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# Investments in Real Estate in Russia

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# Contents

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<b>Preface</b>	1
<b>1. Main Provisions</b>	2
1.1 Legal Basis	2
1.2 Concept and Types of Real Estate	3
1.2.1 The Concept and Main Types of Real Estate	3
1.2.2 Land Plots	4
1.2.2.1 General Overview	4
1.2.2.2 Particularities of Land Plots as Objects of Investment Activities	4
1.2.2.2.1 Natural Objects	5
1.2.2.2.2 Restrictions on the Turnover-Ability of Land Plots	5
1.2.2.2.3 Usage in Accordance with Designation	5
1.2.2.2.4 The Process of Dividing the State Ownership of Land into Russian Federation Ownership, Ownership of Russian Federation constituent territories and Municipal Ownership	6
1.2.2.2.5 Interdependence Between Titles to Land Plots and Titles to Real Estate Objects Located Thereon	8
1.2.2.2.6 Restrictions on Rights of Foreign Individuals and Legal Entities to Certain Types of Land Plots	9
1.2.3 Buildings and Constructions	9
1.2.3.1 General Overview	9
1.2.3.2 Particularities of Buildings and Constructions as Objects of Investment Activities	9
1.2.3.2.1 City Planning Rules Concerning Construction, Reconstruction and Capital Repairs of Buildings and Constructions	9
1.2.3.2.2 Buildings and Constructions that are Historical and Cultural Landmarks	10
1.2.3.2.3 Interdependence Between Titles to Land Plots and Titles to Buildings and Constructions Located Thereon	11
1.2.4 Residential and Nonresidential Premises	11
1.2.4.1 General Overview	11
1.2.4.2 Particularities of Residential and Nonresidential Premises as Objects of Investment Activities	11
1.2.4.2.1 Designation	12
1.2.4.2.2 Rights of Individuals Residing Together with Owners of Residential Premises	12
1.2.4.2.3 State Authorities' Consent to Alienation of Residential Premises	13
1.2.4.2.4 Common Property of the Owners of Residential Premises in Buildings	13

1.3	Subjects of Rights to Real Estate .....	13
1.3.1	Russian Citizens and Legal Entities .....	14
1.3.2	Foreign Citizens, Persons without Citizenship and Foreign Legal Entities .....	15
1.3.3	The Russian Federation, Russian Federation constituent territories, and Municipalities .....	15
1.4	System of Registration of Real Estate Objects and Rights Thereto ...	16
1.4.1	Concept and Main Types of Registration .....	16
1.4.2	Cadastral and Technical Registrations (Inventory) .....	17
1.4.3	State Registration of Rights to Real Estate and Transactions Therewith .....	17
1.5	Procedure for Acquiring Rights to Real Estate .....	19
1.5.1	General conditions for acquiring rights to real estate .....	19
1.5.2	Procedure for acquiring the title to a land plot .....	20
1.5.2.1	Procedure for acquiring the title to a privately owned land plot .....	20
1.5.2.2	Procedure for Acquiring the Title to a State or Municipally Owned Land Plot for the Purpose of Construction .....	22
1.5.2.3	Procedure for Acquiring the Title to a State or Municipally Owned Land Plot for Non-Construction Purposes .....	25
1.5.3	Procedure for Acquiring the Lease Right to a Land Plot .....	27
1.5.3.1	Procedure for Acquiring the Lease Right to a Privately Owned Land Plot .....	27
1.5.3.2	Procedure for Acquiring the Lease Right to a State or Municipally Owned Land Plot for Construction Purposes .....	28
1.5.3.3	Features of Granting Land Plots for Residential Construction and Comprehensive Development for Residential Construction Purposes ...	31
1.5.4	Procedure for Acquiring the Title to Buildings and Structures .....	32
1.5.4.1	Procedure for acquiring the title to privately owned buildings .....	32
1.5.4.2	Procedure for Acquiring the Title to State or Municipally Owned Buildings .....	33
1.5.4.3	Procedure for Acquiring the Title to a Building as a Result of Construction .....	35
1.5.5	Procedure for Acquiring the Lease Rights to a Building .....	36
1.5.5.1	Procedure for Acquiring the Lease Rights to a Privately Owned Building .....	36
1.5.5.2	Procedure for Acquiring the Lease Rights to a State or Municipally Owned Building .....	37
1.5.6	Acquiring Rights to a Land Plot when Acquiring Rights to a Building Located Thereon .....	39
1.5.6.1	Acquiring Rights to a Land Plot Owned by the Owner of a Building Located Thereon .....	39
1.5.6.2	Acquiring Rights to a Land Plot Owned by a Third Party .....	39
1.6	Legal Regulation of Construction Activities .....	40
1.6.1	City Planning Design, Zoning and Territory Planning .....	40

1.6.2	Development of Built-up Areas .....	42
1.6.3	Licensing Construction Activities and Transitioning to Self-regulation .....	42
1.6.4	Development of Design Documentation .....	44
1.6.5	Construction Permit .....	46
1.6.6	Control and Supervision at the Construction Stage .....	47
1.6.7	Permit to Commission a Constructed Structure .....	48
1.7	Land Payments .....	48
1.7.1	Value of a land plot during acquisition .....	48
1.7.2	Payment for Land Plot Use .....	49
1.7.2.1	Land Tax .....	50
1.7.2.2	Rent .....	51
<b>2.</b>	<b>Particularities of Regional Legislation .....</b>	<b>52</b>
2.1	Particularities of investing in real estate in Moscow .....	52
2.1.1	Legal basis .....	52
2.1.2	Objects and legal forms of investment activities .....	53
2.1.3	General conditions for acquiring rights to land plots for investment purposes in the city of Moscow .....	53
2.1.3.1	Priority of lease relations .....	53
2.1.3.2	City planning structures of the city and district levels .....	54
2.1.3.3	Investor financed construction of engineering infrastructure .....	54
2.1.4	Lease of land plots .....	54
2.1.4.1	General provisions .....	54
2.1.4.2	Lease agreement for a land plot for constructing nonresidential property .....	57
2.1.5	Agreement on developing a built-up area .....	60
2.1.6	Concession agreement .....	65
2.1.7	Acquisition of the ownership of land plots by owners of buildings and structures located on the land plots .....	69
2.2	Particularities of Investments in Real Estate in St. Petersburg .....	72
2.2.1	Legal Basis .....	72
2.2.2	Objects and Forms of Investment Activities .....	73
2.2.3	General Procedure for Granting Investors Rights to Real Estate Objects in St. Petersburg .....	73
2.2.3.1	Main Provisions .....	73
2.2.3.2	Investment Agreements .....	75
2.2.3.2.1	Types of Agreements Concluded with Investors .....	75
2.2.3.2.2	Content of an Agreement .....	75
2.2.4	Simplified Procedure for Lease of Land Plots in St. Petersburg .....	80
2.2.4.1	General Information .....	80
2.2.4.2	Procedure for Holding Auctions for Rights to Lease Land Plots .....	81
2.2.4.3	Main Provisions of a Land Plot Lease Agreement .....	81
2.2.5	Formation of Industrial and Special Economic Zones .....	82

<b>3.</b>	<b>Structure of an Investment Project and Stages of Its Implementation</b>	84
3.1	General Information. Choosing an Investment Object	84
3.2	Verifying Rights to Real Estate (Investment Objects) to be Acquired	86
3.4	Investment Project Organizational Work (Structuring)	88
3.5	Developing an Investment Project Financing Scheme	89
3.5.1	Equity Financing	90
3.5.2	Credit Financing	90
3.5.3	Combined Approach to Financing	91
3.6	Preparing Drafts of Necessary Documents and Signing them	91
3.6.1	The Project Company's Foundation Documents	92
3.6.2	Investment Agreement	92
3.6.3	Agreement on Participation in Share Participation Construction	94
3.6.4	Loan Agreement	95
3.6.4.1	Loan Agreement Conditions	95
3.6.4.2	Securing the Project Company's Obligations under Loan Agreements	96
3.6.5	Agreement on Subscription to Shares in the Project Company	97
3.6.6	Agreement on Developing Design Documentation	97
3.6.7	Construction Contract	99
3.6.8	Insurance Agreement	101
3.6.9	Agreement with a Management Company	101
3.6.10	Lease Agreement and Preliminary Agreements	103
<b>Contacts</b>		106

# Preface

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The brochure "Investments in Real Estate in Russia" has been prepared by specialists of the international law firm BEITEN BURKHARDT for those who see business prospects in the rapidly developing Russian real estate market as well as due to the continual growth of investors' interest in this sector of the economy.

BEITEN BURKHARDT has more than fifteen years of legal consulting experience in the real sector of the Russian economy, including real estate. While preparing this brochure we strove to present interested readers with a comprehensive review of current legislation regulating real estate transactions in the Russian Federation, as well as give several assessments concerning practical issues associated with implementing real estate investment projects.

This brochure covers key issues concerning transactions with real estate that is most often the object of investment activities, namely land plots, buildings and structures.

Given that Moscow and St. Petersburg are traditionally the absolute leaders among the constituent territories of the Russian Federation as concerns the number and scope of real estate investment projects, we devote particular attention to the legislative features of these cities.

We hope that those interested in our knowledge and extensive practical experience in the promising area of investing in real estate in Russia will contact one of the Russian offices of BEITEN BURKHARDT for a consultation.

We would be happy to share information with you and give useful, practical advice based on the specific nature of your particular investment project.

BEITEN BURKHARDT– Moscow – St. Petersburg  
2009

# 1. Main Provisions

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## 1.1 Legal Basis

Relationships between foreign investors and Russian legal entities, citizens, state authorities and institutions, with respect to issues related to real estate transactions, the registration of real estate, and the state registration of rights to real estate, are governed by the Russian Federation Constitution, as well as codes, federal laws and other regulatory legal acts, in particular, such as:

- The Russian Federation Civil Code
- The Russian Federation Land Code
- The Russian Federation City Planning Code
- The Russian Federation Tax Code
- The Federal Law "On the State Registration of Rights to Real Estate and Transactions Therewith"
- The Federal Law "On the State Cadastre of Real Estate"
- The Federal Law "On Mortgage (Pledge of Real Estate)"
- The Federal Law "On Participation in Shared Construction of Apartment Buildings and Other Real Estate and on Amending Certain Legislative Acts of the Russian Federation"
- The Federal Law "On Transfer of Land or Land Plots from One Category to Another"
- The Russian Federation Government Regulation "On Approval of the Rules for Maintaining the Single State Register of Rights to Real Estate and Transactions Therewith"
- The Decree of the President of the Russian Federation "On Privatization in the Russian Federation of Immovable Historical and Cultural Landmarks of Local Significance"
- And others



The Russian Federation Constitution, codes, federal laws and other regulatory legal acts adopted by Russian Federation authorities are effective throughout the Russian Federation and establish the main principles and provisions for regulating legal relationships in the field of investment activities.

At the same time, state authorities of individual constituent territories of the Russian Federation may adopt laws and other legal acts related to issues connected with investment activities in the real estate field, for instance:

- St. Petersburg Law No. 282-43 dated June 17, 2004 "On the Procedure for Granting Real Estate Objects Owned by St. Petersburg for Construction and Reconstruction"
- St. Petersburg Law No. 742-136 dated December 3, 2008 "On Strategic Investment Projects, Strategic Investors and Strategic Partners of St. Petersburg"
- And others

Laws and other legal acts issued by Russian Federation constituent territories may contain special provisions and rules applicable only on the territories of the respective Russian Federation constituent territories. At the same time, legislation of the Russian Federation constituent territories may not contradict the codes and laws of the Russian Federation.

At the local level, on the basis of and in order to implement codes, laws and other legal acts of the Russian Federation and Russian Federation constituent territories, local authorities may, within the limits of their competence, adopt legal acts establishing procedures and rules which are also to be taken into account and observed while conducting transactions with real estate objects.

## **1.2 Concept and Types of Real Estate**

### **1.2.1 The Concept and Main Types of Real Estate**

Pursuant to Russian Federation legislation, real estate includes land plots, subsoil plots and everything that is securely attached to land, i.e. any objects which may not be relocated without incommensurate damage to their purpose, including buildings, constructions and unfinished construction objects.

According to Russian law, the main characteristic of real estate objects is inseparable attachment to land. However, regardless of existing attachment to land, by virtue of direct stipulation of the law, real estate, also defined as immovable property in the Russian Federation Civil Code, also includes other property subject to state registration, namely: aircraft and sea-going vessels, vessels of internal navigation, and space objects, as well as residential premises (rooms, apartments) and nonresidential premises.

A prominent feature of all types of real estate is the requirement for state registration of rights to real estate and transactions therewith in cases and in accordance with the procedure stipulated by Russian Federation legislation (see section 1.4.3 "State Registration of Rights to Real Estate and Transactions Therewith").

In this brochure particular attention is paid to the following types of real estate: land plots, buildings and constructions, residential and nonresidential premises.

## **1.2.2 Land Plots**

### **1.2.2.1 General Overview**

A land plot is recognized as a part of the earth's surface whose borders are defined in accordance with federal laws.

The owner of a land plot has the right to use everything that is situated under and above the land plot's surface unless otherwise provided by Russian Federation legislation.

It is necessary to note that subsoil is the part of the earth's crust located under the soil layer. Within the borders of the Russian Federation, subsoil (inclusive of the subsoil area and the minerals, energy and other resources contained therein) is state property. Subsoil plots may not be the subject of any purchases, sales, gifts, inheritances, contributions, or pledges, nor may they be otherwise alienated. However, subsoil plots may be granted under license for use for purposes of extracting minerals, building and exploiting underground constructions, etc.

Pursuant to subsoil legislation, the owner of a land plot has the right, without performing blasting works, to extract common minerals on a land plot it owns (for instance, sand, clay).

Land plots, as individually defined objects, have unique characteristics, inter alia: certain borders, sizes (areas), locations and cadastre numbers. All main data on land plots, as well as descriptions thereof, are contained in land plot cadastre passports, issued by the state authorities responsible for the cadastral registration of land plots (see section 1.4.2 "Cadastral and Technical Registrations (Inventory)").

### **1.2.2.2 Particularities of Land Plots as Objects of Investment Activities**

While performing investment activities concerning land plots, it is necessary to consider the following most significant particularities of the status of land plots as real estate objects:

#### 1.2.2.2.1 Natural Objects

As land plots are natural objects, land is used in consideration of the requirements of nature protection (ecological) legislation of the Russian Federation. In the interest of land protection, state and local authorities may restrict powers to own, use and manage privately owned land plots.

#### 1.2.2.2.2 Restrictions on the Turnover-Ability of Land Plots

From the point of view of restrictions on turnover-ability, Russian Federation land legislation distinguishes between land plots barred from turnover and land plots with restricted turnover.

Land plots **barred from turnover** may not be privately owned or be the subject of civil transactions. A comprehensive list of such land plots is provided in the Russian Federation Land Code. Such land plots include land occupied by state owned objects, for instance: state nature reserve areas, Federal Security Service objects, and atomic power using objects.

Land plots with **restricted turnover** are not granted to private owners, except in certain cases established by federal laws, but may be the subject of civil transactions. A comprehensive list of such land plots is provided in the Russian Federation Land Code. Such land plots include state and municipally owned land plots, for instance: those located within the forest fund, those occupied by underwater engineering constructions, and those granted for communications purposes and to transport organizations (in particular, for placing airports, railway stations, and terminals).

The turnover of agricultural land is governed by the special Federal Law "On the Turnover of Agricultural Land", which establishes a specific procedure and specific conditions for transactions with land plots of the agricultural designation.

#### 1.2.2.2.3 Usage in Accordance with Designation

Land in the Russian Federation is used in accordance with its approved designation. According to its designation, land in the Russian Federation is divided into seven categories:

- 1) Agricultural land
- 2) Settlement land
- 3) Land for industry, the energy sector, transport, communications, radio broadcasting, television broadcasting, informatics, land for maintaining space activities, defense and security land, and land of other special designations

- 4) Land for specially protected territories and objects
- 5) Forest fund land
- 6) Water fund land
- 7) Reserve land

A land category must be indicated in state and municipal authorities' acts on granting rights to land plots, agreements in which land plots are the subject, state real estate cadastre documents, documents on the state registration of rights to real estate and transactions therewith, as well as others.

The parties to a land plot transaction may not, at their discretion, change the designation (category) of a land plot. The procedure for transferring land from one category to another is established by the Federal Law "On Transfer of Land or Land Plots from One Category to Another". The said Federal Law stipulates, in particular, that until state property has been delimited, land is transferred from one category to another and is assigned to a certain category by the Government of the Russian Federation when the following types of land are being transferred:

- Land necessary for federal needs
- Land for determination or change of boundaries of cities of federal importance – Moscow and St. Petersburg

In other cases, transfers are effected by executive authorities of the constituent territories of the Russian Federation or by local authorities in cases provided for by laws of the constituent territories of the Russian Federation.

#### **1.2.2.2.4 The Process of Dividing the State Ownership of Land into Russian Federation Ownership, Ownership of Russian Federation constituent territories and Municipal Ownership**

Land plots may be state owned, privately owned or municipally owned.

Privately owned land plots are land plots owned by Russian citizens and legal entities, foreign citizens, persons without citizenship and foreign legal entities.

Municipally owned land plots are land plots owned by municipalities (town and rural settlements, etc.).

State owned land plots are land plots owned by the Russian Federation (federal ownership) and by the constituent territories of the Russian Federation.

Pursuant to the Russian Federation Land Code, state ownership encompasses all land not privately or municipally owned.

The process of dividing land into Russian Federation ownership, ownership of Russian Federation constituent territories and municipal ownership, used previously in accordance with the Federal Law "On Dividing the State Ownership of Land", proved to be inefficient, and on July 1, 2006, new principles for dividing the ownership of land were established.

Current legislation has dropped the method of preparation of lists of land plots to be divided. Currently state ownership of land is divided on the basis of the rules for allocating land to the ownership of the Russian Federation, of the constituent territories of the Russian Federation and municipal ownership, which were included in the Federal Law "On Enactment of the Land Code of the Russian Federation".

Land plots with objects of federal property which were granted to federal authorities, to fiscal and unitary enterprises, as well as other land plots and land as set forth in federal laws, are deemed to be in the ownership of the Russian Federation. The same regulations are established for the respective constituent territories and municipal entities of the Russian Federation (within their borders). The cities of Moscow and St. Petersburg have ownership of the land plots being in the property of the constituent territories as well as in the municipal property and situated within the borders of these cities.

The implementation of the abovementioned provisions means that the division of state ownership of land is carried out as of the moment of entry into force of the respective amendments to the Federal Law "On Enactment of the Land Code of the Russian Federation", i.e. as of July 1, 2006. Therefore, the title to other land plots (not mentioned above) is not divided in the majority of cases.

The rules for disposing of land plots depend on the fact of whether the state ownership of such land plots has been divided or not. The disposal of land plots whose title has been divided on the basis of the abovementioned regulations can be carried out by the authorized state authorities of the respective level upon due state registration of the title to such land plots.

The disposal of land plots whose state ownership is not divided shall be carried out by the following bodies:

- Local government bodies of the respective level, as stated in the Federal Law "On Enactment of the Land Code of the Russian Federation", or
- Executive bodies of the state authorities of constituent territories of the Russian Federation (in settlements being administrative centers or capital cities of Russian

Federation constituent territories, if such is provided for by law of the respective constituent territory of the Russian Federation), unless otherwise provided for by Russian Federation legislation on motorways and road activities

The disposal of such land plots in Moscow and St. Petersburg is carried out by the executive bodies of these constituent territories of the Russian Federation, if such authority has not been transferred to institutions of local government and unless otherwise provided for by Russian Federation legislation on motorways and road activities.

Legislation establishes that lacking the state registration of the title to land plots whose state ownership is not divided shall not be a hindrance for disposing of them.

#### **1.2.2.2.5 Interdependence Between Titles to Land Plots and Titles to Real Estate Objects Located Thereon**

The interdependence between titles to land plots and titles to real estate objects located thereon is shown in the following principle provisions of the Russian Federation Land Code on the transfer of titles to land plots.

Land plots may not be alienated without the constructions located thereon provided that the constructions and the land plots belong to one and the same person. If buildings, constructions, structures and the land plots they are located on belong to one person, they may be alienated only together with such land plots, with the following exceptions:

- Alienating parts of buildings, constructions and structures that may not be specifically singled out together with parts of land plots
- Alienating buildings, constructions and structures located on land plots barred from turnover

In case of transferring the title to a building, construction or structure located on another individual's land plot to another person, such person acquires the right to use the respective part of the land plot occupied by the building, construction or structure which is required for its use on the same conditions and to the same extent as the previous owner.

The owner of a building, construction or structure located on another individual's land plot has the right of first refusal on purchases and leases of such land plot.

It is necessary to note that the Russian Federation Land Code establishes the principle of "unity of the fate of a land plot and the real estate securely attached thereto," according to which all objects securely attached to a land plot shall follow the fate of such land plot, with the exception of certain cases stipulated by federal laws.

#### **1.2.2.2.6 Restrictions on Rights of Foreign Individuals and Legal Entities to Certain Types of Land Plots**

Pursuant to current Russian Federation legislation, foreign citizens, foreign legal entities, persons without citizenship, as well as Russian legal entities in which more than 50% of the share capital is held by foreign citizens, legal entities or persons without citizenship, may hold only leasehold rights to agricultural land plots.

Furthermore, foreign citizens, persons without citizenship and foreign legal entities may not hold titles to land plots located on border territories, the list of which is approved by the President of the Russian Federation in accordance with the federal legislation on the State Border of the Russian Federation, or titles to land plots located on other special territories.

### **1.2.3 Buildings and Constructions**

#### **1.2.3.1 General Overview**

Buildings and constructions are often objects of investment activities. Buildings and constructions are real estate objects due to their characteristic of inseparable attachment to land and the impossibility of relocating them without incommensurate damage to their purpose.

