important to organise coordinated work of the company. Practice of our company shows that there exist three main spheres of risk for business including:

1. Management of the company.

Divulgence of confidential information, development of his or her own business instead of business of the company where a manager has been employed, and the last but not the least, formal attitude to work, resulting in failure of the Russian project. The managing personnel of the company may become both a reliable support for the new business and a real threat for it. It depends of the two aspects: motivation of managers and control over them. This should be always kept in mind when employing a manager for your company in Russia.

2. Contractors in bad faith.

A well formulated agreement and correctly completed executive documents will be a guaranty for return of the money from a deal in case of problems with its fulfilling. Therefore, it is necessary to pay enough attention to legal support of the new company's activity. Lawyers should check all the documents and contracts. It would be good also to attract lawyers to the process of coordinating draft agreements for all big deals of your company.

3. Tax authorities.

Being guided by the provisions of articles 87-105 of the Russian Federation's Tax Code tax authorities in Russia may seriously complicate current activity of your company when checking tax accounts. Once in 3-4 years specialists of the tax service may check activity of your company. That is

why it is important to attentively complete all documents on deals and carefully maintain records on accounts. In Russia you have to be ready for that your company may get involved in a judicial dispute with a tax authority.

We recommend thinking not only of current activity but also of strategic development of your business in Russia: our country provides great opportunities for further expansion of business, for example, in St. Petersburg. A foreign company may expand its activity through opening new branch offices, representative offices, creating daughter companies. Already on the initial stage of opening business in Russia you should outline a plan for future development. It is expedient to do it on the initial stage for creation of a functioning scheme of management in all departments, branch offices, representative offices, daughter, dependent companies and other units of a foreign company.

Right decisions made in accordance with this article will help a foreign investor to create profitable and stably developing business in Russia. Under proper control over current activity of the company and correct planning of its development nothing threatens business in Russia. A lot of successful foreign companies having connected their activity with Russia and cooperating with our law firm prove it. Our country is open to investors. Running business here is not very complicated. Russian authorities constantly create new guaranties and privileges for foreigners by opening new spheres for business. In such a way, several special economic zones (SEZ), where investors are given special tax privileges and custom preferences, have been created in Russia. To the territories of SEZ the procedure of «a free custom zone» applies. It means that foreign goods are placed and used in SEZ without payment of custom duties and value added tax. Thus, on St. Petersburg's territory a special economic zone «Novo-Orlovskaya» has been created. A SEZ in the settlement of Strelna near St. Petersburg on the territory of «Neudorf» has been created as well.

Entrepreneur activity always contains elements of risk. The task of our company is to minimise possible risks of a future investor. Our practice shows that it is not too complicated to create business in Russia. Under proper control and professional approach to business it will be a successful and profitable project.