

DEAR READERS!

I am pleased to present to you a first edition of a research and practice commentary on the Federal Law On Making Foreign Investments in Business Companies of Strategic Importance for the Country's Defence Potential and Security of the State, which marks the tenth anniversary of that law.

This work has been prepared by foreign investment experts of the Federal Antimonopoly Service of Russia in conjunction with our colleagues from the Antimonopoly Experts' Association, leading practicing lawyers specializing in investment and antimonopoly legislation.

The commentary presents a vision of the subject matter by the State and business entities, lively discussions of the most complex rules, a combination of the understanding of issues encountered by business entities with the vast experience possessed by the Federal Antimonopoly Service and the latest experience of the Federal law's application. In our opinion, all this has produced a synergy and contributed to making this commentary a truly high-quality and effective "guide" of foreign investment legislation for the legal and business communities.

I am certain that this fundamental work will help improve knowledge and experience of supervising the making of foreign investments in the Russian Federation.

Respectfully yours,

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DEAR COLLEAGUES!

This year marks a landmark anniversary – 10 years since the passing of the Federal Law On Making Foreign Investments in Business Companies of Strategic Importance for the Country's Defence Potential and Security of the State (57-FZ of 29 April 2008).

It is important to note that the Law, passed ten years ago, did not represent a tightening of the foreign investment regime in Russia or created any new subject matter. The purpose was to incorporate and unite scattered rules restricting the procedures for foreign companies' ownership of Russian enterprises' capital, to codify them into a single Federal Law, to create a single decision-making procedure understood by all and to move from a prohibitive regime to a system of pre-monitoring and to set sanctions for violations of the law. Before 2008, such restrictions were scattered over sectoral legislation. Many of those restrictions, imposed back in Soviet times, were embodied in subordinate acts and/or regulations, and some of those regulations were classified (so a foreign investor all set to execute a transaction would suddenly be told that the transaction was prohibited, but no reasons were provided). That situation was fundamentally altered, of course, and the restrictions based on the Russian Constitution establishing a certain procedure for making foreign investments in enterprises of strategic importance became straightforward and transparent and were elevated to the level of Federal legislation.

Now, what is Federal Law No. 57-FZ? First, the Federal Law defines rules for foreign investors to execute transactions that enables them to establish control over or acquire assets of strategic enterprises. Second, it sets an absolute ban for foreign states and for companies controlled by foreign states and certain other entities to establish control over strategic enterprises. Third, the Federal Law contains a closed list of strategic activity areas. Fourth, it sets a procedure for examining foreign investors' requests for pre-approval of transactions that are subject to supervision under that Federal Law and establishes the powers of government authorities in supervising foreign investments.

Lastly, the Federal Law sets measures intended to prevent violations of that procedure and to eliminate consequences thereof.

In other words, Federal Law No. 57-FZ stipulates clear and straightforward rules that define its scope. First of all, it applies to transactions and other actions that may be performed by foreign investors in or outside Russian territory (so it has extraterritorial effect) to establish their control over strategic companies. The Federal Law also applies to relationships involving acquisition of assets of strategic companies in excess of 25 per cent of their fixed assets' balance sheet value.

Very importantly, apart from traditional corporate law rules, dealing with company control through stock ownership, the Federal Law also addresses certain other transactions and actions that require prior approval. This refers to acquisition by foreign states of opportunity to block decisions of a strategic company's board also refers to rights, including the right to appoint the sole executive, the right to elect a certain number of members of the executive management team, the right to determine decisions by a strategic company's executive management. In fact, the Federal Law addresses more sophisticated arrangements than stock ownership, involving, for instance, shareholder agreements and various multi-level transactions.

The past ten years have seen evolvement of a whole system of laws and regulations. In addition to Federal Law No. 57-FZ, this also includes the Federal Law On Foreign Investments in the Russian Federation (Federal Law No. 160-FZ dated 9 July 1999), the Federal Law On Fishing and Preservation of Aquatic Biological Resources (Federal Law No. 166-FZ dated 20 December 2004), the Federal Law On Subsoil Resources (Federal Law No. 2395-1 dated 21 February 1992), a number of Federal Government Decrees: a Decree On a Government Commission for Control over Foreign Investments in the Russian Federation (RF Government Decree No. 510 dated 6 July 2008), a Decree Approving the Rules of Pre-Approval of Transactions

and Approval of Establishment of Control by Foreign Investors or a Group of Entities Including a Foreign Investor over Business Companies that are of Strategic Importance for the Country's Defence Potential and Security of the State (RF Government Decree No. 838 dated 17 October 2009), a Decree Approving the Rules for Information to be Provided by Foreign Investors or a Group of Entities Including a Foreign Investor about Transactions Involving Shares of (Ownership Interest in) the Charter Capital of Business Companies that are of Strategic Importance for the Country's Defence Potential and Security of the State and about Transactions and Other Actions Subject to Pre-Approval (RF Government Decree No. 795 dated 27 October 2008), and administrative regulations of government authorities and interdepartmental orders (as amended and supplemented).