As individually defined objects, buildings and constructions have unique characteristics, inter alia: addresses (locations), names, areas, numbers of stories and designations. The main data on buildings and constructions, as individually defined real estate objects, are contained, in particular, in the cadastre passports of the respective real estate objects, as well as in other documents (see section 1.4.2 "Cadastral and Technical Registrations (Inventory)").

#### **1.2.3.2 Particularities of Buildings and Constructions as Objects of Investment Activities**

While performing investment activities concerning buildings and constructions it is necessary to consider the following most significant particularities of the status of buildings and constructions as real estate objects:

##### **1.2.3.2.1 City Planning Rules Concerning Construction, Reconstruction and Capital Repairs of Buildings and Constructions**

When carrying out construction, reconstruction or capital repairs of buildings, structures or constructions, it is necessary to consider the regulations and rules established by legal acts of the Russian Federation in the field of city planning design, design and construction of real estate (see section 1.6 "Legal Regulation of Construction Activities").

#### 1.2.3.2.2 Buildings and Constructions that are Historical and Cultural Landmarks

Pursuant to Russian Federation legislation, cultural heritage objects include buildings and constructions, as well as related creations of art, sculptures, applied and decorative art, science and technology objects, and other objects of material culture which appeared as a result of historical events and are valuable from the point of view of history, architecture, city planning, art, science and technology, social culture, etc., are evidence of epochs and civilizations, and are authentic sources of information on the genesis and development of culture. These said real estate objects are subject to state registration for the purposes of their preservation.

The state protects cultural heritage objects (historical and cultural landmarks) by means of imposing liabilities for damaging or destroying respective objects, controlling the development of city planning and design documents, and granting permits to carry out construction, sanitation and other works in established cases. Until completion of the procedures for dividing the state ownership of cultural heritage objects into federal ownership, ownership of constituent territories of the Russian Federation and municipal ownership, the privatization of cultural heritage objects in a number of cases has been suspended.

One of the main principles for using a cultural heritage object (historical and cultural landmark) is the preservation of its original exterior and interior. In this regard, in the case of privatization of cultural heritage objects, as well as in the case of granting of the lease rights to the said state owned objects to private parties, the rights of the private owners and lessees are encumbered by obligations to maintain and preserve the cultural heritage objects (preservation obligations). When restoring and repairing buildings and structures pertaining to historical and cultural landmarks, the design documentation is subject to approval by the state authorities for preserving landmarks and shall be duly confirmed. Restorations and repairs of such buildings and structures are carried out under control of the state authorities for preserving landmarks.

The Single State Register of Cultural Heritage Objects (Historical and Cultural Landmarks) of the Peoples of the Russian Federation, which contains data on cultural heritage objects, is currently being compiled in the Russian Federation. The respective authority responsible for protecting cultural heritage objects will issue cultural heritage object passports, for buildings and constructions inserted in the said Register, to the owners of the respective real estate objects. A cultural heritage object passport is one of the mandatory documents required for registering titles to buildings or constructions in case of transactions therewith, provided that such buildings or constructions have been inserted in the Single State Register of Cultural Heritage Objects (Historical and Cultural Landmarks) of the Peoples of the Russian Federation. Currently, historical and cultural landmarks are registered on the basis of respective lists maintained by executive authorities of the constituent territories of the Russian Federation and, at the federal level, by the federal body ensuring the protection of cultural heritage objects.



### **1.2.3.2.3 Interdependence Between Titles to Land Plots and Titles to Buildings and Constructions Located Thereon**

While planning and implementing investment activities concerning buildings and constructions, it is necessary to take into account the provisions of Russian Federation legislation that establish interdependence between titles to buildings and constructions and titles to land plots thereunder (see section 1.2.2.2.5 "Interdependence Between Titles to Land Plots and Titles to Real Estate Objects Located Thereon").

## **1.2.4 Residential and Nonresidential Premises**

### **1.2.4.1 General Overview**

Residential and nonresidential premises are real estate objects by virtue of direct stipulation of the law. The characteristic of the status of residential and nonresidential premises as real estate objects is the requirement for state registration of the rights thereto and transactions therewith in cases and in accordance with the procedure established by Russian Federation legislation.

Residential and nonresidential premises are real estate objects that are distinct from the buildings in which they are located although inseparably attached to. It is necessary to note that a single building may contain both residential and nonresidential premises. Residential premises are distinct premises designated for individuals' residence that must meet sanitary and technical requirements and rules established in the Russian Federation, while nonresidential premises are premises not designated for individuals' residence. Due to the fact that the law does not provide for a definition of nonresidential premises, it is advisable to take into consideration that, according to general provisions of the laws of the Russian Federation and existing court procedure, nonresidential premises being real estate objects shall meet such a criterion as the possibility of their independent use without changing the designated use of the building as a whole.

As individually defined real estate objects, residential and nonresidential premises have unique characteristics: addresses (locations), names, areas, and designations. All main data on residential and nonresidential premises are contained, in particular, in premises cadastre passports, technical passports (excerpts from technical passports), apartment passports and real estate object plans (see section 1.4.2 "Cadastral and Technical Registrations (Inventory)").

### **1.2.4.2 Particularities of Residential and Nonresidential Premises as Objects of Investment Activities**

While performing investment activities connected with acquiring rights to nonresidential premises, it is necessary to take into account the absence of a nonresiden-

tial premises regime developed in detail, for example the rights of nonresidential premises owners to the common property of the buildings in which such premises are located are not clearly defined. Investment activities that require concluding transactions with residential premises must be performed in conformity with the special provisions of Russian Federation legislation concerning residential premises and, most importantly, the Russian Federation Housing Code. Furthermore, the dependent nature of the said objects with respect to the buildings in which they are located should be taken into account.

#### **1.2.4.2.1 Designation**

According to the general rule, residential premises are designated for individuals' residence. Residential premises may be used for performing professional activities or individual entrepreneurial activities by individuals that lawfully reside at these premises. Such use may not violate other individuals' rights and lawful interests as well as requirements for residential premises. In order to use residential premises for other purposes not related to residence, it is necessary to convert such premises into nonresidential premises. Residential buildings are prohibited from housing any industrial productions. The conditions and procedure for transferring residential premises to the nonresidential premises category, and vice versa, are determined by the Russian Federation Housing Code, subject to the requirements of legislation on city planning activities.

#### **1.2.4.2.2 Rights of Individuals Residing Together with Owners of Residential Premises**

Pursuant to Russian Federation legislation, family members of an owner of residential premises have rights to use the residential premises equal to those of the owner, unless otherwise provided for by an agreement between them.

Family members of an owner include his/her spouse, children and parents residing together with the owner at the premises owned by him/her. Other relatives and disabled individuals, and, on extraordinary occasions, other individuals, may be recognized as family members of the owner if they have lived with the owner at the premises as members of his/her family.

The right of use of residential premises by the owner's family members terminates in case of transfer of the title to the premises to another person, as well as in case of termination of family relations with the owner. In case of termination of family relations with the owner, the right of former family members to use the residential premises can be preserved for a definite period of time on the basis of a court ruling. Prior to the lapse of the said period of time the right of use terminates simultaneously with the termination of the title to the given residential premises of its owner.

#### **1.2.4.2.3 State Authorities' Consent to Alienation of Residential Premises**

Residential premises occupied by underage family members of the owner of the residential premises who are in his/her custody or guardianship, or those left without parental custody, may be alienated only upon the consent of the Trustee Board if such alienation affects the rights and protected interests of the said persons.

#### **1.2.4.2.4 Common Property of the Owners of Residential Premises in Buildings**

The owners of premises in an apartment building have common share ownership rights to the building's common premises, load-bearing constructions, mechanical, electrical, plumbing and other equipment, located outside or inside apartments, which provide services to multiple apartments, as well as to the land plot on which the apartment building is located, along with the greenery and public amenities elements.

An apartment purchaser directly acquires common share ownership right to the common property in the apartment building by virtue of acquisition of the title to an apartment in such building.

Apartment owners may not alienate their shares in the ownership rights to the common property of a residential building or perform any other actions which entail transferring such shares independently of titles to apartments.

### **1.3 Subjects of Rights to Real Estate**

All participants in legal relations that may be subjects of rights to real estate in accordance with Russian Federation legislation may be conditionally divided into two groups: private subjects and public subjects.

Private subjects include:

- Individuals (Russian citizens, foreign citizens and persons without citizenship)
- Legal entities (Russian and foreign)

Public subjects include:

- The Russian Federation
- The constituent territories of the Russian Federation
- Municipalities

Public and private subjects of rights to real estate are vested with various volumes of rights. The rights and obligations of each subject of rights to real estate have their own particularities that are established by Russian Federation legislation.

For instance, **certain types of real estate** may be owned only by the Russian Federation or its constituent territories (for example, land plots barred from civil turnover).

**Certain types of rights to real estate** may be held only by certain subjects. For instance, subjects of the right of permanent (perpetual) use of land plots may be state and municipal establishments, public enterprises, centers of historical heritage of the presidents of the Russian Federation, and state and local authorities. Rights of permanent (perpetual) use are not granted to other legal entities or individuals. At the same time, the said rights of individuals and legal entities to land plots in state or municipal ownership which commenced prior to October 30, 2001, are preserved.

The difference in the legal status of participants in legal relations in the real estate field is further expressed by the difference in the methods of acquisition of rights to real estate. In addition to the possibility of acquiring rights on the basis of ordinary civil transactions, the Russian Federation, Russian Federation constituent territories and municipalities, as opposed to citizens and legal entities, are entitled to acquire titles to real estate through other methods, for example by recalling, including by means of buying out, real estate for state and municipal needs. Special legislative rules regulate the particularities of acquisitions of titles to land plots and rights of terminable free use of land plots by religious organizations.

### 1.3.1 Russian Citizens and Legal Entities

Russian citizens and legal entities may hold titles to real estate and have other rights to real estate in the cases stipulated by current Russian Federation legislation, and, in particular, have equal access to acquiring rights to land plots in accordance with provisions of the Civil Code and the Land Code of the Russian Federation.

Citizens' and legal entities' titles, including land titles, are recognized and protected by the Russian Federation Constitution.

Cases of restrictions of Russian citizens' and legal entities' rights to real estate objects are established by the Russian Federation Constitution and federal laws. Thus, for instance, citizens and legal entities may not hold titles to forest fund land, water objects connected with other water objects, or minerals that are not widespread.

Restrictions, established by legislation, on the acquisition of titles to agricultural land by legal entities in whose registered capitals foreign citizens, legal entities or persons

without citizenship hold a share in excess of 50% are reviewed in section 1.2.2.2.6 "Restrictions on Rights of Foreign Individuals and Legal Entities to Certain Types of Land Plots".

### **1.3.2 Foreign Citizens, Persons without Citizenship and Foreign Legal Entities**

According to the general rule, foreign citizens, persons without citizenship and foreign legal entities may acquire rights to real estate on equal bases with Russian citizens and legal entities, with the exception of specific cases established by law (Part 3, Article 62 of the Russian Federation Constitution).

Examples of legally established restrictions are as follows:

- Foreign citizens, persons without citizenship, and foreign legal entities may not hold titles to land plots located on border territories, the list of which is to be determined by the President of the Russian Federation, or located on other specifically determined territories. Until the President of the Russian Federation determines the list of border territories, land plots located on border territories are prohibited from being granted for ownership to foreign citizens, persons without citizenship, and foreign legal entities.
- The Russian Federation Land Code stipulates that titles to state and municipally owned land plots may be granted to foreign citizens, persons without citizenship and foreign legal entities only for payment, whereas in certain cases Russian citizens and legal entities are entitled to obtain state and municipally owned land plots free of charge.
- The Law on turnover of agricultural land bans acquisitions of titles to agricultural land by foreign citizens, persons without citizenship and foreign legal entities. The said parties are only allowed to lease agricultural land plots.

### **1.3.3 The Russian Federation, Russian Federation constituent territories, and Municipalities**

Public subjects of legal relations – the Russian Federation, Russian Federation constituent territories and municipalities – acquire and exercise their rights and obligations through relevant authorities (governmental and local authorities). The powers of governmental and local authorities to manage real estate are established by acts determining the status of such authorities.

Public subjects have a special status with respect to the possession and management of real estate objects. Russian Federation legislation determines the particular types of real estate that may be owned exclusively by the state, for example, particular buildings and constructions recognized as historical and cultural landmarks or land plots occupied by state wilderness areas (see section 1.2.2.2.2 "Restrictions on the Turnover-Ability of Land Plots").

A prominent characteristic of public constituent territories is the fact that the Russian Federation, constituent territories of the Russian Federation and municipalities are not only owners of real estate, but also have state administrative powers enabling them to regulate management, possession and use of real estate objects by other subjects of rights. Furthermore, the jurisdiction of governmental authorities includes issues such as maintaining the state registration of real estate objects and protecting land and other real estate objects of state significance.

## **1.4 System of Registration of Real Estate Objects and Rights Thereto**

### **1.4.1 Concept and Main Types of Registration**

In Russia there are currently two main systems: the system of state registration of real estate objects and the system of state registration of rights to real estate and transactions therewith. Moreover, state registrations of land plots and other real estate objects are carried out in a different manner.

Land plots, buildings and structures, as well as other real estate objects are registered in the course of cadastral and technical registrations (inventory).

Rights of subjects to each real estate object, data on restrictions on the said rights, as well as information on transactions conducted with the real estate are registered within the procedure of state registration of rights to real estate and transactions therewith by entering the respective records in the Single State Register of Rights to Real Estate and Transactions Therewith.

Nonetheless, legislation of the Russian Federation provides for significantly changing the current procedure by combining the said registration systems in the near future. The first stage contemplates combining the procedures for registering land plots and other real estate objects, which should be completed by 2010. This will result in the creation of a single state cadastre of real estate – a systematized collection of data on all real estate registered in Russia. Further, at the second stage it is planned to create a single federal information system, including not only information on real estate, but also information on rights to real estate and transactions therewith. It is supposed that this information system will be formed by 2012.

### **1.4.2 Cadastral and Technical Registrations (Inventory)**

Real estate objects (land plots, buildings, constructions, residential and nonresidential premises, unfinished constructions) are described and individualized as a result of the cadastral and technical registrations (inventory) of such real estate objects.

As a result of cadastral and technical registrations (inventory), the respective real estate objects acquire characteristics that allow for unambiguously distinguishing them from all other real estate objects. In particular, during cadastral and technical registrations (inventory) a real estate object is assigned a cadastre number which exists as long as such real estate object is a single object of registered rights. Furthermore, during cadastral and technical registrations plans of real estate objects are prepared, land plots and real estate objects attached thereto are described, and the exact locations (addresses) of real estate objects are indicated, etc.

State cadastral registrations of land plots and state technical registrations of capital construction structures (buildings, constructions, residential and nonresidential premises, unfinished constructions) are carried out by authorized state bodies and institutions at the locations of such real estate.

The state cadastral registration of a land plot results in execution of a cadastre passport of the land plot, which contains information on the borders and area of the land plot, the cadastral number, the buildings and structures located on the land plot, as well as other unique characteristics of the plot.

State technical registrations of capital construction structures result in execution of cadastre and technical passports of the respective structures. The said documents contain information on the main parameters of the real estate (address, area, cadastral number, designation, number of stories, etc.), as well as its plan. A cadastre passport contains information on the real estate that is required for the state registration of rights thereto or transactions therewith. As compared to a cadastre passport, a technical passport contains more detailed information on the technical characteristics of the real estate.

The system of technical registration of real estate is currently undergoing both structural and qualitative changes. It is assumed that, as of January 1, 2010, the procedure of technical description and registration of capital construction structures will change completely and be similar to the current procedure of cadastral registration of land plots.

### **1.4.3 State Registration of Rights to Real Estate and Transactions Therewith**

Rights to real estate and transactions therewith are subject to mandatory state registration in the Single State Register of Rights to Real Estate and Transactions

Therewith. State registration is a legal act of the state recognizing and confirming rights to real estate.

The registration of rights to real estate is crucial since rights to real estate objects subject to state registration commence, change or terminate only upon the insertion of the respective entries in the Single State Register of Rights to Real Estate and Transactions Therewith.

The existing system of state registration of rights to real estate and transactions therewith was established by the Federal Law "On State Registration of Rights to Real Estate and Transactions Therewith" dated July 21, 1997, No. 122-FZ.

Rights to real estate that commenced prior to the entry into force of the Federal Law "On State Registration of Rights to Real Estate and Transactions Therewith" (January 31, 1998) are recognized as legally valid even if they have not undergone the state registration introduced by the said Federal Law. The state registration of such rights may be performed upon the request of the holders of such rights, with certain exceptions. In particular, state registration of rights that commenced prior to the entry into force of the Federal Law "On State Registration of Rights to Real Estate and Transactions Therewith" is required in case of state registration of the rights to such real estate that commenced after the said Federal Law took effect or in case of state registration of a transaction that was conducted with respect to such real estate after the said Federal Law took effect. Land plots whose state ownership is not divided are the exception. State registration is not required for the state title to such land plots.

As a rule, the state registration of rights and transactions is performed on the basis of an application filed by the rightholder (party holding the title or other proprietary right to the respective real estate) or by the parties to the transaction. An application for state registration must include the documents required for conducting it pursuant to Russian Federation legislation, in particular:

- Documents establishing the existence, commencement, termination, transfer, and restriction (encumbrance) of the rights to the real estate object (for instance, agreements, acts of state or local authorities, court rulings, etc.)
- The cadastre passport of the respective real estate

A performed state registration of the commencement and transfer of rights to real estate is confirmed by a Certificate of State Registration of Rights. A performed state registration of agreements and other transactions is confirmed by special registration inscriptions on the documents that convey the content of the transactions.

State registrations of rights to real estate and transactions therewith are performed at the location of the respective real estate by territorial administrations of the Federal



Service for State Registration, Cadastre and Cartography (formerly known as the Federal Registration Service).

It is important that an investor know that the fact of state registration of rights to real estate is, in and of itself, not an absolute guarantee of protection of the investor's rights and interests. A state registration of rights to real estate may be annulled upon a court ruling in case of invalidation of the legal act or agreement being the grounds for registration of the rights. Therefore, a legal due diligence on the rights acquired by the investor, conducted by independent experts, is a necessary condition of any transaction with real estate in Russia.

## **1.5 Procedure for Acquiring Rights to Real Estate**

### **1.5.1 General conditions for acquiring rights to real estate**

For the purposes of this brochure the procedure for acquiring rights to real estate is understood as the main actions stipulated by legislation of the Russian Federation that result in acquisition of rights to particular real estate.

The procedure for acquiring rights to real estate has certain features in each particular case and depends on the conditions for acquiring such rights, which include, in particular:

- the type of real estate to which rights are acquired (for example: a land plot, building, structure, etc.)
- the acquired right to real estate (for example: title, lease right (long-term or short-term), lien (mortgage), right of limited use of another's land plot (servitude), etc.)
- the basis for acquiring rights to real estate (for example: acquiring rights to real estate on the basis of an agreement or other transaction, an act of a state or local government authority, a court ruling, etc.)
- the right to real estate belonging to the party alienating the right to the given real estate (for example: title (private, state, municipal), lease right, right of economic management, right of operational management, right of permanent perpetual use of a land plot, etc.)
- the objective of acquiring the right to real estate (for example: acquiring rights to a land plot for the purpose of construction, acquiring rights to a building or structure for the purpose of reconstruction, etc.)

This section reviews the most common means of acquiring rights to real estate within the framework of implementing investment projects, such as, in particular:

- acquiring the title or lease right to a privately owned land plot
- acquiring the title or lease right to a state or municipally owned land plot
- acquiring the title or lease right to a privately owned building or structure
- acquiring the title or lease right to a state or municipally owned building or structure

In all cases of acquiring rights to real estate the individual features of the status of the real estate should be considered (see section 1.2.2.2 "Particularities of Land Plots as Objects of Investment Activities," section 1.2.3.2 "Particularities of Buildings and Constructions as Objects of Investment Activities"), as well as the features of the status of the acquirer and the party alienating the rights to the real estate (see section 1.3 "Subjects of Rights to Real Estate").

## 1.5.2 Procedure for acquiring the title to a land plot

From the standpoint of investment activities, most often the most attractive option is acquiring the title to a land plot since the title grants the greatest scope of authority in relation to the land plot.

A large portion of land in Russia is not private, but rather state or municipally owned. Such land plots are granted to the ownership of citizens and legal entities for a fee, with certain exceptions.

The main distinction of the procedure for acquiring the title to a state or municipally owned land plot is that such land plots are disposed of on the basis of a resolution of state or local government bodies authorized to dispose of such land plots. In this regard, acquiring the ownership of a state or municipally owned land plot generally requires taking a large number of required actions in connection with undergoing several administrative procedures.

The procedure for acquiring state or municipally owned land plots for the purpose of construction differs from the procedure for acquiring the ownership of such land plots for purposes not connected with construction. Furthermore, there are special procedures for granting state or municipally owned land plots for residential construction as well as for comprehensively developing them for the purposes of residential construction.

### 1.5.2.1 Procedure for acquiring the title to a privately owned land plot

Within the framework of implementing investment projects, one of the most common means of acquiring the title to a privately owned land plot is concluding a sale and purchase agreement for the land plot.

Before a potential investor takes a decision on acquiring the ownership of a particular land plot, it is recommended that the seller's rights to the given plot be analyzed. More detailed information on this issue is provided in section 3.2. of this brochure "Verifying Rights to Real Estate (Investment Objects) to be Acquired".

The main stages of acquiring the title to a privately owned land plot on the basis of a sale and purchase agreement are as follows:

- state cadastral registration of the land plot (if it has not been previously carried out for the plot)
- conclusion of the sale and purchase agreement for the land plot
- state registration of the buyer's title to the land plot

Explanations of each stage are provided below.

### **State cadastral registration of the land plot**

Only a land plot whose borders are duly defined and which has undergone state cadastral registration may be the object of a sale and purchase. Therefore, if the land plot offered for sale has not undergone state cadastral registration, such procedure must be carried out.

The state cadastral registration of a land plot is carried out in the manner established by law (see section 1.4.2 "Cadastral and Technical Registrations (Inventory)").

### **Conclusion of the sale and purchase agreement for the land plot**

A sale and purchase agreement for a land plot is concluded in writing by drawing up one document signed by the parties.

A sale and purchase agreement for a land plot must contain the material conditions stipulated by legislation of the Russian Federation, in the absence of which the agreement is deemed not concluded, in particular: the price of the land plot and data that allow for precisely identifying the land plot. A sale and purchase agreement must also comply with other requirements stipulated by current legislation of the Russian Federation.

It should be noted that Russian legislation provides for certain special restrictions concerning the conditions of a sale and purchase agreement for a land plot. The following conditions are invalid when incorporated into a sale and purchase agreement for a land plot:

- establishing the seller's right to buy back the land plot at its discretion
- restricting further disposal of the land plot, including restricting mortgage, lease of the land plot, other transactions with the land
- limiting the seller's liability if rights to the land plot are claimed by third parties

The interests of a land plot purchaser are further protected by the requirement, established by the Land Code of the Russian Federation, for the seller to provide the buyer with all available information on the encumbrances on the land plot and the restrictions on its use. If the seller furnishes the buyer with knowingly false information that may affect the buyer's decision to purchase the given land plot, the buyer is entitled to claim for a reduction in the purchase price or for termination of the sale and purchase agreement for the land plot and compensation for the losses it has incurred. In particular, such information includes information on encumbrances on the land plot and restrictions on its use, on the permit to develop the land plot, on use of neighboring land plots, having a significant effect on the use and value of the sold land plot, and other information.

### **State registration of the buyer's title to the land plot**

The transfer of a title under a sale and purchase agreement for a land plot is subject to state registration. The title of a purchaser of a land plot accrues as of the moment of such state registration and is verified by a certificate of state registration of right.

The state registration of a buyer's title based on a sale and purchase agreement is carried out in the manner established by law (see section 1.4.3 "State Registration of Rights to Real Estate and Transactions Therewith").

#### **1.5.2.2 Procedure for Acquiring the Title to a State or Municipally Owned Land Plot for the Purpose of Construction**

In practice the granting of ownership of state or municipally owned land plots occurs significantly less frequently than the granting of lease rights to such land plots. This is primarily due to the positions of state and local government authorities, formed amid the lack of delimitation of the state ownership of land and insufficient legislative regulation.

In order to acquire a state or municipally owned land plot, within the framework of a preliminary legal analysis it is necessary to first identify the state or local government body that is authorized to dispose of the respective plot. Competent state or local government authorities themselves usually select land plots for the proposed construction of a structure and offer them to investors on certain conditions.

In accordance with the Land Code of the Russian Federation, the ownership of land plots for construction is granted at tenders. The exception is when a land plot is granted to a party with which an agreement on developing a built-up area is concluded

pursuant to city planning legislation of the Russian Federation (see section 1.6.2. of this brochure "Development of Built-up Areas"). Acquiring rights to a land plot without tenders being conducted is also possible in compliance with the procedure of preliminary approval of the locations of structures, however in such case a plot is not granted for ownership but rather for lease (see section 1.5.3.2. "Procedure for acquiring the lease right to a state or municipally owned land plot for the purpose of construction").

It is also necessary to note that from January 1, 2010, the granting of land plots for construction from state or municipally owned land will be carried out, with certain exceptions, only given the existence of the rules for land use and development (see section 1.6.1 "City Planning Design, Zoning and Territory Planning").

The main stages of acquiring the title to a state or municipally owned land plot for the purpose of construction (without preliminary approval of the location of the structure) are as follows:

- 1) formation of the land plot and execution of its cadastral registration
- 2) conducting tenders for selling the land plot and signing of the protocol on the results of the tenders
- 3) conclusion of a sale and purchase agreement for the land plot
- 4) state registration of the buyer's title to the land plot

Explanations of each stage are provided below.

### **Formation of the land plot**

The first stage – formation of the land plot – is required for separating the land plot from the total mass of state or municipal land and defining its borders pursuant to the established procedure. The formation of the land plot is carried out by state or local government authorities and includes the performance of cadastral works and the state cadastral registration of the land plot (see section 1.4.2 "Cadastral and Technical Registrations (Inventory)"), determination of the permitted use of the land plot, definition of the technical conditions for connecting future structures to engineering service networks, adoption of a resolution on conducting tenders and publication of information on conducting the tenders.

### **Conducting tenders for selling the land plot and signing of the protocol on the results of the tenders**

The procedure for organizing and conducting tenders is currently regulated by the Decree of the Government of the Russian Federation "On Organizing and Conducting

Tenders for Selling State or Municipally Owned Land Plots or the Right to Conclude Lease Agreements for Such Land Plots” dated November 11, 2002, No. 808.

The local government or executive state body authorized to grant the respective land plot, or a specialized organization operating on the basis of an agreement therewith, acts as the organizer of the tenders (see section 1.3 “Subjects of Rights to Real Estate”).

The local government or executive state body authorized to grant the respective land plot determines, on the basis of a report of an independent appraiser, the starting price of the land plot, the incremental bid amount in the case of conducting the tenders in the form of an auction open in terms of the form of submitting price offers, as well as the deposit amount and the mass media that is to publish the notice on conducting the tenders.

The results of the tenders are documented by a protocol, signed by the organizer of the tenders, the auctioneer (in the case of conducting an auction open in terms of the form of submitting price offers) and the winner of the tenders on the day the tenders are conducted. A sale and purchase agreement should be concluded no later than 5 days from the date the protocol is signed.

Information on the results of the tenders is published in the same mass media in which the notice on conducting the tenders was published, within a month from the date the sale and purchase agreement for the land plot is concluded.

### **Conclusion of a sale and purchase agreement for the land plot**

The sale and purchase agreement for the land plot is concluded by the local government or state body authorized to grant the respective land plot (see section 1.3 “Subjects of Rights to Real Estate”).

The general requirements for the form and contents of the agreement, described in section 1.5.2.1 of this brochure “Procedure for acquiring the title to a privately owned land plot,” must also be observed if concluding a sale and purchase agreement for a state or municipally owned land plot.

### **State registration of the buyer’s title to the land plot**

The transfer of the title under the sale and purchase agreement for the land plot is subject to state registration. The title of the purchaser of the land plot accrues as of the moment of such state registration and is verified by a certificate of state registration of right.

The state registration of the buyer’s title is carried out in the manner established by law (see section 1.4.3 “State Registration of Rights to Real Estate and Transactions Therewith”).

### **1.5.2.3 Procedure for Acquiring the Title to a State or Municipally Owned Land Plot for Non-Construction Purposes**

It should be noted that in Russia it is possible that an owner of a building is not the owner of the land plot on which the building is located, but rather has, for example, the right to lease it. For instance, such a situation may occur as a result of privatization of state property or as a result of constructing a new building on a leased land plot. Thus, serving as an example of acquiring the ownership of a land plot for non-construction purposes is the case where an owner of a building or structure located on a land plot acquires the ownership of the land plot (privatization).

An owner of a building, structure or construction has the exclusive right to acquire the ownership (privatize) the land plot on which its building, structure or construction is located.

An indivisible land plot accommodating a building (premises therein) belonging to several parties by title may be acquired by the said parties for joint shared ownership.

Land legislation of the Russian Federation stipulates the following procedure for acquisition of the title to a state or municipally owned land plot by the owner of a building or structure located on such land plot:

- 1) filing of an application for acquiring rights to the land plot
- 2) adoption of a resolution to grant the land plot
- 3) conclusion of a sale and purchase agreement for the land plot (aside from cases of gratuitous granting)
- 4) state registration of the acquirer's title to the land plot

Explanations of each abovementioned stage are provided below.

#### **Filing of an application for acquiring rights to the land plot**

Russian citizens and legal entities, as well as foreign citizens and foreign legal entities, considering the restrictions established by land legislation of the Russian Federation (see section 1.3 "Subjects of Rights to Real Estate"), owning buildings, structures or constructions located on state or municipally owned land plots have the exclusive right to privatize the respective land plots.

The mentioned parties furnish the state or local government body authorized to dispose of the land plots with an application for acquiring rights to a land plot, with the cadastral passport of the land plot attached. Furthermore, the parties must submit

documents confirming the state registration of the rights to the buildings, structures and constructions (or premises therein) located on the land plot, and, in cases stipulated by legislation of the Russian Federation, other documents confirming the accrual of the rights to such real estate.

### **State cadastral registration of the land plot**

If the cadastral registration of the land plot was not carried out previously, the authorized body issues the applicant a layout plan of the land plot in the respective area. At its own expense, the applicant provides for the performance of the cadastral registration of the land plot.

The borders and size of the land plot are defined considering the actual usable area of the land plot in accordance with requirements of land and city planning legislation in light of city planning restrictions, the borders of neighboring land plots (if any), and the natural borders of the land plot.

### **Adoption of a resolution to grant the land plot**

This stage characterizes the main feature of the procedure for acquiring the title to a state or municipally owned land plot. The given feature is that rights to a state or municipally owned land plot are granted on the basis of a resolution of a state or local government body, which in turn serves as the basis for concluding the sale and purchase agreement for the land plot.

The resolution to grant the title to the land plot is adopted by the executive state body or local government body in whose jurisdiction the land plot is located (see section 1.3 "Subjects of Rights to Real Estate").

The adoption of the resolution to grant the ownership of the land plot is accompanied by the preparation of a draft sale and purchase agreement for the land plot, which is then sent to the applicant.

### **Conclusion of a sale and purchase agreement for the land plot**

The sale and purchase agreement for the land plot is concluded on the basis of the resolution of the local government body or executive state body authorized to grant the respective land plot.

The general requirements for the form and contents of the agreement, described in section 1.5.2.1 of this brochure "Procedure for acquiring the title to a privately owned land plot", must also be observed in the case of concluding a sale and purchase agreement for a state or municipally owned land plot.



## **State registration of the acquirer's title to the land plot**

The transfer of the title under the sale and purchase agreement for the land plot is subject to state registration. The title of the acquirer of the land plot accrues as of such state registration and is verified by a certificate of state registration of right.

The state registration of the buyer's title is carried out in the manner established by law (see section 1.4.3 "State Registration of Rights to Real Estate and Transactions Therewith").

### **1.5.3 Procedure for Acquiring the Lease Right to a Land Plot**

The most common case of acquiring rights to a land plot for the purposes of implementing an investment project is acquiring the lease right to a land plot.

As in the case of acquiring title, the procedure for acquiring the lease right to a state or municipally owned land plot, in contrast to the procedure for acquiring the lease right to a privately owned land plot, provides for the competent state or local government body to adopt a respective resolution on granting the land plot. The procedure for acquiring the lease of a state or municipally owned land plot for construction purposes differs from the procedure for acquiring the lease of such land plots for other purposes.

#### **1.5.3.1 Procedure for Acquiring the Lease Right to a Privately Owned Land Plot**

The process of acquiring the lease right to a privately owned land plot can be conditionally divided into the following main stages:

- 1) state cadastral registration of the land plot (if not carried out previously)
- 2) conclusion of a lease agreement for the land plot
- 3) state registration of the lease agreement for the land plot (if necessary)

Additional information on certain conditions of lease agreements that should be given particular attention is presented in section 3.6.10 "Lease Agreement and Preliminary Agreements".

Explanations of each abovementioned stage are provided below.

#### **Conclusion of a lease agreement for the land plot**

The lease agreement for the land plot is concluded in writing by drawing up one document signed by the parties.

The lease agreement for the land plot must contain the material conditions stipulated by legislation of the Russian Federation (in the absence of which the agreement is deemed not concluded), in particular: a description of the land plot that allows for definitively identifying the given plot and indication of the rent amount. Furthermore, the lease agreement for the land plot must also comply with other requirements stipulated by current legislation of the Russian Federation.

The Land Code of the Russian Federation establishes a number of additional guarantees of the rights of a tenant. In the event the landlord provides knowingly false information that may affect

the decision of the tenant of the given land plot, the tenant is entitled to claim for a reduction in the rent or for termination of the lease agreement for the land plot and compensation for losses it has incurred. In particular, such information includes information on encumbrances on the land plot and restrictions on its use, on the permit to develop the land plot, on use of neighboring land plots, having a significant effect on the use and value of the sold land plot, and other information.

### **State registration of the lease agreement for the land plot**

The state registration of the lease of the land plot is carried out through the state registration of the lease agreement for the land plot.

Lease agreements for land plots concluded for terms of no less than one year are subject to state registration. Such agreements enter into force as of their state registration.

The state registration of the lease agreement for the land plot is carried out in the manner established by law (see section 1.4.3 "State Registration of Rights to Real Estate and Transactions Therewith". The state registration of the lease agreement is certified by a special registration inscription on the lease agreement for the land plot.

#### **1.5.3.2 Procedure for Acquiring the Lease Right to a State or Municipally Owned Land Plot for Construction Purposes**

At present, land plots may be granted for lease for construction purposes under two different procedures:

- 1) Without preliminary approval of the locations of structures
- 2) With preliminary approval of the locations of structures

In the case of granting land plots without preliminary approval of the locations of structures, competent state or local government bodies usually choose land plots for the proposed construction of a structure and offer them to investors on certain conditions

for the construction. In the second case, the investor participates in selecting a land plot for locating a structure.

It should be noted that, from 1 January 2010, the granting of land plots for construction from state or municipally owned land will be carried out, with certain exceptions, only given the availability of the rules for land use and development. For more detailed information on city planning documentation see section 1.6.1 "City Planning Design, Zoning and Territory Planning":

The procedure for granting a land plot for lease differs in each above case. A land plot is granted for lease for construction **without preliminary approval of the location** of the structure at tenders in the same manner as a land plot granted for ownership (see section 1.5.2.2. "Procedure for acquiring the title to a state or municipally owned land plot for the purpose of construction"):

- 1) Formation of the land plot
- 2) Conducting tenders (auctions) for selling the right to conclude a lease agreement for the land plot and signing of the protocol on the results of the tenders
- 3) Conclusion of a lease agreement for the land plot
- 4) State registration of the lease agreement for the land plot

The law also provides for the possibility of granting a plot for lease without conducting tenders, given prior and timely publication of an announcement on the land plots offered for lease, if there is only one bid.

A land plot is granted for construction **with preliminary approval of the location** of the structure in the following manner:

- 1) Selection of the land plot
- 2) Adoption of a resolution on preliminary approval of the location of the structure
- 3) Carrying out works for forming the land plot and executing its cadastral registration
- 4) Adoption of a resolution on granting the land plot for construction
- 5) Conclusion of a lease agreement for the land plot
- 6) State registration of the lease agreement for the land plot

Explanations of each aforementioned stage are provided below.

## **Selection of the land plot**

A land plot for construction is selected by state or local government bodies authorized to grant land plots on the basis of an interested party's application for selection of a land plot and preliminary approval of the location of the structure.

A land plot for construction is selected considering the city planning, ecological and other conditions for using it by way of carrying out procedures for approval of the possible alternatives for locating the structure by the respective state authorities, local government bodies and municipal organizations.

The selection of a land plot is documented by an act on selection of the land plot for construction.

## **Adoption of a resolution on preliminary approval of the location of the structure**

The state or local government body authorized to grant state or municipally owned land plots adopts a resolution on preliminary approval of the location of the structure, confirming the act on selection of the land plot pursuant to one of the alternatives for selecting a land plot, or on denial of the location of the structure.

The applicant is issued a copy of the resolution on preliminary approval of the location of the structure with an attached layout plan of the land plot on the cadastral plan or cadastral map of the respective area or a copy of the resolution on denial of the location of the structure.

The location of the structure is not subject to preliminary approval in the case of locating a structure in an urban or rural settlement in accordance with city planning documentation on development and the rules for land use and development (territory zoning) (see section 1.6.1 "City Planning Design, Zoning and Territory Planning"), as well as in the case of granting a land plot for agricultural production or forestry needs or to a citizen for individual residential construction or individual farming activities.

## **Carrying out works for forming the land plot and executing its cadastral registration**

The resolution on preliminary approval of the location of the structure serves as the basis for carrying out cadastral works concerning the land plot (including establishment of the borders of the land plot and preparation of its survey plan) and its state cadastral registration in the manner established by legislation of the Russian Federation (see section 1.4.2 "Cadastral and Technical Registrations (Inventory)"). The cadastral works and the cadastral registration are carried out at the expense of the party that applied for granting the land plot for construction.

## **Adoption of a resolution on granting the land plot for construction**

On the basis of the application from the party interested in the granting of the land plot for construction and the attached cadastral passport of the land plot, the executive state body or local government body authorized to grant land plots adopts a resolution on granting the land plot for construction.

## **Conclusion of a lease agreement for the land plot**

A lease agreement for the land plot is concluded by the local government body or executive state body authorized to grant the respective land plot (see section 1.3 "Subjects of Rights to Real Estate").

The general requirements for the form and contents of the agreement, described in section 1.5.3.1 of this brochure "Procedure for acquiring the lease right to a privately owned land plot," must also be observed in the case of concluding a lease agreement for a state or municipally owned land plot.

Upon completion of the construction the investor, being the owner of the constructed building, has the exclusive right to acquire the ownership of the respective land plot (see section 1.5.2.3 "Procedure for acquiring the title to a state or municipally owned land plot for non-construction purposes") or to execute a long-term lease agreement for the land plot for a term of up to 49 years.

## **State registration of the lease agreement for the land plot**

The state registration of the lease of the land plot is carried out by means of the state registration of the lease agreement for the real estate.

Lease agreements for land plots concluded for a term of at least one year are subject to state registration.

The state registration of the lease agreement for the land plot is carried out in the manner established by law (see section 1.4.3 "State Registration of Rights to Real Estate and Transactions Therewith". The state registration of the lease agreement is certified by a special registration inscription on the lease agreement for the land plot.

### **1.5.3.3 Features of Granting Land Plots for Residential Construction and Comprehensive Development for Residential Construction Purposes**

Land plots for residential construction are granted for ownership or lease from state or municipally owned land without preliminary approval of the location of the structure. Land plots for residential construction or rights to conclude lease agreements for land plots for residential construction are sold at auctions, with certain exceptions.

The comprehensive development of a land plot for residential construction purposes includes preparation of territory planning documentation, works for developing the area by means of constructing engineering infrastructure, residential and other construction.

Land plots are granted for lease for comprehensive development for residential construction purposes at auctions without preliminary approval of the location of the structure. The features of the procedure for conducting such an auction are stipulated by the Land Code of the Russian Federation.

The tenant of a land plot granted for comprehensive development for residential construction purposes, upon due approval of the territory planning documentation and state cadastral registration of the land plots intended for residential and other construction within the borders of a previously granted land plot, has the exclusive right to acquire the ownership of the said land plots or to lease them.

## **1.5.4 Procedure for Acquiring the Title to Buildings and Structures**

Buildings and structures (hereinafter referred to in this section as "Buildings") may be state owned, privately owned or owned by a municipality.

The procedure for acquiring the title to state or municipally owned buildings differs from the procedure for acquiring rights to privately owned buildings and structures. As in the case of acquiring rights to land plots, the main difference is that acquiring rights to state or municipally owned buildings requires compliance with a number of additional administrative procedures established by legislation of the Russian Federation concerning state and municipal property.

### **1.5.4.1 Procedure for acquiring the title to privately owned buildings**

Before a potential investor decides to acquire the ownership of a particular structure it is recommended that a legal analysis is conducted on the seller's rights to the structure. More detailed information on this issue is provided in section 3.2. of this brochure "Verifying Rights to Real Estate (Investment Objects) to be Acquired".

The process of acquiring the title to a privately owned building can be conditionally divided into the following main stages:

- 1) Conclusion of a sale and purchase agreement for the building
- 2) State registration of the buyer's title

Explanations of each aforementioned stage of acquiring the title to a privately owned building are provided below.

## **Conclusion of a sale and purchase agreement for the building**

A sale and purchase agreement for the building is concluded in writing by drawing up one document signed by the parties.

The sale and purchase agreement for the building must contain the material conditions stipulated by Russian Federation legislation (in the absence of which the agreement is deemed not concluded), which include, in particular:

- data that allow for definitively identifying the building transferred under the agreement, including data defining its location on the respective land plot or within the structure of other real estate
- the price of the building

The sale and purchase agreement must also meet other requirements for the execution and contents of a sale and purchase agreement stipulated by current legislation of the Russian Federation.

## **State registration of the buyer's title to the building**

The transfer of the title under the sale and purchase agreement for the building is subject to state registration. The title of the acquirer of the building accrues as of such state registration and is verified by a certificate of state registration of right.

The state registration of the buyer's title is carried out in the manner established by law (see section 1.4.3 "State registration of rights to real estate and transactions therewith").

### **1.5.4.2 Procedure for Acquiring the Title to State or Municipally Owned Buildings**

The title to a state or municipally owned building is acquired within the framework of the procedure for privatizing state or municipal property, i.e. compensated alienation of property owned by the Russian Federation, constituent territories of the Russian Federation, municipalities, to the ownership of individuals and legal entities.

In the case of acquiring a state or municipally owned building, within the context of a preliminary legal analysis it is necessary to identify the state or local government body that is authorized to dispose of the respective structure.

It should be noted that the process of delimiting state ownership, including buildings, into ownership of the Russian Federation, ownership of constituent territories of the Russian Federation and municipal ownership is to date still incomplete. State owner-

ship is delimited pursuant to specially established procedures. Information on structures owned by public civil entities is as a rule recorded in corresponding registers of federal, state and municipal property.

The procedure for acquiring the title to a state or municipally owned building can be conditionally divided into the following stages:

- 1) Adoption of a resolution on the conditions of privatizing the building and publication of an information announcement
- 2) Submission of an application for acquiring the building
- 3) Holding an auction for selling the building
- 4) Conclusion of a sale and purchase agreement for the building
- 5) State registration of the buyer's title to the building

Explanations of each stage are provided below.