This year marks not only the tenth anniversary of Federal Law No. 57-FZ. Also ten years ago, the Russian Government ruled that the Federal Antimonopoly Service would be the Federal executive body authorized to perform the functions of supervising foreign investments in business companies of strategic importance. In the course of the drafting of the law, there were several proposals regarding the authorized body. So why was the Federal Antimonopoly Service finally selected? First, the FAS of Russia has extensive experience in reviewing requests for business concentration, because the transactions covered by Federal Law No. 57-FZ are very similar to transactions reviewed by FAS under the Federal Law On Protection of Competition (Federal Law No. 135-FZ dated 26 July 2006). So the Federal Antimonopoly Service already possessed the relevant competency at that time. Second, it is very important, in our opinion, that business concentration transactions examined under Federal Law No. 135-FZ, Federal Law No. 57-FZ, and Federal Law No. 160-FZ are handled by the same executive government body. This saves us the need to enter into a long process of exchanging information with other government authorities with decision-making powers; the entire process is handled by a single government body, and this enables us to use expert-assisted, horizontal processes to address questions

arising in the course of the examination of requests in a prompt and timely manner and to identify cases when requests submitted under Federal Law No. 135-FZ should be examined under Federal Law No. 57-FZ and vice versa, - and this significantly reduces potential administrative restrictions and barriers that foreign investors might face if the system managing the process were organized differently.

Importantly, decisions on transactions examined under Federal Law No. 57-FZ are made by a collective body – a special Government Commission for Control over Foreign Investments in the Russian Federation. The Commission is headed by the Russian Prime Minister and comprises Deputy Prime Ministers, heads of Ministries and other government agencies responsible for the country’s defenses and security and for its economic development and shaping of government policies and normative and legal regulation of strategic sectors of the economy. The Commission meets on a regular basis to examine transactions submitted for its review in a detailed and meaningful manner and to render reasonable and sound decisions based on substantial discussions.

To support the functioning of the Federal Antimonopoly Service as the body authorized to perform its missions, a special department has been set up ten years ago – a Foreign Investment Supervision Department; it renders opinions on very complex and sophisticated transactions and prepares them for the Government Commission’s review. In some cases, descriptions of a foreign investor’s control arrangements within its group take several linear meters of paper, almost more than one desk can hold, for a transaction structure may comprise dozens of parent company branches, offshore entities, sophisticated trust agreements, involving dozens of jurisdictions, complex schemes of control of Russian parties, etc. This is very fascinating, substantive, and informative work.

Besides, the Federal Antimonopoly Service is currently working to develop case-law involving application of Federal Law No. 57-FZ, with a focus on cases where foreign investors establish control

over strategic companies without prior approval of the Government Commission and without submission of an application to the Federal Antimonopoly Service of Russia. Violations of the law entail economic sanctions that make foreign investments in breach of the established procedure “toxic” to the foreign investor. For example, the Federal Antimonopoly Service is authorized to bring legal action against violating foreign investors to debar their right to vote at the strategic company’s general meetings of shareholders based on illegally acquired shares. Such measures are mainly used as warnings, not very frequently. Practical work involves a variety of scenarios: we have to challenge control acquisition arrangements, including hidden ones, and we even challenge foreign courts’ judgements in Russia; in many cases, violations by foreign investors get eliminated in the course of court proceedings, and disputes are settled amicably, without detriment to Russia’s investment environment. We are pleased to point out that the existing case-law is not very extensive, but is quite successful and diverse.

We release this book in the year of the tenth anniversary of Federal Law No. 57-FZ in the hope that the work accomplished will benefit foreign investors and everyone interested in laws that govern supervision of foreign investments in the Russian Federation. In preparing this commentary, we have tried to outline the Russian regulator’s approach to application of Federal Law No. 57-FZ with maximum clarity and to explore the most complex issues addressed by the Federal Antimonopoly Service in performing its functions.

Respectfully yours,

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