#### **Adoption of a resolution on the conditions of privatizing the building and publication of an information announcement**

A resolution on privatizing the building is adopted by the authorized body of the owner. The resolution determines the name and other data that allow for individualizing the building or structure being privatized, the means of privatization, the price, the payment procedure, and other information required for carrying out the privatization.

At least 30 days prior to the sale of the building the authorized body of the owner of the building provides for the due publication of an information announcement on the sale of the building in mass media.

Apart from the information contained in the resolution on the conditions of privatizing the building, the information announcement contains information on the procedure and conditions for holding the auction, such as: the deadline for submitting applications for participating in the auction, the date, place and time of the auction, the manner of determining the winner and other information pursuant to legislation of the Russian Federation.

#### **Submission of an application for acquiring the building**

Both Russian and foreign individuals and legal entities, with the exception of legal entities in whose charter capitals the Russian Federation, a constituent territory of the Russian Federation or a municipality holds a share exceeding 25%, are entitled to submit an application for acquiring a state or municipally owned building.



In addition to the application, parties wishing to acquire the building must provide several other documents, the list of which is determined in accordance with regulatory acts of the owner of the property being privatized and the information announcement on sale of the building.

### **Holding an auction for selling the building**

In accordance with privatization legislation of the Russian Federation, state or municipally owned buildings are acquired by private parties at auctions. The procedure for organizing and holding an auction is established by the Provision on organizing a sale of state or municipal property at auction, approved by Decree of the Government of the Russian Federation dated August 12, 2002, No. 585.

The decision determining the winner of an auction is documented by a protocol on the outcome of the auction.

Upon the results of the auction the seller and the auction winner (buyer) conclude a sale and purchase agreement in accordance with legislation of the Russian Federation.

### **Conclusion of a sale and purchase agreement for the building**

A sale and purchase agreement for the building is concluded on behalf of the owner of the building or structure by the respective authorized body or institution.

A sale and purchase agreement for a state or municipally owned building must meet the requirements established by privatization legislation of the Russian Federation. In particular, an agreement must regulate a number of mandatory conditions, such as: information on the seller and the buyer, on the building or structure being acquired, its price, on the existence of encumbrances remaining upon transfer of the title, as well as other conditions established by legislation of the Russian Federation.

### **State registration of the buyer's title to the building**

The transfer of the title under the sale and purchase agreement for the building is subject to state registration. The title of the acquirer of the building or structure accrues as of such state registration and is verified by a certificate of state registration of right. The state registration of the buyer's title is carried out in the manner established by law (see section 1.4.3 "State Registration of Rights to Real Estate and Transactions Therewith").

#### **1.5.4.3 Procedure for Acquiring the Title to a Building as a Result of Construction**

A particular feature of acquiring rights to a building, as compared to land, is that the title may be acquired either from the previous owner (most often on the basis of an agreement) or by constructing a new building.

A new building can be created either by constructing the real estate from the ground up or by reconstructing an existing structure.

The main stages of acquiring rights to a newly created building are as follows:

- Conducting engineering surveys and collecting initial data
- Development and state expert evaluation of the design documentation
- Obtaining a construction permit
- Carrying out the construction
- Obtaining a permit to commission the structure
- Technical and cadastral registrations
- Registration of the title to the constructed structure

More detailed information on the separate stages of construction is provided in section 1.6 "Legal Regulation of Construction Activities".

## **1.5.5 Procedure for Acquiring the Lease Rights to a Building**

### **1.5.5.1 Procedure for Acquiring the Lease Rights to a Privately Owned Building**

The process of acquiring the lease rights to a privately owned building can be conditionally divided into the following main stages:

- 1) Conclusion of a lease agreement for the building
- 2) State registration of the lease agreement for the building

Explanations of each abovementioned stage of acquiring the lease rights to a privately owned building are provided below.

#### **Conclusion of a lease agreement for the building**

A lease agreement for the building is concluded in writing by drawing up one document signed by the parties.

The lease agreement must contain data that allow for definitively identifying the building or structure to be transferred to the tenant as well as stipulate the amount of

the rent. Since these conditions are material, in the absence of any of them the lease agreement for the building is deemed not concluded. The lease agreement for the building must also meet other requirements for the execution and contents of a lease agreement stipulated by current legislation of the Russian Federation.

Additional information on certain conditions of lease agreements that should be given particular attention is presented in section 3.6.10 "Lease Agreement and Preliminary Agreements".

### **State registration of the lease agreement for the building**

The state registration of the lease of the building or structure is carried out by means of the state registration of the agreement.

Lease agreements for buildings concluded for a term of at least one year are subject to state registration. Such lease agreements for buildings or structures are only deemed concluded as of their state registration.

The state registration of the lease agreement for the building is carried out in the manner established by law (see section 1.4.3 "State registration of rights to real estate and transactions therewith"). The state registration of the lease agreement is certified by a special registration inscription on the lease agreement for the building.

#### **1.5.5.2 Procedure for Acquiring the Lease Rights to a State or Municipally Owned Building**

The procedure for acquiring the lease rights to a state or municipally owned building differs from the procedure for acquiring the lease rights to a privately owned building in the necessity to undergo several administrative procedures connected with authorized state or local government bodies adopting resolutions on granting the building for lease. In this regard, it is primarily necessary to determine the body authorized to dispose of the given real estate.

The procedure for granting a state or municipally owned building for lease is governed by regulatory acts of the state or local government body authorized to dispose of the respective real estate. Such regulatory acts may establish any additional stages of acquiring the lease rights to a building or structure. Thus, for example, nonresidential premises may be transferred for lease on the basis of the results of tenders.

Unless special conditions are established for acquiring the lease rights to a state or municipally owned building or structure, the process of acquiring the lease rights to a state or municipally owned building can be conditionally divided into the following main stages:

- 1) Submission of an application for acquiring the lease rights to the building
- 2) Conclusion of a lease agreement for the building
- 3) State registration of the lease agreement for the building

Explanations of each abovementioned stage are provided below.

### **Submission of an application for acquiring the lease rights to the building**

In order to acquire the lease rights to the building an interested party applies to the state or local government body authorized to dispose of the respective real estate.

The decision to grant the building for lease is documented by a corresponding resolution of the authorized state or local government body.

### **Conclusion of a lease agreement for the building**

A lease agreement for the building is concluded in writing by drawing up one document signed by the parties.

The main requirements of current legislation of the Russian Federation stipulated for a lease agreement for a state or municipally owned building correspond to the requirements stipulated for lease agreements for privately owned buildings and structures (see section 1.5.5.1 "Procedure for acquiring the lease rights to a privately owned building").

A lease agreement for a state or municipally owned building or structure may stipulate conditions on the particular designated use of the leased building.

### **State registration of the lease agreement for the building**

The state registration of the lease of the building is carried out by means of the state registration of the lease agreement for the building.

Lease agreements for buildings concluded for terms of no less than one year are subject to state registration. Such lease agreements for buildings or structures are only deemed concluded as of their state registration.

The state registration of a lease agreement for a building is carried out in the manner established by law (see section 1.4.3 "State registration of rights to real estate and transactions therewith"). The state registration of a lease agreement is certified by a special registration inscription on the lease agreement for the building.

### **1.5.6 Acquiring Rights to a Land Plot when Acquiring Rights to a Building Located Thereon**

Buildings, constructions and structures are inseparably attached to land plots (see section 1.2.2.2.5 of this brochure “Interdependence Between Titles to Land Plots and Titles to Real Estate Objects Located Thereon”). Therefore, with the exception of cases established by law, it is not permitted to acquire a building without acquiring rights to the land plot.

It should be noted that in Russia it is possible that an owner of a building is not the owner of the land plot on which the building is located, but rather has, for example, the right to lease it. For instance, such a situation may occur as a result of privatization of state property or as a result of constructing a new building on a leased land plot. Consequently, the legislator distinguishes cases where:

- The owner of the building (i.e. the seller or landlord) is simultaneously the owner of the land plot
- The owner of the land plot and the owner of the building are different parties

Each of these situations is reviewed in greater detail below.

#### **1.5.6.1 Acquiring Rights to a Land Plot Owned by the Owner of a Building Located Thereon**

In accordance with land legislation, if a building and the land plot thereunder are owned by one and the same party, such building is alienated together with the land plot.

There are two exceptions to this rule:

- 1) Alienation of a part of a building that may not be specifically separated together with a part of the land plot
- 2) Alienation of a building, construction or structure located on a land plot barred from turnover

A building located on a land plot restricted in turnover is alienated together with the plot if law permits such land plot to be granted for private ownership.

#### **1.5.6.2 Acquiring Rights to a Land Plot Owned by a Third Party**

For cases of acquiring a building from a party that does not own the land plot located thereunder, land legislation establishes a general rule: the acquirer of a building acquires the right to use the corresponding part of the land plot that is occupied by the

building and required for using it on the same conditions and to the same extent as that of the previous owner (for example, lease rights).

## **1.6 Legal Regulation of Construction Activities**

Issues of city planning design of a territory, design and construction of real estate are regulated by legislation on city planning activities, primarily the City Planning Code of the Russian Federation.

The City Planning Code of the Russian Federation also regulates the reconstruction of real estate, i.e. changing the parameters thereof (height, stories, area, capacity figures) and the quality of engineering facilities, as well as capital repairs during which structural and other reliability and safety characteristics of the real estate are affected.

### **1.6.1 City Planning Design, Zoning and Territory Planning**

An important factor when choosing a land plot for construction is knowing which buildings of a particular designation (residential or nonresidential, production or office) and with certain parameters (for example, stories, area within the borders of the land plot) may be constructed on the given land.

Issues of locating and constructing real estate in the Russian Federation at a general level, as well as in constituent territories of the Russian Federation, municipalities, neighborhoods, communities and separate land plots are regulated by the City Planning Code of the Russian Federation within the framework of institutions of territorial planning, city planning zoning and territory planning.

**Territory planning** focuses on determining the designation of a territory based on the aggregate social, economic, ecological and other factors for the purposes of ensuring stable development of the territory, its engineering, transportation and social infrastructure, as well as ensuring consideration of public interests.

The City Planning Code of the Russian Federation provides for developing the following types of territory planning documents:

- Scheme of territory planning of the Russian Federation. The respective documents are currently at the development stage. The provision on the procedure for preparing and coordinating the draft scheme of territory planning of the Russian Federation is approved by Decree of the Government of the Russian Federation dated March 23, 2008, No. 198.
- Schemes of territory planning of the constituent territories of the Russian Federation. The documents of territory planning of the constituent territories of the

Russian Federation, the cities of federal significance, Moscow and St. Petersburg, are general plans.

- Documents of territory planning of municipalities (general plans of settlements, urban districts, schemes of territory planning of municipal districts).

In relation to municipal territories, for the purposes of determining territorial zones and establishing city planning regulations, **city planning zoning** is carried out.

The main document of city planning zoning is the **rules of land use and development**, which establishes territorial zones determining the designation of objects located therein (for example, residential, public-business, production), and city planning regulations.

**City planning regulations** determine the types of permitted use of land plots, the maximum sizes of land plots and limit the permitted construction parameters of buildings (such as the minimum spaces from the borders of land plots when locating buildings, the maximum number of stories and height, etc.), as well as restrictions on use of land plots and real estate located thereon.

City planning regulations do not apply to several categories of land plots (for example, within the borders of historical and cultural monuments, public use areas). Moreover, city planning regulations are not established for certain land (for example, agricultural land).

For the purposes of emphasizing elements of a planning structure (neighborhoods, communities, other elements) and establishing borders of land plots that are developed or intended for construction, **territory planning documentation** is prepared. Territory planning documentation includes:

- Territory planning drafts
- Territory surveying drafts
- City planning designs of land plots

**A city planning design of a land plot** is a document required for obtaining a construction permit for the given plot. The city planning design of a land plot indicates, in particular, the minimum allowed space from the borders of the land plot for the purposes of determining the permitted places for locating a building, information on the city planning regulation (if applicable to the given plot), information on the types of permitted use of the land plot, and information on technical conditions connected to engineering networks (for more detailed information on technical conditions see section 1.6.4. "Development of design documentation").

Currently the frameworks of the documents of territory planning, city planning zoning and territory planning are at the stage of formation, due to which legislation has established several transitional provisions. In particular, it is stipulated that from January 1, 2010, a mandatory condition for issuing construction permits for land plots located within the borders of a respective municipality will be the existence of approved rules of land use and development.

Furthermore, from January 1, 2010, it will be possible, with certain exceptions, to prepare territory planning documentation only given the existence of territorial planning documents.

### **1.6.2 Development of Built-up Areas**

For the purposes of developing already built-up city neighborhoods and communities, legislation of the Russian Federation provides for the possibility for a developer and a local government authority (in Moscow and St. Petersburg a state authority) to conclude an agreement on developing a built-up area. Such agreements are concluded at open auctions concerning areas having apartment buildings that are hazardous or subject to demolition or reconstruction.

Within the framework of the said agreement the developer prepares a draft plan of the respective area and develops it. Moreover, the developer is obligated to pay the cost of the real estate eliminated from the given area in order to further develop it, as well as transfer a portion of the constructed residential premises to municipal (state) ownership.

Local government authorities (state authorities) in turn assume obligations to approve the developer's draft territory plan and take a decision on eliminating residential premises in apartment buildings and land plots located in the built-up area subject to further development by the developer.

The developer is granted land plots located in the respective area and which are state or municipally owned for the purpose of construction without auctions being held.

### **1.6.3 Licensing Construction Activities and Transitioning to Self-regulation**

Since design and construction activities are potentially associated with the risk of causing damage to a large range of people, additional legislative regulation is carried out in relation to the said activities.

Prior to January 1, 2009, the following types of activities could be carried out only given the existence of special permits and licenses:



- Designing buildings and constructions of certain categories
- Constructing buildings and constructions of certain categories
- Conducting engineering surveys for constructing buildings and constructions of certain categories

If a company placed an order for the performance of the said licensable activities, then such company's functions were also subject to licensing.

Licensing of the said types of construction activities was performed by the Federal State Institution "Federal Licensing Center", specifically created within the Federal Agency for Construction and the Housing-Utilities Complex<sup>1</sup> (hereinafter, "Rosstroy"), given the applicant's mandatory observance of the licensing requirements and the conditions stipulated by Decree of the Government of the Russian Federation dated March 21, 2002, No. 174.

Foreign legal entities were entitled to obtain licenses for performing construction activities on the same conditions and grounds as Russian legal entities. However, in practice a foreign legal entity could obtain a license only given the existence of a branch or representative office accredited in the Russian Federation.

In order to obtain a license it was necessary to file an application with the Federal Licensing Center of Rosstroy and submit documents verifying the applicant's compliance with the licensing requirements and conditions. A license was issued for a five-year term unless a shorter term was indicated in the applicant's application.

Within the framework of general state policy on reducing the number of licensed types of activities and creating a more effective mechanism for ensuring construction safety, the Federal Law dated July 22, 2008, No. 148-FZ (hereinafter, the "**Law**") amended several legislative acts in connection with the planned replacement of the institution for licensing construction activities by a **self-regulating** institution.

The adopted amendments provide for compiling a **list of works that affect the safety of capital construction structures** and whose performance is possible only given the existence of a respective competency certificate for such works. The list of the types of works that affect the safety of capital construction structures and for which a competency certificate must be obtained is approved by Order of the Ministry of Regional Development of the Russian Federation dated December 9, 2008, No. 274.

<sup>1</sup> In accordance with Order of the President of the Russian Federation dated May 12, 2008, No. 724, the Federal Agency for Construction and the Housing-Utilities Complex (Rosstroy) was abolished. The functions and authorities of Rosstroy have been transferred to the Ministry of Regional Development of the Russian Federation (Minregion of Russia).

Competency certificates will be issued by special self-regulating organizations in the construction sector, making it necessary for parties wishing to perform the said works to join one of the self-regulating organizations. Moreover, the Law establishes the subsidiary liability of self-regulating organizations for its members' obligations arising due to harm caused, to the extent of the compensation fund established specifically for these purposes.

The Law provides for the creation of three types of self-regulating organizations, thus uniting parties that:

- Conduct engineering surveys
- Prepare design documentation
- Perform construction

For each type of self-regulating organization, special requirements are established as regards the minimum number of members of the organization and the minimum amount of the compensation fund.

Each self-regulating organization is obligated to develop and approve requirements for the issuance of competency certificates for works affecting the safety of capital construction structures. A competency certificate is issued by a self-regulating organization without charging a fee and without a limitation on the term and territory of its validity.

A self-regulating organization may accept legal entities as members (including foreign legal entities) that meet the requirements for the issuance of a competency certificate for one or several types of works. A self-regulating organization must maintain a register of its members, which is subject to publication on the organization's website and must contain, among other things, a list of the types of works for which a competency certificate is held by each member of the self-regulating organization, as well as information on issued competency certificates.

The cancellation of licensing in the construction sector should take place on January 1, 2010. During the period from January 1, 2009, to January 1, 2010, performance of the respective types of works is permitted, at the executor's choice, on the basis of: a) a license; or b) a competency certificate. Moreover, the granting of new licenses ceased as of January 1, 2009.

#### **1.6.4 Development of Design Documentation**

Design documentation is text materials in the form of maps (schemes) and determines the architectural, functional and technical, structural and engineering and technical solutions required for construction.

Design documentation is prepared on the basis of an assignment of the client, engineering survey results, the city planning design of the land plot in accordance with the requirements of technical regulations, technical conditions and other documents (for more detailed information on an agreement on developing design documentation see section 3.6.6. "Agreement for general design").

Design documentation is prepared by specialized (design) organizations having the proper license / competency certificate (concerning the issue of licensing reforms see section 1.6.3 "Licensing construction activities and transitioning to self-regulation").

The main steps of preparing design documentation are:

- Preparation of the city planning design of the land plot, the technical conditions for connecting the object to engineering networks, as well as other required initial documentation
- Direct development of the design documentation
- Conducting of a state expert evaluation of the design documentation

**Technical conditions** for connecting capital construction structures to engineering networks, as well as information on the connection fee, are provided by the organizations operating such networks, without a fee being charged, at the request of local government authorities or rightholders of the land plots.

- The technical conditions for connecting capital construction structures to engineering networks provide for:
- The maximum capacity
- The connection terms
- The validity of the technical conditions (not less than two years)

Design documentation is prepared on the basis of **engineering survey** results. An assignment on conducting engineering surveys may be included into an agreement on developing design documentation. The provision on conducting engineering surveys for preparing design documentation, construction, reconstruction, capital repairs of capital construction structures is approved by Decree of the Government of the Russian Federation dated January 19, 2006, No. 20.

The contents of design documentation depend on the type of planned construction works. Design documentation for capital construction structures includes the following main sections:

- Explanatory notes with initial data
- Planning scheme of the land plot
- Architectural solutions
- Structural and spatial planning solutions
- Engineering and technical measures, contents of technical solutions
- Construction organization plan
- Plan of organization of demolition or dismantling works
- Environmental protection measures
- Fire safety measures

Design documentation for capital construction structures and engineering survey results are subject to a **state expert evaluation**, with the exception of cases established by the City Planning Code of the Russian Federation. The procedure for conducting a state expert evaluation of design documentation is established by the Provision on organizing and conducting a state expert evaluation of design documentation and engineering survey results, approved by Decree of the Government of the Russian Federation dated March 5, 2007, No. 145.

Conducting other state expert evaluations of design documentation is not permitted, with the exception of state ecological expert evaluations of design documentation for a number of structures, particularly structures constructed on land of specially protected nature areas.

### 1.6.5 Construction Permit

In order to construct, reconstruct or perform capital repairs on a building, if it affects structural or other characteristics of its reliability and safety, a construction permit is required. A construction permit is not required when constructing structures that are not capital construction structures (for example, kiosks, sheds, other temporary structures) or which are auxiliary use structures.

A construction permit confirms the compliance of the design documentation with city planning requirements for using the land plot and provides for the right to perform construction, reconstruction or capital repairs of structures.

A construction permit is issued to a developer on the basis of the documents determined by the City Planning Code of the Russian Federation, for the term provided for by the construction organization plan.

It is prohibited to perform construction activities without a permit. Legislation stipulates liability for construction without a permit in the form of an administrative fine for legal entities in an amount from 500,000 to 1,000,000 rubles or suspension of activities for up to 90 days.

## **1.6.6 Control and Supervision at the Construction Stage**

### **Construction control**

In accordance with provisions of the City Planning Code of the Russian Federation, construction control is mandatory and is conducted by the developer and the contractor in order to verify that performed works comply with:

- The design documentation
- The requirements of technical regulations
- The results of engineering surveys
- The requirements of the city planning design of the land plot

For the purposes of exercising control and supervision over the construction and taking decisions on its behalf in mutual relations with the contractor, the client (developer) may conclude an agreement on rendering the client corresponding services with an engineer (engineering organization).

### **Designer supervision**

The necessity to conduct designer supervision pertains to the client's authorities and is generally established in the assignment for designing the structure (see section 3.6.6. "Agreement for general design"). In a number of cases established by law conducting designer supervision is mandatory.

Moreover, the author of architectural work (architect) has the right to conduct designer control over the development of construction documentation and the right of designer supervision over the construction of the building. Without the designer's consent his/her work may not be amended or supplemented (right of integrity of a work).

### **State construction supervision**

State construction supervision is conducted by an authorized state body. State construction supervision verifies:

- That works performed and construction materials used comply with the requirements of technical regulations and the design documentation
- The existence of a construction permit
- That the parties performing the construction have the required licenses or competency certificates for the works

The officials conducting state construction supervision are entitled to unhindered access to the structures under construction. Upon the results of conducting the verification, the state construction supervision authority draws up an act that serves as the basis for issuing the party performing the construction with instructions for rectifying identified violations.

### **1.6.7 Permit to Commission a Constructed Structure**

The commissioning of a structure confirms the completion of the construction in full in accordance with the construction permit, the city planning and design documentation.

In order to commission a structure the developer applies to the authorized state body that issued the construction permit, the existence and correctness of the required documents are verified, and the capital construction structure is inspected, after which the applicant is issued a permit to commission the structure.

On the basis of the said permit the structure undergoes state registration, as does the investor's title to the constructed structure (see sections 1.4.2 "Cadastral and Technical Registrations (Inventory)" and 1.4.3 "State Registration of Rights to Real Estate and Transactions").

## **1.7 Land Payments**

### **1.7.1 Value of a land plot during acquisition**

The procedure for determining a land plot's value during acquisition of the title to it varies depending on whether the plot is owned by a private person, the state or a municipality.

When acquiring a land plot from a private owner, the land plot's value is determined by the parties' agreement and is fixed in the land plot sale and purchase agreement.

When acquiring a state owned or municipally owned land plot, the procedure for determining the land plot's value has particularities that have been established by legal

acts of the Russian Federation, constituent territories of the Russian Federation, or municipalities.

State and municipally owned land plots are generally granted at auctions (see section 1.5.2.2 "Procedure for Acquiring Ownership Rights to State or Municipally Owned Land Plots"). In such case, the starting price of a land plot is determined on the basis of a report by an independent appraiser. A land plot is sold for the largest price offered for the land plot during bidding.

The procedure for determining the price for selling state and municipally owned land plots to owners of buildings, structures or constructions located on such land plots (see section 1.5.2.3 "Procedure for Acquiring the Title to a State or Municipally Owned Land Plot for Non-construction Purposes") is regulated in a special manner. Until January 1, 2010, the sales price of the said land plots is determined as follows:

- The price of land plots occupied by buildings, structures and constructions previously acquired from the state or a municipality is established by the constituent territories of the Russian Federation within up to 20% of the cadastral value of the land plots in cities with a population exceeding 3 million people and up to 2.5% of the cadastral value in other locations. If a constituent territory of the Russian Federation has not established a particular amount of the price of a land plot, the largest land plot price for the respective location shall apply.
- In other cases the value of land plots when sold to owners of buildings, structures and constructions located thereon is determined by the constituent territory of the Russian Federation by establishing a particular coefficient in an amount of from 3 to 30, applicable to the land tax rate, in relation to the bought-out land plots (see section 1.7.2.1 "Land Tax"). If a constituent territory of the Russian Federation has not determined the particular amount of the coefficient, the minimum land tax rate per unit of area of the land plot shall apply.

As of January 1, 2010, the said rules for determining the buyout value of land plots will be replaced by a general rule under which the sales price of such land plots will be determined by executive state authorities of the constituent territories of the Russian Federation and local government authorities within limits not exceeding the cadastral value of the respective land plots.

## **1.7.2 Payment for Land Plot Use**

One of the main principles of Russian Federation land legislation is that use of land is subject to payment. According to this principle, any use of land is subject to a fee, with the exception of certain cases established by Russian Federation legislation.

Land use payments are in the form of the land tax and lease payments. The land tax is payable by owners of land plots and persons having rights of permanent (perpetual) use or lifetime ownership with hereditary succession of the land plots. Persons using land plots on the basis of lease rights and rights of free terminable use are not charged land tax.

### 1.7.2.1 Land Tax

In accordance with the Russian Federation Tax Code, the land tax is considered a local tax. This means that the land tax is generally regulated by the Russian Federation Tax Code and regulatory acts of representative bodies of municipalities, and in the cities of federal importance, Moscow and St. Petersburg – by laws of the respective Russian Federation constituent territories. The land tax becomes effective on the territory of certain municipalities on the basis of regulatory legal acts of representative bodies of the municipalities, and in the cities of federal importance, Moscow and St. Petersburg – on the basis of laws of these Russian Federation constituent territories.

The Russian Federation Tax Code determines the general provisions on the land tax, which cannot be changed at the local level, in particular the:

- Taxpayers
- Taxation object
- Tax base
- Maximum tax rate
- Tax concessions
- Procedure for tax calculation

The tax base is determined as the cadastre value of a land plot calculated in accordance with Russian Federation land legislation. Tax rates may not exceed:

- 0.3% of the cadastre value of land plots – for agricultural land, land occupied by housing and engineering infrastructure objects of the housing and utility complex, as well as land provided for personal households
- 1.5% of the cadastre value of land plots – for other categories of land

It should be taken into consideration that, according to Russian Federation land legislation, if the cadastre value of land is not determined, its normative price should be applied as determined in accordance with the Decree of the Russian Federation



Government "On the Procedure for Determination of the Normative Price of Land," No. 319 dated March 15, 1997.

Inter alia, religious organizations are exempt from the land tax on land plots on which buildings of religious and charitable designations are located, as well as all-Russia public organizations of the disabled, on land plots used for their authorized activities.

#### **1.7.2.2 Rent**

When acquiring the right to lease a land plot, the procedure for determining the rent amount varies depending on the lessor's type of title (state, municipal or private).

When leasing a land plot from a private owner, the rent amount is determined by the agreement between the lessor and the lessee.

When leasing a state or municipally owned land plot, the rent amount is also determined by the agreement between the lessor and the lessee. However, in such case the lessor is a respective authority acting within the framework of its powers, and the procedure for determining the rent amount may be governed by special legal acts. Pursuant to Russian Federation legislation, the Russian Federation Government may establish common bases for determining rent amounts for state or municipally owned land plots. The procedure for determining rent amounts for land plots owned by the Russian Federation, a constituent territory of the Russian Federation or a municipality is established by a competent authority of the owner: the Russian Federation Government, state authorities of the constituent territory of the Russian Federation or local government authorities, respectively.

Concerning land plots whose state ownership is not delimited into Russian Federation ownership, ownership of constituent territory of the Russian Federation and municipal ownership, the procedure for determining the rent amount, conditions and terms for paying it are established by state authorities of the respective constituent territory of the Russian Federation.

## 2. Particularities of Regional Legislation

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### 2.1 Particularities of investing in real estate in Moscow

This section reviews the main features of investment activities pertaining to state owned real estate located in Moscow.

#### 2.1.1 Legal basis

The main provisions concerning acquiring rights to land plots and investing in real estate in Moscow are established by the following laws and other regulatory legal acts of the city of Moscow:

- Law of the city of Moscow "On Land Use in the City of Moscow" dated December 19, 2007, No. 48 (hereinafter, "**Law of the City of Moscow No. 48**")
- Law of the city of Moscow "City Planning Code of the City of Moscow" dated June 25, 2008, No. 28
- Decree of the Government of Moscow "On Transferring Land Plots on the Territory of the City of Moscow to Private Ownership" dated June 27, 2006, No. 431-PP (as amended; hereinafter, "**Decree No. 431-PP**")
- Decree of the Government of Moscow "On Further Development of the System of Preparing and Conducting Auctions during the Implementation of Investment Projects in the Area of Capital Construction on the Territory of the City of Moscow" dated May 20, 2008, No. 417-PP (hereinafter, "**Decree No. 417-PP**")
- Decree of the Government of Moscow "On Amending the Procedure for Adopting Resolutions on Granting Land Plots and Introducing Amendments into Legal Acts of the Government of Moscow on Forming and Granting Land Plots and Land Rent" dated January 27, 2009, No. 46-PP
- Decree of the Government of Moscow "On the Procedure for Considering Applications for Amending Lease Agreements for Land Plots and Investment Contracts (Agreements) Providing for Construction (Reconstruction) of City Planning Structures or on Terminating Them" dated March 27, 2007, No. 196-PP
- Decree of the Government of Moscow "On the Procedure for Holding Tenders and Auctions for Selecting Investors to Implement Investment Projects" dated April 27, 2004, No. 255-PP (as amended)

## **2.1.2 Objects and legal forms of investment activities**

In accordance with legislation of the city of Moscow, the main objects of investment activities are:

- Land plots for new construction
- Buildings and structures subject to reconstruction (restoration), capital repairs
- Built-up areas subject to city planning development
- City transportation, utilities and other infrastructure

The legal form (agreement type) in which investments are made in real estate depends on the source of financing. Thus, reconstructing real estate owned by the city of Moscow using city budget funds may be carried out within the framework of placing a competitive order for performing works for state needs, with transfer of the land plot for gratuitous fixed-term use for the period of reconstruction to the party with which the state contract is concluded.

In the case of implementing investment projects in the area of capital construction in the city of Moscow which are carried out using funds of private investors on state owned land plots, tenders are prepared and conducted, including in the following forms:

- Auctions for the right to conclude a lease agreement for a land plot for capital construction
- Auctions for the right to conclude an agreement on developing a built-up area
- Competitions for the right to conclude a concession agreement

The basis for preparing and implementing a particular investment project at a tender is the Unified Address List of City Planning Structures on the Territory of the City of Moscow, approved by the Government of Moscow.

## **2.1.3 General conditions for acquiring rights to land plots for investment purposes in the city of Moscow**

### **2.1.3.1 Priority of lease relations**

An obligatory condition for legal entities and individuals to construct and reconstruct city planning structures in the city of Moscow is that rights be held to the land plot intended for these purposes.

The granting of rights to land plots in Moscow to investors is regulated by Law of the City of Moscow No. 48. In accordance with this Law, land plots are granted to citizens and legal entities only for lease, aside from cases where federal laws establish the obligation of transferring land plots owned by the city of Moscow, or land plots whose state ownership is not delimited, to private ownership.

### **2.1.3.2 City planning structures of the city and district levels**

For the purposes of conducting tenders for implementing investment projects, all city planning structures (buildings, constructions) in the city of Moscow pertain to one of two levels: the city level or the district level.

Structures of the district level are recognized as structures of an area of no more than 1,500 square meters, not having an outlet to thoroughfares of municipal significance and located outside nature reserves. Other located city planning structures are of the city level.

Concerning structures of the city level, the Department for Competition Policy of the City of Moscow (hereinafter, the "DCP") acts as the organizer of tenders, whereas concerning structures of the district level, prefectures of the respective administrative districts of the city of Moscow organize tenders. In Moscow there are district commissions and a city commission for reviewing issues of preparing documentation for tenders, the work of which is organized by the DCP and prefectures, respectively.

### **2.1.3.3 Investor financed construction of engineering infrastructure**

In accordance with Decree No. 417-PP, during preparation of the starting conditions for conducting tenders, empowered authorities of the city of Moscow stipulate obligations on the investor financing, if necessary, the full scope of works for designing and constructing engineering networks, structures and utilities, particularly of city importance, including the street and road network, using its own and raised funds, with the said objects being transferred to Moscow's ownership without subsequent compensation from the city budget.

## **2.1.4 Lease of land plots**

### **2.1.4.1 General provisions**

#### **Procedure for acquiring lease rights**

Rights to conclude a lease agreement for a land plot are acquired in two ways:

- 1) At tenders, held in the form of competitions or auctions<sup>2</sup>
- 2) Without conducting tenders in cases provided for by law. In particular, land plots are granted for lease to owners of capital construction structures located on the land plots without conducting tenders (see also section 1.5.3.4 of the brochure)

For the purposes of preparing investment tenders, the city of Moscow, using city budget funds, repeatedly develops city planning documentation pertaining to land plots put up for tender.

Only land plots that are free of rights of third parties (for example, land plot tenants, owners of buildings and premises) may be put up for tender.

Lease agreements for land plots that provide for constructing and operating city planning structures are concluded on behalf of the city of Moscow by the Department of Land Resources of the City of Moscow (hereinafter, the "DLR").

### **Term of a lease agreement**

The term of a lease agreement for a land plot is determined by agreement of the parties with dependence upon the actual use, encumbrances and restrictions on use of the land plot, as well as in accordance with the General Plan of the City of Moscow.

Law of the City of Moscow No. 48 establishes the following term limits for lease agreements for land plots:

- Not more than 5 years – concerning land plots for locating structures and constructions that are not capital construction structures
- Not more than 1 year – concerning land plots within the borders of common use land
- Not less than 25 and not more than 49 years – concerning land plots occupied by capital construction structures. At the same time, a shorter term may be established by agreement of the parties
- A term not exceeding the reservation term – concerning land plots within the borders of land reserved for state needs of the city of Moscow

<sup>2</sup> This provision is contained in Law of the City of Moscow No. 48. At the same time, Decree No. 417-PP only provides for the possibility of conducting tenders in the form of an auction for the right to conclude a lease agreement for a land plot for the purpose of construction. In accordance with federal legislation, formed land plots shall be sold only at auctions.

- The term for carrying out repair and construction works, but not more than 5 years concerning land plots within the borders of common use land occupied by thoroughfares, streets, squares, lanes, roads, embankments, coastline, walkways, granted for lease exclusively for maintaining repair and construction works without the right to construct real estate structures on the said plots

### **Fee for the right to conclude a lease agreement for a land plot**

For the right to conclude lease agreements for land plots owned by the city of Moscow and land plots whose state ownership is not delimited a fee is charged on conditions determined by the Government of Moscow.

The market value of the right to conclude a lease agreement for a land plot is subject to assessment by an independent appraiser and is confirmed by the order document of the Government of Moscow on granting the land plot. If the value of the right to conclude a lease agreement for a land plot is a criterion for determining the winner of a tender, then the final value of the right is determined upon the results of the tender. The said fee is paid prior to the conclusion of the lease agreement for the land plot. However, if the conditions of the tender stipulate payment in installments, the fee is paid according to the fee schedule attached to the lease agreement.

A fee for the right to conclude a lease agreement for a land plot is not charged in the cases stipulated by Law of the City of Moscow No. 48, in particular:

- In case of transfer for lease of a land plot to the owner of buildings, structures or constructions located thereon
- In case of prolongation of the term of a lease agreement (conclusion of a lease agreement for a new term) for a land plot if upon expiry of the term of the agreement tenders are not conducted for selling the right to conclude a lease agreement for the respective plot or such tenders did not take place
- In case of transfer for lease of a land plot to the tenant of buildings, structures or constructions located thereon that are state owned by the city of Moscow
- In case of transfer for lease of a land plot on the basis of a concession agreement

If the resolution on granting a land plot for lease provides for payment of a fee for the right to conclude the lease agreement, then the respective lease agreement for the land plot is supplemented with a provision pursuant to which the tenant acquires the right to conduct transactions with the right to lease the land plot given payment of the fee for the right to conclude the lease agreement in full.

## Rent

In accordance with Law of the City of Moscow No. 48, the procedure for determining the amount of the rent for land plots owned by the city of Moscow and for land plots whose state ownership is not delimited, as well as the procedure, conditions and terms for paying the rent for using such land plots, are established by the Government of Moscow. The aforementioned issues are regulated by the Decree of the Government of Moscow "On Developing the Procedure for Establishing Rent Rates for Land in the City of Moscow" dated April 25, 2006, No. 273-PP (as amended).

When determining a rent amount, consideration is given to the permitted use of the land plots, the types of business and other operations conducted thereon, as well as additional conditions for using the land plots established for resolving social tasks and tasks for city development. The amount of the annual rent for a land plot is established as a percentage of its cadastral value. The amount of the annual rent for a land plot for which the right to conclude a lease agreement was acquired at a tender is established upon the results of the tender if the amount of the annual rent rate was a criterion for determining the winner of the tender.

Rent is paid by a tenant quarterly in equal portions, no later than the fifth of the first month of the quarter, unless the lease agreement stipulates otherwise. In particular, in the case of concluding a lease agreement for a land plot at a tender, the procedure, conditions and terms for paying rent may be determined upon the results of the tender if the amount of the annual rent was a criterion for determining the winner of the tender.

The obligation to pay rent commences for the tenant on the date following the day of state registration of the lease agreement for the land plot, or, if the lease agreement is concluded for a term of less than one year and is not subject to state registration, on the date following the day it is signed by the parties.

Unless the agreement stipulates otherwise, for each day of delay in performing the obligation to pay rent the tenant shall pay a penalty of 1/300 of the refinancing rate of the Central Bank of the Russian Federation, valid on the date the penalty is paid, applied to the outstanding amount of rent (as of preparing this version of the brochure the refinancing rate equals 12.5% per annum).

### **2.1.4.2 Lease agreement for a land plot for constructing nonresidential property**

#### **Form of and procedure for concluding an agreement**

A lease agreement for a land plot for the capital construction of nonresidential property is concluded by the DLR with the winner of an auction for the right to conclude a lease agreement for the land plot.

The criterion for determining the winner of an auction may be the amount of the fee for the right to conclude a lease agreement or the rent amount.

The model form of a lease agreement for a land plot for the capital construction of nonresidential property was approved by Decree No. 417-PP (Annex 3).

### **Subject of the agreement**

Under a lease agreement the investor is, for a fee, granted a land plot for constructing nonresidential real estate according to the characteristics stipulated by the agreement (total area, height, number of stories, parking requirements, and other parameters). Land plots granted for lease shall be free of any types of real estate. If necessary, buildings and structures existing on the land plot are demolished at the expense of the city budget prior to an auction being held for the right to conclude a lease agreement.

### **Terms under an agreement**

A lease agreement is concluded for the term required for constructing the real estate on the land plot, which, however, may not exceed 4 years 11 months and 28 days from the date the parties signed the lease agreement.

A lease agreement also establishes the terms and scope of the stages of implementation of the investment project:

- **First stage** – the tenant develops, coordinates and confirms the design documentation and obtains a construction permit. The first stage may not last longer than 6 months from the date of state registration of the lease agreement.
- **Second stage** – the real estate is constructed and commissioned and the tenant's title to the constructed property undergoes state registration. The second stage must be completed by the expiry of the term of the lease agreement.

### **Main obligations of the tenant**

Within the term of the agreement the tenant is obligated to take the following actions associated with implementing the investment project:

- Prepare the architectural and construction design, obtain a construction permit, construct and commission the real estate, with execution of the title thereto within the terms stipulated by the lease agreement

If the tenant fails to meet the deadlines for implementing the investment project, the landlord is entitled to claim for premature termination of the lease agreement



and for recovering a forfeiture in the amount of 5% (or 10% if the land plot is located within the borders of the Central Administrative District of the city of Moscow) of the fee for the right to conclude the agreement, established upon the results of the auction, for each full calendar month of delay

- Ensure that works are carried out for designing, constructing and commissioning engineering networks and structures required for engineering and technical services for the capital construction structure in accordance with the technical conditions issued by the operating organization
- If the lease agreement stipulates that the tenant is obligated to carry out, using its own and raised funds, works for designing and constructing engineering networks and structures of city importance, provide for gratuitously transferring the results of such works to the ownership of the city of Moscow as represented by the Department of Property of the City of Moscow

### **Agreement termination due to breach by the tenant**

Upon a claim of the landlord, an agreement may be prematurely terminated by a court in cases where the tenant has, in particular:

- Erected unauthorized construction structures on the land plot, including in case of constructing structures in violation of duly approved design and city planning documentation
- Violated the conditions for granting of the land plot determined by the conditions of the auction
- Violated the design deadlines stipulated by the agreement
- Violated the construction and commissioning deadlines stipulated by the agreement

As mentioned above, the landlord is also entitled to claim for premature termination of the lease agreement, with recovery of forfeiture and losses provided for by the agreement, if the tenant fails to meet the deadlines for the separate stages of designing and constructing the structure on the land plot.

### **Compensation for losses of the tenant in case of premature termination of the lease agreement**

In case of premature termination of the agreement the tenant is entitled to claim for compensation for direct, documented expenditures connected with carrying out city planning activities within the permitted (functional) use of the land plot and capital construction structure, the size and parameters thereof.

## **The tenant's right to the land plot upon completion of the construction**

Within 7 days after the due execution of the title to the erected real estate the tenant is obligated to furnish the landlord with the required documents for re-executing the rights to the land plot. In such case, as the owner of the building or structure located on the land plot, the tenant developer is entitled to conclude with the city a long-term lease agreement for the purpose of operating the real estate structure (from 25 to 49 years, or for a shorter term upon agreement of the parties) or to acquire the ownership of the land plot pursuant to the provisions of article 36 of the Land Code of the Russian Federation (see sections 2.1.4.1 and 2.1.7 of the brochure).

### **2.1.5 Agreement on developing a built-up area**

This type of agreement formalizes the relations between an investor and the city administration as regards reconstruction and comprehensive development of an area of the city of Moscow.

The legal grounds for concluding an agreement of this type are articles 46.1-46.3 of the City Planning Code of the Russian Federation (see section 1.6.2. "Development of Built-up Areas").

#### **Resolution on developing a built-up area**

A resolution on developing a built-up area may be adopted if the following real estate structures are located in such area:

- Apartment buildings acknowledged as being hazardous and subject to demolition in the manner established by the Government of the Russian Federation
- Apartment buildings scheduled for demolition or reconstruction on the basis of city target programs
- Other capital construction structures (in addition to the aforementioned) whose type of permitted use and limit parameters do not conform to city planning regulations

A resolution on developing a built-up area is adopted by the Government of Moscow after the required preliminary studies are conducted, namely:

- Determination of a possible mechanism for reclaiming the land plot (area) considering the expenditures and resources required for developing the built-up area, the opinion of users of residential and nonresidential premises, the fulfillment of the conditions connected to engineering networks, and the construction of social and transportation infrastructure

- Preparation of an optimal organizational and economic mechanism for implementing the project for developing the area upon the results of the performed works

An integral part of a resolution on developing a built-up area is a resolution on conducting tenders in the form of an auction for the right to conclude an agreement on developing a built-up area.

### **Form of and procedure for concluding an agreement**

An agreement on developing a built-up area is concluded with the winner of the auction for the right to conclude the said agreement. The amount of the fee for the right to conclude the agreement is the criterion determining the winner.

The model form of an agreement on developing a built-up area was approved by Decree No. 417-PP (Annex 2).

An agreement on developing a built-up area is signed on behalf of the city by the Mayor of Moscow or another person delegated thereby (as of preparing this version of the brochure the right to sign agreements is vested in the first deputy Mayor of Moscow in the Government of Moscow, Mr. U.V. Roslyak).

### **Subject of the agreement. The investor's obligations under the agreement**

The subject of the agreement is developing a built-up area within the elements of the planning structure of the city (neighborhood, community) or parts thereof, using funds of the investor and/or parties engaged by the investor, within the framework of which the investor is obligated to take the following measures, using its own or raised funds, within the terms established by the agreement:

- 1) Prepare the territory development plan, including the territory parcel plan, in accordance with the city planning regulation and regulations of city planning design for the development of a built-up area
- 2) Settle, considering the requirements of residential legislation, property issues with owners and tenants of premises in buildings subject to demolition (reconstruction) and other rightholders of real estate located in the said territory, including:
  - Buyout of residential premises from owners or providing them with equivalent residential premises in the district of residence or other districts upon their consent, including by way of constructing new housing for these purposes
  - Acquisition of residential premises in the district of residence, selected upon the consent of the relocated tenants, or construction in the district of resi-

dence (reconstructed neighborhood) of homes for relocation. The said residential premises are subject to gratuitous transfer to the ownership of the city of Moscow for their further transfer to the relocated citizens

- Resettlement and transport of citizens from evacuated homes to a granted residential area, payment of expenses, connected with transferring and formulating the residential area, to the relocated citizens, etc.
- Acquisition from the respective rightholders, in accordance with civil and land legislation, of the rights to land plots and real estate located within the borders of the built-up area and not subject to expropriation for state needs

- 3) State cadastral registration of released land plots
- 4) Conclusion of lease agreements for land plots (of a term of up to 5 years) for architectural and construction design and construction (reconstruction) of real estate in accordance with the developed and duly approved development plan
- 5) Construction of structures, including of social designation, in the built-up area in accordance with the approved development plan
- 6) Financing of the design and construction of engineering networks and structures, including city main structures and communications providing for the development of the built-up area, pursuant to issued technical conditions
- 7) Payment for technological connection to the electricity distribution networks of OAO "Moskovskaya Elektrosetevaya Kompaniya"

### **Assistance from the city administration**

Within the framework of the agreement, the city administration assumes the obligation to render the investor required assistance in implementing the project for developing the built-up area, expressed primarily in the need to adopt several resolutions, in particular:

- Approval of the development plan for the built-up area
- On expropriation via buyout of residential premises in apartment buildings and eviction of citizens from the residential premises granted under social rent agreements, acknowledged as hazardous and subject to demolition, as well as the land plots on which such apartment buildings are located
- On termination of agreements on rental of residential premises, lease of nonresidential premises and land plots located in the respective area

- On the technical conditions for connecting erected structures to engineering services networks and the connection fee
- On granting land plots for lease to the investor for the purpose of design and construction

### **Rights of the parties to the agreement to real estate upon the results of performing the agreement**

Upon the results of performing the agreement, the parties' rights to the real estate are distributed as follows:

- 1) The following real estate is executed in the name of the investor:
  - Constructed residential and nonresidential premises
  - Land plots and capital construction structures located within the borders of the built-up area and not subject to expropriation for state needs in accordance with civil and land legislation
- 2) The following real estate is executed in the name of the city of Moscow:
  - Residential premises, including premises constructed by the investor with a designated purpose for tenants in buildings subject to demolition. The said premises are gratuitously transferred by the investor to the ownership of the city
  - Structures of engineering, social and utilities infrastructure, civil defense

The list of structures subject to transfer to the ownership of the parties upon the results of implementing the agreement is documented by an additional agreement to the agreement on developing a built-up area after the investor duly draws up the territory development plan.

### **Terms under the agreement**

The agreement on developing a built-up area enters into force as of its signing by the parties and is valid for the term agreed upon by the parties. The term of the agreement may be changed and suspended by agreement of the parties in light of the occurrence of force majeure circumstances. A change in the term of the agreement is documented by an additional agreement, stating the reasons for the change, as well as the penalties if applicable.

The agreement also determines the terms for executing the separate stages of the project for developing the built-up area:

- **First stage** – payment of funds to the budget of the city of Moscow, in the amount determined upon the results of the auction; preparation of the development plan for the built-up area and its approval; development of the territory parcel plan; adoption of a legal act on expropriation of residential premises and land plots, as well as eviction of citizens from repossessed residential premises. Stage term – 18 months
- **Second stage** – preparation of the development design for the area, the schedule for developing the built-up area, including the schedule for constructing (reconstructing) structures; vacation of the land plots subject to development; resettlement of residents (owners and tenants), removal of users of nonresidential premises; state cadastral registration of vacated land plots; conclusion of short-term lease agreements for land plots for architectural and construction design and construction (reconstruction) of real estate. Stage term – 18 months
- **Third stage** – design, construction (reconstruction) and commissioning of real estate. The stage term is determined on the basis of the construction organization plan and fixed in the schedule for constructing (reconstructing) structures
- **Fourth stage** – completion of payments and settlement of claims of the parties, the parties sign an act on the results of implementing the agreement on developing a built-up area, documentation of the property rights of the parties under the agreement

### Features of granting the investor land plots

Lease agreements for land plots are concluded after the due approval of the development plan for the built-up area given the existence of documents confirming the settlement of property and legal issues with owners of residential and nonresidential premises subject to demolition (reconstruction) and rightholders of land plots subject to development.

Land plots are granted to the investor without holding tenders for the purpose of designing and constructing real estate.

The annual rent for a land plot is established in the amount of the land tax for the respective land plot.

Following the documentation of the titles to the residential and nonresidential premises erected within the borders of the built-up area, the investor is entitled to acquire the ownership of the land plots on which the erected buildings and structures are located or to lease them for a long term (see sections 2.1.4.1 and 2.1.7 of the brochure).

## Termination of the agreement due to breach by the investor. Compensation for losses of the investor

If the investor does not perform its contractual obligations, the administration is entitled to refuse to perform obligations and terminate the agreement unilaterally by notifying the investor in writing one month prior to termination.

In case of termination of the agreement, the administration has the priority right to buy out from the investor the results of the works performed on the basis of documents confirming the investor's expenditures, without application of inflation coefficients and adjustment coefficients (at the moment of termination). In such case, the buyout amount is determined as the amount of confirmed expenditures of the investor without consideration of, in particular:

- Unearned income and indirect losses
- Interest payments made while raising borrowed funds
- Penalties under overdue loans and other outstanding liabilities associated with implementing the agreement
- Payments for insuring risk(s)
- Expenditures for overdue pre-project documentation
- Expenditures for works that have lost their value due to long-term non-development of the construction site
- Expenditures incurred by the investor when participating in the auction

If the parties disagree on determining the buyout amount, the dispute is subject to consideration in the Arbitration Court of the city of Moscow.

### 2.1.6 Concession agreement

The legal regulation of concession agreements is the prerogative of the Russian Federation and is carried out on the basis of the Federal Law "On Concession Agreements" dated July 21, 2005, No. 115-FZ (hereinafter, the "**Law on Concession Agreements**").

The city of Moscow plans to use concession agreements within the framework of city programs for developing utilities, transportation infrastructure, the energy industry, and structures of the social and cultural designation.

## **Definition of a concession agreement**

A concession agreement is an agreement under which one party (concessionaire) undertakes, at its own expense, to create and/or reconstruct the real estate determined by the agreement (object of the concession agreement), the title to which belongs or will belong to the other party (concessor), to take actions using (operating) the object of the concession agreement, and the concessor undertakes to grant the concessionaire, for the term established by the agreement, the right to possess and use the object of the concession agreement for taking the said actions.

## **Parties to a concession agreement**

The role of concessor is played by the city of Moscow as a subject of the Russian Federation. Particular rights and obligations of the concessor may be executed by legal entities authorized by the concessor.

In accordance with decree of the Government of Moscow "On Approval of the Provision on the Department of Property of the City of Moscow" dated April 1, 2008, No. 255-PP, the said department concludes, in relation to property of the city of Moscow, concession agreements as well as other agreements documenting relations in the area of public private partnerships. At the same time, it should be noted that as of the date of preparing this version of the brochure, by Order of the Mayor of Moscow dated October 21, 2008, No. 277-RM, the right to sign concession agreements concluded during the implementation of investment projects in the area of capital construction in the city of Moscow is vested in the first deputy Mayor of Moscow in the Government of Moscow, Mr. U.V. Roslyak.

The role of concessionaire may be played by an individual entrepreneur, a Russian or foreign legal entity, or two or more of the said legal entities acting under a simple partnership agreement (joint venture agreement).

## **Objects of a concession agreement**

Objects of a concession agreement may be, for example, roads and engineering structures of transportation infrastructure, systems of utilities infrastructure and other utilities facilities, the metro and other common use transportation, healthcare facilities, educational, cultural, and sporting facilities, facilities used for arranging vacations and tourism, other facilities of the social and cultural designation.

## **Procedure for concluding a concession agreement**

A concession agreement is concluded with the winner of a competition for the right to conclude a concession agreement. In cases stipulated by the Law on Concession Agreements, an agreement may be concluded without holding a competition.



The procedure for holding a competition and the requirements for the competition documentation are determined by the Law on Concession Agreements.

### **Term of a concession agreement**

The term of a concession agreement is established by the concession agreement considering the term for creating and/or reconstructing the object of the concession agreement, the volume of investments in the creation and/or reconstruction of the object of the concession agreement and the payback period of such investments, other obligations of the concessionaire.

In the practice of the city of Moscow there are instances of concession agreements concluded for a term of 49 years (see Decree of the Government of Moscow "On Holding Open Competitions for the Right to Conclude Concession Agreements concerning Real Estate of the Recreation Center 'Krasnaya Gvozdika', the Sanatory Complex 'Vlasevo', the Children's Sanatory Center 'Priziv'" dated April 22, 2008, No. 315-PP).

### **Conditions of a concession agreement**

The conditions of a concession agreement are divided into material and additional conditions.

#### **1) Material conditions**

A concession agreement must include the following material conditions:

- Obligations of the concessionaire to create and/or reconstruct the object of the concession agreement, to meet the deadlines for creating and/or reconstructing it, with its subsequent transfer to state or municipal ownership
- Term of the concession agreement
- Description, including technical and economic figures, of the object of the concession agreement
- Procedure for granting the concessionaire land plots intended for carrying out the actions stipulated by the concession agreement, and the term for concluding lease/sublease agreements with the concessionaire for the land plots (if concluding such agreements is required for carrying out the actions stipulated by the concession agreement)
- Objectives and term for using/operating the object of the concession agreement

- Means of securing the concessionaire's performance of the obligations under the concession agreement, the amounts of the provided security and the term for which it is provided
- Amount of the fee paid by the concessionaire to the concessor during the period of use / operation of the object of the concession agreement (concession fee), the form, procedure and terms for paying it
- Other material conditions stipulated by federal laws

In the absence of any material conditions an agreement is not considered to have been concluded.

## 2) Additional conditions

A concession agreement may contain any other conditions not contradicting legislation of the Russian Federation, including:

- Volume of investments in the creation and/or reconstruction of the object of the concession agreement
- Obligations of the concessor to finance a part of the expenses for creating and/or reconstructing the object of the concession agreement, the expenses for using / operating the said object; to grant the concessionaire state or municipal guarantees, as well as the amount of, procedure and conditions for granting such guarantees
- Obligations of the concessionaire to prepare design documentation for the object of the concession agreement
- Obligations of the concessor and/or the concessionaire to prepare the area required for creating and/or reconstructing the object of the concession agreement and/or for carrying out actions stipulated by the concession agreement
- Procedure for reimbursing expenses of the parties in case of premature termination of the concession agreement
- Amounts of forfeitures for the parties' breach of obligations under the concession agreement

Additional conditions, the list of which is open-ended, are established by agreement of the parties.

## Features of granting concessionaires land plots

In accordance with the Law on Concession Agreements and the Law of the City of Moscow No. 48, a land plot on which the object of a concession agreement is located and/or which is required for the concessionaire to carry out the actions stipulated by

the concession agreement shall be granted to the concessionaire for lease. In such case, a fee for the right to conclude a lease agreement for a land plot is not charged. Pursuant to the Law on Concession Agreements, a concessionaire is not entitled to transfer its rights under a lease agreement for a land plot to other parties or sublease the land plot, unless the lease agreement for the land plot provides otherwise. Termination of the concession agreement is the basis for termination of the rights granted to the concessionaire in relation to the land plot.

## **2.1.7 Acquisition of the ownership of land plots by owners of buildings and structures located on the land plots**

In accordance with article 36 of the Land Code of the Russian Federation, citizens and legal entities that own constructions and structures located on state or municipally owned land plots have the exclusive right to privatize the land plots or to acquire the right to lease the said land plots.

### **Price of privatized land plots**

Until 1 January 2010 the following prices for land plots are established:

- 1) In the amount of 20% of the cadastral value of the land plot:
  - For commercial organizations and individual entrepreneurs that own capital construction structures located on such land plots, if the structures were alienated from state or municipal ownership (privatized)
  - For citizens and noncommercial organizations, if the said parties' titles to capital construction structures accrued prior to the enactment of the Land Code of the Russian Federation (30 October 2001) and federal laws do not establish for the said owners another procedure for acquiring the ownership of the land plots
- 2) In the amount of 30-fold the land tax rate per unit of area of the respective land plot for other parties

The first group combines parties that are entitled to buy out land plots for preferential prices. Preferential treatment applies, in particular, to commercial organizations and individual entrepreneurs that have privatized real estate, for example industrial and commercial facilities, without privatizing the respective land plots. Moreover, note should be taken of the position of the Supreme Arbitration Court of the Russian Federation (SAC RF), pursuant to which preferential treatment for a buyout is applicable only if the real estate located on the land plot to be privatized was acquired by the purchaser directly in the process of privatization, and not as a result of secondary transactions with the real estate (see, for example, Ruling of the SAC RF dated January 22, 2009, No. 15055/08).

From 1 January 2010, owners of capital construction structures will acquire the ownership of land plots occupied by such structures and owned by the city of Moscow or the state prior to delimitation for a price equaling the cadastral value of the land plots, unless federal legislation establishes otherwise.

Resolutions of the Government of Moscow (bodies authorized thereby) on granting land plots for ownership to owners of capital construction structures establish the deadline for paying the fee for acquiring a land plot, not exceeding 30 days from the conclusion of the agreement on sale and purchase of the land plot, and a condition on the necessity to simultaneously pay the fee for acquiring the land plot. In exceptional cases, considering the special social significance of an enterprise as a property complex, payment in installments may be provided for.

### **City planning restrictions concerning privatized land plots**

A prohibition on constructing and reconstructing buildings and structures on a land plot is established by a resolution of the Government of Moscow (the body authorized thereby) on transferring the ownership of land plots to owners of capital construction structures.

A prohibition on construction and reconstruction is removed by the Government of Moscow (the body authorized thereby), having adopted a resolution on transferring the respective land plot for ownership, upon an application of the owner of the land plot and provided it has paid 80% of the cadastral value of the plot, valid at the moment the prohibition on construction and reconstruction is removed<sup>3</sup>.

A prohibition on construction and reconstruction is removed with a prior change of the type of permitted use of the land plot on the basis of an application of the owner of the land plot within the framework of an established city planning regulation.

A prohibition on construction and reconstruction does not apply, in particular, to reconstruction of capital construction structures that does not result in a change in the type of permitted use of the land plot, established in the resolution on transferring the land plot for private ownership and the agreement on sale and purchase of the land plot. In such case, the prohibition on construction and reconstruction is removed upon an application of the owner of the land plot without payment.

### **Procedure for adopting a resolution on privatizing a land plot**

A resolution on granting a land plot for private ownership is adopted on the basis of an application of the owner of the building, construction or structure located thereon.

<sup>3</sup> Despite the fact that Law of the City of Moscow No. 48 does not outline this issue, in accordance with the Federal Law "On Enactment of the Land Code of the Russian Federation" dated October 25, 2001, No. 137-FZ, the said city planning restrictions are applicable only in relation to land plots bought out by owners of buildings and structures located thereon for preferential prices prior to January 1, 2010 (see above).

The issue of granting a land plot for joint shared ownership of applicants is considered on the basis of an application submitted to the DLR on behalf of the owners of all parts of the building, construction or structure located on the land plot.

A resolution on granting the ownership of a land plot required for using a building or structure is adopted by the Government of Moscow or prefects of administrative districts of the city of Moscow. On applications from legal entities, prefects of administrative districts of the city of Moscow adopt resolutions concerning land plots located within the territories of the administrative districts, unless the territory belongs to the natural complex of the city of Moscow and the total area of the building, construction or structure exceeds 3 thousand square meters.

On the basis of a submitted application the DLR gathers the required information for preparing a resolution on granting a land plot or on forming a land plot (information on the total area and stories of the building, on the functional designation of the building and its layout plan, on restrictions on turnover of the land plot, on encumbrances on the land plot and restrictions on its use, on the type of actual use of the land plot, on the existence of unauthorized construction, etc.).

Based on the gathered information the DLR prepares proposals on granting or refusing to grant the land plot to the ownership of the applicant and forwards them to the prefecture of the administrative district of Moscow in which the land plot is located.

### **Grounds for denying the privatization of a land plot. Procedure for appealing a denial**

A denial to grant a land plot to the ownership of the applicant is possible under the following circumstances:

- Land plot is restricted in turnover or barred from turnover
- Land plot is reserved for state needs or there is a resolution on expropriation of the land plot for state needs
- In relation to the land plot, the title, right of permanent (unlimited) use or right of lifetime ownership with hereditary succession of other parties has been registered
- In relation to a part of the building or structure located on the land plot or premises therein, the title of third parties has been registered and such parties have not applied for granting of the land plot for ownership
- Part of the building or structure is owned by the state or municipality

A resolution to deny a land plot from being granted to the ownership of an applicant may be appealed in court.

If the circumstances that served as the basis for denial to grant a land plot to the ownership of an applicant cease, the applicant has the right to reapply for the granting of the land plot for ownership.

### **Procedure for concluding an agreement on sale and purchase of a land plot**

A resolution on compensated granting of a land plot is the basis for preparing a draft agreement on sale and purchase and an act of transfer and acceptance of the land plot according to the model forms approved by the Government of Moscow.

If, within the term established by the resolution on compensated transfer of the land plot to the applicant, the applicant has not signed the agreement on sale and purchase of the land plot and has not notified the DLR of identified technical errors committed during the preparation of the resolution or the draft agreement on sale and purchase of the land plot, the resolution on compensated granting of the land plot is subject to cancellation.

## **2.2 Particularities of Investments in Real Estate in St. Petersburg**

### **2.2.1 Legal Basis**

While considering issues concerning investments in real estate in St. Petersburg it is important to take into consideration the investment process particularities established by St. Petersburg legislation.

In St. Petersburg a new legislative basis was formed which regulates the procedure for making investments in real estate owned by the state and located on the territory of St. Petersburg.

Currently, legal regulation of investments in real estate is carried out, first of all, on the basis of the St. Petersburg Law "On the Procedure for Granting Real Estate Objects Owned by St. Petersburg for Construction and Reconstruction" No. 282-42 dated June 17, 2004 (hereinafter, the "Law").

The previously effective St. Petersburg Law "On Investments in Real Estate in St. Petersburg" No. 191-35 dated July 30, 1998, and a number of legislative acts issued by the St. Petersburg Administration have been abolished.

## 2.2.2 Objects and Forms of Investment Activities

Pursuant to the Law, objects of investment activities may include:

- 1) Land plots granted for new construction
- 2) Unfinished construction objects
- 3) Buildings and constructions subject to reconstruction

Depending on whether the investment object is a land plot or a building (or an unfinished construction object), the following forms of investment activities are possible:

- Granting a land plot for lease or transferring the title thereto to the investor for the purpose of constructing a new object with future commencement of the investor's title to the result of the investments (building, construction built, etc.)
- Granting buildings, constructions and parts thereof subject to reconstruction or construction completion for the purpose of creating a new real estate object

## 2.2.3 General Procedure for Granting Investors Rights to Real Estate Objects in St. Petersburg

### 2.2.3.1 Main Provisions

In accordance with the general procedure established by the Law, real estate objects in St. Petersburg are granted to investors as follows:

- 1) Through tenders, which can be held in the form of:
  - An auction – in this case, the largest amount of payments transferred by an investor is the criterion for determining the winner
  - A competition – in order to hold which, in addition to the conditions for transfer of funds the conditions for creation and use of the result of investments must be determined. For the purpose of determining the results of a competition, a competition commission is formed, which is to prepare a conclusion with respect to the party that has offered the best conditions. Tenders are open as to the composition of participants and are held by a special organization authorized by the St. Petersburg Government. Tenders are currently organized by OAO "Property Fund of St. Petersburg" (hereinafter, the "Property Fund"). Depending on whether the object of investment to be put up for tender is a land plot or a building, the subject of a tender can be:

- A land plot or the right to conclude a land plot lease agreement
- The right to conclude an investment agreement

2) For designated use, particularly in the following cases:

- Granting land plots for lease for purposes of construction, provided that preliminary approval of the location of the real estate object is obtained, as stipulated by land and city planning legislation
- Granting land plots for purposes of reconstruction of production facilities, of objects of engineering and transport infrastructure (with preservation of their designated use) located on such land plots as a part of such production areas, engineering and transport infrastructure areas
- Granting land plots for construction to a party with which an agreement is concluded on developing a built-up area within a territory to be developed in accordance with a decision adopted by the St. Petersburg Government
- Granting dormitories for reconstruction
- Granting buildings recognized as being in a dilapidated condition, in accordance with the established procedure, for reconstruction
- Granting buildings for reconstruction for purposes of making investments in the spheres of culture, academic research, public health services, environmental sciences, education, physical training and sports, and development of the hotel and tourist infrastructures
- To the sole participants of failed tenders that offered investment conditions that meet tender requirements
- In other exceptional cases

It is not permitted to grant the titles to land plots for the purposes of designated use, with the exception of granting land plots for construction to a party with which an agreement is concluded on developing a built-up area.

The procedure for granting real estate objects to investors is established by the Law and the Provision on the Procedure for Adopting Resolutions on Granting Real Estate Objects for Construction and Reconstruction, approved by Decree of the Government of St. Petersburg No. 1592 dated September 21, 2004.



### **2.2.3.2 Investment Agreements**

#### **2.2.3.2.1 Types of Agreements Concluded with Investors**

A resolution on granting a real estate object is adopted by the St. Petersburg Government. Either with the winner of the tender or with the party to which the real estate object was granted for designated use an agreement is concluded which determines the basic conditions for granting of the real estate object and performance of construction or reconstruction works.

St. Petersburg, as represented by the Committee for City Property Management (hereinafter, "KUGI"), and investors can conclude the following types of agreements:

- 1) Agreement on sale and purchase of a land plot – a transaction concluded as a result of a tender for paid alienation of a state owned land plot designated for construction
- 2) Agreement on lease of a land plot on investment conditions – a combined agreement aimed at performance of investment activities relating to a land plot and containing all obligations of the parties related to lease of a land plot, construction development thereof, and fulfillment of other investment conditions
- 3) Investment agreement – a combined agreement containing the parties' obligations for fulfillment of the conditions of construction development of a land plot, performance of reconstruction, finalization of construction of a real estate object (to be concluded if the object of investment is a building or an unfinished construction object). Agreements with investors are concluded in a simple written form and are subject to state registration.

#### **2.2.3.2.2 Content of an Agreement**

The Law provides for a number of obligatory investment conditions that must be included into agreements with investors:

- 1) The legal form of granting the real estate object and further rights to be acquired by the investor to the result of investments
- 2) The payment amount for granting of the real estate object. The payment can be determined, in particular, in the following forms:
  - Initial price – in case of sale of a land plot
  - Rent – in case of conclusion of a land plot lease agreement
  - Value of the right to conclude an investment agreement – if the object of investments is a building

The initial payment amount for granting of a real estate object is determined on the basis of an independent appraiser's valuation. The actual amount of payment (payments) is determined on the basis of the results of a tender, or – in case of granting for designated use – on the basis of the initial amount, taking into account further change of the parameters of the real estate object being created (total area, functional designation, etc.) in comparison with the parameters used for determining the initial amount of payments.

- 3) Deadline for completion of construction (reconstruction) works
- 4) An investment agreement must additionally include conditions concerning the possibility and procedure for assignment and pledge by the investor of its rights and obligations under the investment agreement, as well as conditions concerning the possibility of registration of the right to an unfinished construction object

Along with the obligatory investment conditions, an agreement may also include provisions establishing additional obligations of the investor:

- To reimburse losses and other expenses connected with the demolition of movable and immovable property, relocation of constructions, transport communications, and communications lines and engineering equipment, as well as
- To transfer to St. Petersburg either apartments for housing the people residing in the buildings to be reconstructed or nonresidential premises to house state institutions and enterprises

The forms of the agreements specified in section 2.2.3.2.1 above have been approved by Regulation of the Committee for City Property Management of the St. Petersburg Government No. 235-p dated July 5, 2005 (all agreements with an investor are hereinafter called the "Agreement").

The standard forms of the following documents were approved by the aforesaid Regulation:

- Investment agreement to be concluded with respect to buildings and constructions under reconstruction as well as unfinished construction objects
- Lease agreement for a land plot granted for purposes of completion of construction/reconstruction of a real estate object. The said agreement is concluded for implementation of the Investment Agreement and execution of the investor's leasehold right to the land plot on which the object under reconstruction/construction is located

- Lease agreement for a land plot under investment conditions. Such agreement is concluded in case of granting of land plots for purposes of new construction. In such case, two versions of these agreements are provided for: one version contains a provision on transfer of funds by the investor for purposes of city infrastructure development while the other version does not contain such a provision

Comments on the main provisions of the Agreements concluded with investors are provided below:

### **Designated use of a real estate object**

An Investment Agreement contains a description of the designated use of the real estate object to be granted to the investor, whereby the term "designated use" is used for defining the particular result of the investment activities, such as the construction of a hotel, business center, shop.

Changing the designated use of the real estate object stated in the Agreement is possible only upon St. Petersburg's consent. If such object is used for purposes other than those stipulated in the Agreement, St. Petersburg is entitled to unilaterally terminate the Agreement with the investor.

### **Payments under an agreement**

Each of the abovementioned Agreements contains different provisions on the types of and procedure for making payments.

In accordance with the Investment Agreement, the investor shall effect payment for the right to enter into the Investment Agreement, the amount of which has to be determined on the basis of the tender results or on the basis of a Regulation of the Government of St. Petersburg (in case of designated granting). The mentioned payment can be effected in a lump sum within one month as of the moment of entering into the Investment Agreement or in installments by means of transferring quarterly payments. In the second case, interest shall accrue on such quarterly payments as determined in the Investment Agreement.

Additionally, in accordance with the Lease Agreement for a Land Plot granted for purposes of completion of construction/reconstruction of a real estate object, the investor shall make quarterly rent payments in the amount determined by the law. The rent payment amount is determined on the basis of the methodology approved by the Regulation of the St. Petersburg Government "On Methodology for Determining Rent Payments for Land Plots" No. 1561 dated September 14, 2004 (hereinafter, the "Methodology for Determining Rent Payments").

A rent payment amount depends on the land plot's location (its belonging to a certain zone of city planning significance) and functional use. Furthermore, increasing or reducing coefficients may be applied to certain objects and territories (e.g. increasing rent payment rates for land plots located in trade areas near metro and railway stations).

Regardless of the fact that the lease agreement for a land plot is considered concluded from the moment of its state registration, it incorporates a clause stating that the conditions of the agreement that regulate relations with respect to owning and using the investment object, in particular the investor's obligation to pay rent, come into force from the moment of the signing of the act on transfer and acceptance of the land plot, which is, as a rule, signed simultaneously with the conclusion of the agreement.

As a rule, a concessionary rent payment rate in the amount of 1/10 of the common rate is established by the Agreement for the period of planning and constructing. Once construction is completed, the rent payment amount is changed and depends on the intended function of the constructed object.

In case of entering into a Lease Agreement for a Land Plot under investment conditions, the provision on payments under the agreement can be conceived as follows: The investor shall effect rent payment in the amount determined on the basis of the tender results or on the basis of a Regulation of the Government of St. Petersburg (in case of designated granting). In such case, the total amount of the rent payment equals approximately the market value of the right to long-term lease of the land plot. The rent payment can be effected in a lump sum within one month as of the moment of entering into the Agreement or in installments by means of transferring quarterly payments. In the second case, interest shall accrue on such quarterly payments as determined in the Agreement.

In the second case, the lease agreement for a land plot can provide for payments consisting of two parts: payment for the development of city infrastructure, the amount of which equals, as a rule, the market value of the long-term lease of the land plot (to be effected either in a lump sum or in installments), and the rent payment in the amount determined by the law (in accordance with the Methodology for Determining Rent Payments).

In case of changes in the designated use or increase in the area of the construction object in comparison to the characteristics set forth in the Agreement, the investor is obligated to effect additional payment under the Agreement.

## **Agreement terms**

Agreements with investors are concluded for the term of construction. A fixed schedule for implementation of the investment project – construction or reconstruction – is agreed upon in the agreements. A delay in implementation of the investment

project by the investor serves as the basis for both the imposition of penalties on such investor and the termination of the Agreement upon St. Petersburg's initiative.

If the investor cannot complete the construction (reconstruction) within the terms set forth in the Agreement, the terms of construction (reconstruction) can be prolonged or a decision to terminate the Agreement can be taken. A decision to terminate the Agreement is taken if the volume of construction works already performed on the investment object is less than 10% (which corresponds to the carrying out of ground-works).

If the breach of the construction (reconstruction) terms was caused by the investor, the investor shall pay penalties in accordance with the Agreement, and in certain cases determined by the law shall also pay the difference between the initial and current market value of the object granted to the investor (or the amount of the rent payment for the land plot, respectively).

### **Transfer and pledge of rights under an agreement**

The standard form of an Investment Agreement provides for the possibility of transferring the investor's rights under the Agreement to a third party (assignment of rights under the agreement) as well as pledging the investor's rights under the Agreement. An assignment or pledge of rights under the Investment Agreement is subject to complete performance by the investor of its obligations in terms of transferring the established payments and performance of other investment conditions. Within seven days the investor is obligated to provide KUGI with documents confirming that the transaction entailing transfer or pledge of rights under the Investment Agreement has been conducted. Simultaneously with the assignment of rights under the Investment Agreement the investor shall assign the rights under the Lease Agreement for the land plot granted for completing the construction/reconstruction of the real estate.

Generally, an assignment of rights under the Lease Agreement for a land plot under investment conditions may be executed only upon the lessor's (St. Petersburg's) consent and provided that the investor has transferred rent for a period constituting at least half of the remaining term of the Agreement. Rights under the Lease Agreement for a land plot under investment conditions may be pledged provided the investor is not in debt for payments under the Agreement.

### **Attraction of co-investors**

The standard forms of the Agreements do not circumscribe the possibility of attracting co-investors (share participants) for financing the investment project. The main investor (i.e. the investor that concluded the Agreement with St. Petersburg) is responsible for implementing the investment project in full, regardless of whether or not co-investors are attracted for its fulfillment.

## **Registration of rights to an unfinished construction object**

The Investment Agreement provides that if the investor fulfills its obligations in full regarding transfer of funds and execution of other investment conditions, the investor is entitled to register the title to an unfinished construction object.

In case of conclusion of the Lease Agreement for a land plot under investment conditions, registration of the investor's title to an unfinished construction object is possible only upon the consent of St. Petersburg as represented by KUGI.

## **Applicable law and arbitration**

Agreements concluded with investors may be regulated only by Russian Federation legislation as in accordance with the Russian Federation Civil Code agreements concerning real estate located on the territory of the Russian Federation are governed by Russian law.

Disputes concerning real estate, or rights to real estate, located on the territory of the Russian Federation may be settled only by Russian Federation arbitration tribunals. If real estate is not the subject of the dispute (i.e. the dispute was caused by some other provision of the Investment Agreement, such as for example, payments for infrastructure have not been made), such dispute may be transferred to another court for consideration.

## **2.2.4 Simplified Procedure for Lease of Land Plots in St. Petersburg**

### **2.2.4.1 General Information**

The simplified procedure for lease of land plots is stipulated by the Regulation of the St. Petersburg Government "On Granting for Lease of State Owned Land Plots Located on the Territory of St. Petersburg" No. 405 dated March 16, 2004.

According to the said procedure, investors may acquire the right to lease "formed" land plots for 6 (six) years, i.e. land plots that have undergone cadastral registration and which are free from third party rights. Land plots are granted to investors for the purposes of preparing necessary city planning documents, determining the possibility to build, developing design documents, as well as further construction. Land plots are granted through open tender.

It is necessary to mention that the simplified procedure does not apply to land plots situated within territories designated for residential construction purposes.

#### **2.2.4.2 Procedure for Holding Auctions for Rights to Lease Land Plots**

Rights to lease state owned land plots are granted at open auctions organized by the Property Fund of St. Petersburg acting on behalf of KUGI. The criterion for winning an auction is placing the highest bid for rent payments.

Individuals and legal entities, including foreign legal entities, that have duly submitted all necessary documents and effected an advance payment equaling 20% of the total annual rent amount for the land plot, are allowed to participate in an auction.

The advance payment secures the auction winner's fulfillment of the obligation to conclude a land plot lease agreement and is returned to all losing auction participants after the auction results are announced. The advance payment effected by the auction winner is counted towards the amount of the first payment under the land plot lease agreement. The initial price under the auction equals the total annual rent amount for the land plot, as determined on the basis of a report of an independent appraiser, and the bid increment is 5% of the initial price. The participant that has offered the largest annual rent amount for the land plot becomes the auction winner. This participant signs a land plot lease agreement on the conditions specified in section 2.2.4.3 below.

#### **2.2.4.3 Main Provisions of a Land Plot Lease Agreement**

The sample form of a land plot lease agreement was approved by Order of KUGI No. 273-p dated May 6, 2004. In particular, the sample agreement contains the following main provisions:

##### **Designated use of a land plot**

Land plots are granted for the purposes of preparing necessary city planning documents, determining the possibility to build, and developing design documents.

Provided that the said documentation has been prepared and a construction permit obtained, the lessee is entitled to construct real estate objects on the leased land plot. The designated use of a real estate object to be constructed on the leased land plot is not specified in the sample agreement.

##### **Rent payments**

During the first three years, the investor pays 90% of the total rent amount for the entire term of the agreement (30% in each year of the lease).

For the fourth, fifth and sixth years of the land plot lease agreement, the investor pays 3.33% of the total rent amount respectively, provided that the investor has commenced construction works in accordance with the established procedure. If upon the lapse of

3 years as of the conclusion of the land plot lease agreement the investor has failed to commence construction works, the rent is increased by two times up to 6.66% of the total rent payment per annum for the entire term of the agreement. The average annual rent payment for the land plot, determined as a result of the auction and used for calculating the above payments under the agreement, remains unchanged for the entire 6 year term of the agreement. Once construction is finished, if the lease agreement with the investor is extended for 49 years the rent amount is changed and established with dependence upon the functional use of the constructed real estate object in accordance with current legislation.

If the investor refuses to fulfill the lease agreement for any reason, the rent payments transferred by the investor are not returned.

### **Agreement terms**

Agreements are concluded for terms of 6 years and enter into force as of state registration.

If the investor has completed construction of the real estate object within the established terms, the land plot may be granted for a 49-year lease or may be purchased by the investor in accordance with current legislation (see sections 1.5.2.3 and 1.5.3.4 of the brochure).

### **Transfer of rights and obligations under an agreement**

The standard form of a land plot lease agreement provides for the possibility of transferring the rights and obligations under the agreement to a third party. The lessee is obligated to notify KUGI in advance of the intention to transfer the rights and obligations. In such case KUGI's consent to the assignment of the rights and obligations under the lease agreement is not required.

## **2.2.5 Formation of Industrial and Special Economic Zones**

Industrial zones are developed in St. Petersburg on the basis of Decree of the St. Petersburg Government No. 1961 dated December 14, 2004 "On Development of Territories Designated for Locating Industrial, Transport and Logistics, Public and Commercial and Warehouse Objects". The said Decree specifies a list of territories proposed for locating industrial, transport and logistics, public and commercial and warehouse objects, such as Shushary, Metallostroy, Konnaya Lahta, Predportovaya-3, Noidorf (Strel'na), Kamenka, Rybatskoye, etc. The city Government provides financing for the preparation of the necessary city planning documentation and ensures observance of the terms for its preparation.



Industrial zones will house plants of automobile producers such as Toyota and General Motors.

Apart from manufacturing facilities, it is planned to locate hi-tech factories (mainly software producers) in the industrial zone Noidorf.

The first project of such type in St. Petersburg, where the territory was prepared at the expense of the budget, was the industrial zone of Pulkovo.

In accordance with legislation of the Russian Federation, a special economic zone for technology development with two divisions was established on the territory of St. Petersburg: on the territory of the industrial zone Noidorf and to the north of the forest park "Novo-Orlovsky". Engineering, transport and social infrastructure is created on the territory of the said zone at the expense of the budgets of the Russian Federation and St. Petersburg to attract companies carrying out technology development activities, mainly in high-technology branches of the economy. Land plots on the territory of the special economic zone are granted to its residents only on the basis of lease rights. In accordance with Decree of the Government of the Russian Federation dated December 21, 2005, No. 780, the rent for such land plots may not exceed 2% of their cadastral value per year.

## 3. Structure of an Investment Project and Stages of Its Implementation

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### 3.1 General Information. Choosing an Investment Object

The implementation of any investment project, regardless of its goals, is connected with the necessity to decide on a number of legal and practical issues at each stage of the project. The main stages of implementation of any investment project include:

- Developing the project's concept and determining its goals. For instance, (i) making short-term investments (for a period of 1.5 to 2 years) in order to subsequently sell the real estate, (ii) acquiring a structure for long-term investment, for example, for its subsequent lease or sale, which is generally connected with the reconstruction stage and changing the real estate's designation, (iii) acquiring a land plot for constructing new real estate property
- Marketing in order to determine and assess the most suitable structure for implementation of the investment project, and deciding on the project's financial payback (preparation of a business plan)
- Forming contractual relations and the necessary organizational structure for the practical implementation of the investment project, acquiring rights to real estate, obtaining state authorities' approvals and permits

This section considers the main legal and practical issues that arise during the implementation of each stage of investment projects.

In the Russian market, the possibilities for choosing real estate for investment purposes have significantly expanded in recent years. Apart from international exhibitions held annually in and outside Russia, such as ExpoReal, MIPIM, Barcelona Meeting Point, InterStroy Expo, BATIMAT, PROEstate, etc., at which private and state real estate investment projects are presented, an investment object may be chosen directly in the Russian market. Search options may generally be divided into two main groups:

- 1) Searching for objects with the help of realty agencies that specialize in the market for large investment objects (buildings, land plots), for instance:
  - [www.knightfrank.ru](http://www.knightfrank.ru)  
the Russian division of the international consulting company
  - Knight Frank – ([www.knightfrank.com](http://www.knightfrank.com))

- [www.snr-realty.com](http://www.snr-realty.com)  
the realty firm Stiles & Riabokobylko, an associate member of Cushman & Wakefield in Russia and the CIS ([www.cushwake.com](http://www.cushwake.com))
- [www.cbre.ru](http://www.cbre.ru)  
the Russian division of the international company CB Richard Ellis
- [www.joneslanglasalle.ru](http://www.joneslanglasalle.ru)  
the Russian representative office of the international realty company Jones Lang LaSalle
- [www.colliers.ru](http://www.colliers.ru)  
the real estate agency COLLIERS INTERNATIONAL or with the help of a Russian partner – a company specializing in the real estate market or which is itself an owner of any real estate

2) Applying directly to the Administration of the region (town) in which implementation of an investment project is planned

Information on investment projects is usually provided by state executive or local authority (Administration) subdivisions that are responsible either for working with investors or for managing state property. Lists of objects proposed for investment purposes can be found on the websites of the Administrations of certain regions (in such cases industrial structures are usually implied), for example:

- [www.mossgup.ru](http://www.mossgup.ru)  
the Specialized State Unitary Enterprise for sale of property of the city of Moscow
- [www.property-fund.ru](http://www.property-fund.ru)  
the St. Petersburg Property Fund
- [www.stateinvest.spb.ru](http://www.stateinvest.spb.ru)  
the State Institution "Investment Administration" in St. Petersburg
- [http://mio.mosreg.ru/konk\\_i\\_aukzioni/](http://mio.mosreg.ru/konk_i_aukzioni/)  
the Ministry of Property Relations of Moscow Oblast (information on tenders and auctions for sale and lease of property owned by Moscow Oblast)
- [www.leofi.ru](http://www.leofi.ru) – the Property Fund of Leningrad Oblast
- <http://admgor.nnov.ru/realty/index.html> – information on investment objects in the real estate field on the website of the Administration of Nizhny Novgorod

### **3.2 Verifying Rights to Real Estate (Investment Objects) to be Acquired**

At the initial stage, one of the main issues an investor encounters is verification of a seller's (or lessor's) rights to proposed real estate.

As a rule, the certificate of title is the document that verifies the title to particular real estate. The very fact of existence of a certificate of title allows for considering an individual or legal entity to be the owner of the particular real estate. Nonetheless, it is necessary to note that the said certificate is not a document that establishes rights, and therefore its existence may not protect an investor against risks associated with violations of the procedure for acquiring the rights to the particular real estate committed by the preceding owner. It should be noted that the title may be invalidated by a court upon a claim lodged by a prosecutor or other party considering itself to be the owner of the real estate, in particular based on lack of duly prepared documents establishing rights which verify the lawful acquisition of the rights to the real estate.

A significant portion of the real estate currently offered on the market was obtained by the owners as a result of privatization of such real estate. In the case of acquiring a privatized object, the risks associated with violations of privatization legislation should be examined first of all. The privatization of collective farms currently proposed and plots for both lease and acquisition serves as an example of one of the typical violations. The procedure established by law for the privatization of collective farms included passing a resolution on privatization, dividing the land into shares among all collective farm employees and the employees' subsequent contribution of such shares to the registered capital of the newly created enterprise (usually a joint stock company). Quite frequently that final formal stage at which contributions to the registered capital should have been made was not observed in practice, which now allows any interested party to challenge the results of such privatizations.

Here it is necessary to note that in a number of cases the consideration of disputes concerning invalidation of the results of certain privatizations may be closed due to expiration of the limitation period, 10 years, as most privatization transactions were conducted at the beginning of the 1990s.

In the case of acquiring a state or municipally owned land plot, the main goal of verification is to determine which state authority is entitled to manage the land plot. This particularity is primarily connected with the fact that municipal authorities sometimes pass, in violation of their authorities, resolutions on land management in respect of land plots to which the state titles are not divided.

With respect to newly created property, it is also necessary to verify the documents establishing rights. In particular, in the case of acquiring rights to real estate created in accordance with an investment agreement, it is necessary to analyze the agreement's

provisions related to the procedure for alienating such real estate or rights thereto, including the necessity to obtain the consent of the other party under the agreement to the alienation, the possibility of engaging a co-investor and other conditions significant for entering into the investment project.

Therefore, in all cases it is crucial to conduct a legal due diligence on the owner's rights to the real estate to be sold, and such due diligence must be completed prior to deciding on the real estate acquisition. Such a legal due diligence analyzes a complex of issues. For example, a few such issues are listed below, with indication of the documents required for conducting the due diligence on the rights of the person alienating the real estate:

Main Issues	Required Documents
Procedure of title acquisition	Documents related to the privatization of the real estate by the seller and all preceding transactions therewith, including acquisition of the required corporate and antimonopoly approvals for the transactions
Appropriate state registration of the seller's title	Certificate of Title, issued by the competent state authority
Existence of encumbrances on the real estate and restrictions on the seller's rights	Lease agreements concluded with third parties, mortgage agreements, servitudes
Permitted use of the real estate	For land plots – cadastre passport (cadastre excerpt) For buildings – cadastre or technical passport

### 3.3 Execution of Rights to Investment Objects

The procedure for executing an investor's rights to an investment object includes the following main stages:

- 1) Preparation and approval of documents on whose basis the investor acquires the rights to the investment object (for example, an investment agreement, sale and purchase or license agreements, etc.). At this stage the parties may also conclude a preliminary agreement to fix their intentions, which will be valid during the period of preparing the documents required for conducting the transaction and registering

the rights to the real estate. A preliminary agreement must contain information which allows for unambiguously identifying its subject (i.e. the real estate), as well as material conditions of the agreement. The conclusion of the main agreement may be subject to the fulfillment of certain conditions prescribed by the respective preliminary agreement, for instance changing the real estate's designation, singling out a particular part of the real estate as an independent real estate structure, lifting existing encumbrances on the seller's rights, etc.

- 2) Preparation of the documents for the cadastral and technical registrations of the real estate, which are required for clearly determining the property's characteristics and for the subsequent state registration of the rights thereto, as well as other documents required in accordance with current legislation. At this stage, in particular, the following are required: the investor's preparation of the land plot cadastre passport, the cadastre passport and technical plans for the building or its premises, documents on appraisal of the real estate (if required); acquisition of approvals required for conducting the transaction (for example, resolutions of the legal entity's competent management body on approval of the transaction (if such transaction is a large-scale transaction pursuant to Russian Federation legislation), and acquisition of the antimonopoly authorities' consent to the acquisition of the assets.
- 3) Conclusion of the agreement (execution of another document establishing rights) and state registration of the rights to the real estate.

A detailed description of each stage and a detailed description of the particularities established by regional legislation regarding the execution of rights to real estate are provided in sections 1 and 2 above.

### **3.4 Investment Project Organizational Work (Structuring)**

Regardless of the financing method the investor chooses (described below), in order to optimize the structuring operations connected with the investment project, and in order to reduce the participants' risks, a separate company is usually established (hereinafter, the "project company"). Such a company receives, on one hand, all the rights to the investment project and, on the other hand, all the contractual obligations connected with financing, conducting necessary construction works, and relations concerning the future use of the investment object. The rights to the initial investment object may be transferred to the project company by means of the following main methods:

- On the basis of an agreement (for instance, a sale and purchase agreement or a long-term lease agreement)
- As a contribution to the project company's registered capital

If the rights to the investment object are transferred by a Russian company, it is important to consider the necessity of obtaining the approval of the corporate management bodies of the Russian company (if the value of the property to be alienated constitutes more than 25% of the book value of the company's assets/property), as well as to consider the necessity of obtaining the preliminary consent of the Federal Antimonopoly Service. Pursuant to the requirements of Russian Federation legislation in effect at the moment of preparing this edition of the brochure, the consent of the Federal Antimonopoly Service is required in case of any alienation (including sale and purchase transactions, lease, contributions to registered capitals, etc.) of fixed production assets whose value exceeds 20% of the book value of the fixed production and intangible assets of the party alienating such property, provided that the aggregate amount of the assets of the party alienating the property, the party acquiring the property and the group of parties to which they belong exceeds 3 billion rubles (or its total proceeds from sales of goods for the last calendar year exceed 6 billion rubles) and the value of the party (group of parties) alienating the property exceeds 150 million rubles.

Initially, 100% of the project company's shares may belong to the company that is the owner of the investment object, and subsequently, following the "entry" of other investors into the investment project, the shares in the project company's capital may be distributed in proportion to each investor's participation.

### **3.5 Developing an Investment Project Financing Scheme**

As financing an investment project in the real estate field is generally associated with significant monetary expenditures, such financing is mainly carried out by means of raising investments from third parties, which may be provided in various forms. The particular main forms are: (i) so-called "equity financing," i.e. financing through co-investors attracted to participate in the project, and (ii) credit financing (debt financing) by raising credit funds from banks and other financial institutions. Furthermore, in practice a combination of these two methods is frequently used.

A relatively independent means of financing projects in the construction sphere is concluding investment agreements or agreements on participation in share participation construction. The subject of such an investment agreement is financing by co-investors of the construction of a structure, resulting in the accrual of rights to claim related to the respective parts of the constructed real estate. Generally, funds from legal entities are raised on the basis of investment agreements, while agreements on participation in share participation construction are used for raising funds from individuals for the purposes of residential construction. The said agreements and the sample contents thereof are described in Sections 3.6.2 and 3.6.3 below.

Contractual relations with legal entities and entrepreneurs can be executed in accordance with the Civil Code and laws of the Russian Federation on investment activities unless such contractual relations are regulated by an agreement on share participation construction.

### 3.5.1 Equity Financing

Equity financing may be carried out in various forms:

- Sale of the project company's package of shares (ownership interest)
- Admission of co-investors to the project company's shareholder composition by means of in-kind contributions from them (for example, rights to an investment object or a part thereof)

The strong points of financing through share issuance are, firstly, the absence of any interest payment obligations (as opposed to when using credit funds), and, second, an increase in the project company's financial stability.

For the main investor, however, this financing method leads to a reduction in its share of distributed profits, as well as to its partial loss of control over the project company.

### 3.5.2 Credit Financing

In addition to investors' in-kind contributions to the project company's capital, due to which they jointly participate in the investment project (equity financing), project financing may also be carried out by means of drawing loans and credit (debt financing).

Investors providing credit financing gain profits from the investment project in the form of interest payable on the credit (loans).

Due to the instability of financial markets in Russia, while implementing investment projects, long-term and short-term financing is quite often the thorniest issue.

Short-term lending is not a typical method for financing long-term investments (such as investments in real estate) as the deadline for repaying loan resources must correspond to the period for paying back such investments by means of profits gained from implementing the investment project. However, under Russian economic circumstances investments are often financed by means of short-term loans. At the same time, refinancing is periodically carried out at the time a loan agreement expires, i.e. a loan agreement with a bank is extended for another short-term period or the loan is repaid by means of loan resources from another lender. It is necessary to note that short-term loan financing is connected with particular risks for investors. The main risk



concerns liquidity, i.e. a lender's refusal to extend a short-term loan or the impossibility to adequately replace a loan with another. In such circumstances the project company's short-term solvency (liquidity) drastically declines, which leads to a reduction in the amount of free capital required for maintaining the project company's day-to-day activities.

### **3.5.3 Combined Approach to Financing**

An investment project may be financed by attracting both ordinary co-investors (the method of share participation in the project) and co-investors that simultaneously act as creditors. Such creditors may, for instance, be international financial organizations such as the European Bank for Reconstruction and Development or the International Financial Corporation. In such case, profits from the investment project are distributed between such investors in two forms: (a) in the form of loan interest and (b) in the form of dividends on the investors' share participation in the project company's capital.

## **3.6 Preparing Drafts of Necessary Documents and Signing them**

In order to implement an investment project in the real estate field it is necessary to thoroughly develop an entire package of documents determining the relations between the investors, the procedure for the project company's activities, the investment project financing and the performance of necessary construction works. Depending on the investment project's stages of implementation, such documents may be divided into the following groups:

- Execution of the investment project's organizational structure – the project company's foundation documents, the investment agreement (joint activities agreement) and the documents required for transferring the rights to the investment object to the project company
- Financing the investment project – for instance, loan agreements, credit agreements, agreements for subscription to shares in the project company
- Performance of design and construction works – agreement for the performance
- of design and exploratory works, agreement for development of design documentation, construction contract, agreement with the contractor
- Management and disposal of the real estate that is the result of the investments (agreements with management companies, building lessees, etc.)

As an example, some of the main documents that support the implementation of an investment project are considered below.

### **3.6.1 The Project Company's Foundation Documents**

Depending on the organizational and legal structure chosen by the investors for carrying out the investment project, it is necessary to prepare the respective corporate documents required for creating such a structure (the project company's documents in the jurisdiction chosen by the investors). In addition, it is necessary to prepare other agreements that regulate the issues of the relations between the investors, which may be a joint activities agreement or an agreement on exercising rights of participants in the project company. Such an agreement is usually concluded with the co-investors at the moment of their entry into the project, which may occur both at the initial stage and following the establishment of the project company. In the documents related to executing the investment project's organizational and legal structure special attention must be devoted, in particular, to the following issues:

#### **Managerial control in the project company**

Depending on the status and goals of the investment project's participants, the project company's foundation documents may provide for the participation of one or several main investors in the company's management. In the case of portfolio investments (when a significant, but not controlling, stake in the company is acquired), the company's Articles of Association (or another internal document determining the relations of its shareholders) may contain a provision stating that all main resolutions (including on distributing profits, conducting large-scale transactions, forming the company's management bodies) must be passed by a qualified majority vote.

#### **Provision on the possibility to exit the project**

If the implementation of the investment project is connected with high risks, at the initiative of a co-investor a provision on the possibility to exit the project and be compensated for invested funds may be incorporated into the documents determining the relations of the project participants.

### **3.6.2 Investment Agreement**

An investment agreement (or agreement on investments in construction) can be concluded if legal entities or individual entrepreneurs act as co-investors and the respective investment project is implemented in the area of commercial real estate. Within the framework of an investment agreement, the investor finances the construction or reconstruction of real estate, as a result of which the investor will have the right to demand that the respective part of the constructed or reconstructed real estate be granted upon completion of the construction.

In practice, investment agreements are often used for raising investments by developers that hold rights to real estate (e.g. title or right to lease a land plot or building), plan to construct or reconstruct such real estate and often hold permits for the respective construction works.

The relations under an investment agreement are regulated by general provisions of civil legislation. There are no special requirements for the conditions and procedure for entering into an investment agreement. State registration of an investment agreement is not required.

An investment agreement is entered into in a free form and generally includes the following provisions:

- Description of the real estate in relation to which the investment activities are performed
- Amount of investments in the construction or reconstruction of the real estate as well as the form of, procedure and terms for making such investments (e.g. determining the payment schedule)
- The investor's rights to the real estate upon its construction or reconstruction (e.g. title to the constructed building or a part of the premises in the reconstructed building)
- The developer's obligations to construct and reconstruct the real estate, including the terms for completing the respective works and commissioning the real estate, quality guarantees, the procedure for reporting to the investor, as well as liability for breaching the said obligations
- The investor's rights to the land plot under the building (construction) subject to the investment activities. Considering the requirements of Russian legislation on the interdependence between a land plot and structures located thereon (see sections 1.2.2.2.5 and 1.2.3.2.3 of this brochure), it is recommended that the investor regulate the procedure for using the land plot (e.g. sale or lease of the land plot to the investor) with the developer holding the rights to the land plot
- Governing law of the investment agreement and the procedure for dispute resolution

It should be noted that financing residential construction on the basis of an investment agreement is possible. However, it is not permitted to transfer to individuals the investor's rights under the investment agreement if it will result in direct accrual of such individuals' rights to residential premises upon completion of construction of an apartment building.

### 3.6.3 Agreement on Participation in Share Participation Construction

The subject of agreements on participation in share participation construction is financing by the shared construction participants (hereinafter, **"share participants"**) of the construction of real estate, as a result of which they obtain the right to demand that respective parts of the real estate be granted to their ownership upon completion of the construction.

Guarantees of protection of the share participants' rights, legal interests and property are established by the Federal Law "On Participation in Share Participation Construction of Apartment Buildings and Other Real Estate and on Amending Certain Legislative Acts of the Russian Federation" dated 30 December 2004 No. 214-FZ (hereinafter, the **"Law on Share Participation Construction"**).

The Law on Share Participation Construction must be applied if funds are raised from citizens for constructing apartment buildings. At the same time, the Law does not apply to relations of legal entities and individual entrepreneurs that are connected with investment activities for constructing real estate not based on an agreement on participation in share participation construction.

In accordance with the Law on Share Participation Construction, legal entities holding the title or leasehold right to a land plot and a construction permit may act as developers, i.e. parties raising funds for construction purposes.

Under an agreement on participation in share participation construction (hereinafter, **"agreement"**), the developer undertakes to construct real estate using its own means and/or by engaging other parties and, after obtaining a permit to commission the real estate, to transfer part of the property (selected premises inside the property) to the share participant, who has paid the sum stipulated by the agreement. The Law on Share Participation Construction establishes a number of obligatory requirements for developers raising funds from co-investors on the basis of agreements on participation in share participation construction: a developer is entitled to raise funds only after (1) due receipt of a construction permit, (2) publication and/or placement of a project declaration in cases provided for by the Law on Share Participation Construction, and (3) state registration of the developer's title or leasehold right to the land plot granted for constructing the real estate.

An agreement is concluded in writing and is subject to state registration. The obligatory conditions of an agreement include, in particular: (1) information on the part of the real estate to be transferred to the share participant (for example, an apartment) as defined on the basis of the design documentation, (2) the deadline for the developer to transfer the share participation construction property to the share participant, (3) the

price of the agreement, i.e. the amount to be paid by the share participant in accordance with the agreement, and the payment procedure, as well as (4) the warranty period for the share participation construction property.

The developer's performance of its obligations under an agreement on participation in share participation construction must be secured by a bank guarantee that provides for joint liability of the bank to the share participant for the developer's obligations under the agreement, or by a pledge (mortgage) by operation of law as follows:

- As of the date of state registration of an agreement, the land plot owned by the developer, or the right to lease the land plot, as well as the real estate being constructed thereon are considered pledged to the share participants
- As of the date of state registration of the developer's title to the unfinished construction, it is considered pledged to the share participants
- In case of state registration of the developer's title to premises constituting a part of the real estate that was constructed by raising funds from share participants, the said premises are considered pledged to the share participants

Upon completion of the construction and commissioning of the building, a share participant is entitled to register the title to the part of the constructed real estate for which he/she has paid. The basis for the state registration of the share participant's title is the commissioning permit (submitted by the developer once) and the transfer act signed by the developer and the share participant.

### **3.6.4 Loan Agreement**

A loan agreement may be concluded both with the investors participating in the investment project and directly with the project company itself. In cases when loans are obtained directly by the project company, the co-investors participating in the project company are often the company's guarantors with respect to its performance of the obligations under the loan agreements.

#### **3.6.4.1 Loan Agreement Conditions**

When concluding a loan agreement it is necessary to pay special attention to the following conditions:

- The purposes and conditions for granting the loan (purpose of the loan, amount, currency, terms for granting and repayment, interest rate, conditions for early repayment, penalties for delay in repayment of the principal amount and accrued interest), as well as the conditions precedent for granting the loan

- The commercial terms for granting the loan (including the amount of the flat initial commission, the commission fee for maintaining the loan, etc.)
- Provisions related to "syndication" of the loan
- The creditor's access to the project company's financial and accounting data (may be provided for in an agreement with one or several main creditors)
- Governing law and the dispute resolution procedure

Quite often the loan repayment conditions are connected with the profits gained from the investment project. In this regard, prior to agreeing on the loan repayment conditions it is extremely important to prepare a detailed and reliable financial plan for the investment project, which includes, in particular, a cash flow estimate.

#### **3.6.4.2 Securing the Project Company's Obligations under Loan Agreements**

Security for the project company's performance of its obligations under concluded loan agreements may be, in particular:

- An agreement on pledge of an investment object belonging to the project company (for instance, a land plot)
- An agreement on pledge of a building being an investment object, the construction of which is yet to be finished
- An agreement on pledge of a building being an investment result upon the completion of its construction (for instance, a constructed building)
- Mortgage, by operation of law, of a land plot on which construction is being carried out as well as the building being constructed thereon. In accordance with the Federal Law "On Mortgage (Pledge of Real Estate)," a land plot, or the leasehold right to such land plot, on which a building has been or is being constructed through use of credit funds or special purpose loan funds is considered pledged as of the date of state registration of the borrower's title to the building constructed or being constructed, or as of the date of the registration authority's receipt of a notice from the lender and the borrower on conclusion of the credit agreement (loan agreement) (Clause 1 of Article 64.2 of the Federal Law). Moreover, unless a mortgage agreement or a loan agreement stipulates otherwise, in the case of mortgage of a land plot the pledge right also applies to the pledgor's building or structure located or being constructed thereon (Clause 1 of Article 64 of the Federal Law)
- Agreements on assignment of the project company's rights under its agreements (for example, under preliminary lease agreements with future lessees of premises)

in the building constructed by the project company, utilities agreements, and agreements for providing services connected with management of the constructed real estate)

- Agreements for securing the performance of the project company's obligations to its creditors by certain participants in the project company (for instance, in the form of guarantees, property pledges, providing bank guarantees)

### **3.6.5 Agreement on Subscription to Shares in the Project Company**

A subscription agreement must, in particular, contain the following conditions related to the co-investors' acquisition of shares in the project company:

- The procedure and terms for paying for the shares
- The deadlines for issuing the shares subject to subscription (including the deadlines for the company's authorized bodies to pass the resolutions required for the share issuance) and the conditions precedent for implementation of the share subscription
- The categories of the shares to be issued (ordinary or privileged)
- The possibility of subscribing to additional shares of subsequent issuances in order to preserve the size of each shareholder's ownership interest in the project company (or the possibility of changing the ratio of ownership interest subject to agreement between the investment project's participants)
- Governing law and the procedure for dispute resolution

### **3.6.6 Agreement on Developing Design Documentation**

In order to develop and obtain approval for design documentation for constructing future real estate, the project company concludes an agreement with a specialized design organization (architect) that acts as the client.

The design organization must have a respective license or competency certificate for the corresponding type of works (for more detailed information on licensing see section 1.6.3. "Licensing Construction Activities and Transitioning to Self-regulation"). Design documentation must be developed in accordance with Russian legislation and construction regulations.

In the event of engaging a foreign design organization (architect) to develop design documentation or particular parts thereof (for example, architectural solutions), note should be taken of the necessity to subsequently engage Russian specialists that have the required permits, bringing the documentation into compliance with the Russian construction regulations.

In practice, the primary options for organizing the cooperation of a Russian and a foreign designer are to additionally engage a Russian design organization to participate in developing the design documentation or for the foreign design organization to directly establish a branch or subsidiary in Russia, which obtains the required permits and fully prepares the design documentation. Pursuant to the chosen option, the structure of the contractual relations with the developer is also developed.

When preparing an agreement on developing design documentation, it is necessary to consider special provisions of the Civil Code of the Russian Federation dedicated to agreements on performing design and prospecting works.

It may be advisable to supplement the agreement with obligations of the contractor to perform works within the following scope:

- Assistance with obtaining the city planning design of the land plot, the technical conditions and other required initial documentation (obtaining initial documentation may also be an obligation of the client)
- Development of the technical specifications for designing (this may also be an obligation of the client)
- Development of the design documentation in full (for more detailed information on the main sections of design documentation see section 1.6.4. "Development of Design Documentation")
- Approval of the design documentation by the competent state authorities and organizations and obtaining an affirmative opinion of the state expert evaluation of the design documentation
- Preparation of working documentation for carrying out construction works

If required engineering surveys were not conducted in advance, an assignment for carrying them out may also be included into the agreement on performing design works.

The contractor bears liability for improper drafting of documentation, including flaws subsequently identified in the course of construction as well as in the process of operating the structure created on the basis of the design documentation. In this regard,



it is recommended to supplement the agreement with the designer's obligation to conclude an insurance agreement for liability in case of harm caused to life, health and property of third parties.

Particular attention should also be paid to the issue of transferring to the client the exclusive rights to the design documentation as an item of intellectual rights, including rights to use it by implementing the construction project.

Moreover, it must be noted that the right of authorship (right acknowledged by the author of the work) and the right of the author to the name (right to use or permit the use of the work in its own name) are inalienable. These rights belong to the citizen by whose creative labor the work is created.

Without the author's consent, it is not permitted to change or supplement his/her work (right of integrity of the work). Distorting or otherwise changing the work, and discrediting the honor, merits or business reputation of the author entitles him/her to claim for protection of his/her rights through a judicial procedure. The author of an architectural and city planning work has the right to exercise authorial control over the development of construction documentation and the right of authorial supervision over the construction of the building.

In practice authorial supervision is carried out by the design organization within the framework of the agreement on developing design documentation or on the basis of a separate service agreement.

Depending on the structure of the particular project, the entire set of works for designing the real estate may be included into the construction contract and thus it will not be necessary to conclude a separate agreement with the designer.

### **3.6.7 Construction Contract**

A construction contract is concluded by the project company, acting as the client. Considering the structure of the particular project, various schemes of cooperation with contractors may be chosen.

Depending on who will design the future structure, there are possible alternatives for the project company to conclude separate agreements with the design organization and the general contractor or a single agreement with the general contractor under which both the design and construction will be carried out.

If it is necessary to minimize the client's participation in the construction and impose all liability for implementing the project on the contractor, a turnkey construction contract is concluded. In such case, the contractor assumes all liability for the design, construc-

tion, delivery of construction materials, assembly and commissioning of the structure, as well as ensures that the project complies with mandatory construction regulations and rules. The general contractor chooses the subcontractors for carrying out separate works and enters into contractual relations with them.

In practice, it is also possible for the project company (client) to independently conclude agreements with several contractors. However, in such a case there is a risk of reciprocal claims arising between contractors as well as a risk of emergence of shares of unallocated liability for carrying out construction works. Therefore, it is more expedient to establish relations with subcontractors exclusively through a general contractor.

Despite many construction companies having their own standard construction contracts, using them generally requires making significant amendments and conducting a thorough legal due diligence in order to protect the rights of the project company and separate investors. Therefore, in most cases it is more advisable that the project company have its own construction contract form.

A construction contract may be prepared on the basis of samples issued by the International Federation of Consulting Engineers ("FIDIC"). However, it should be noted that in order to apply such contract samples in the Russian Federation they must be adapted and brought into compliance with mandatory provisions of Russian legislation.

The provisions of a construction contract that must be considered while developing it are as follows:

- The total cost of the works and acceptable deviations from the project cost, in accordance with which the project company will have the right to approve deviations and/or suspend works
- The deadlines for performing the works, including establishment of a fixed date for transferring the structure
- The grounds that allow the contractor to exceed the deadlines for transferring the structure as established by the agreement (in the interests of the investors, such grounds should be minimized). In particular, when incorporating force majeure provisions into the agreement the text of the provisions should be thoroughly analyzed and events that must be under the contractor's control should be excluded therefrom. Furthermore, the force majeure provisions must obligate the contractor to take all possible measures to prevent the actual occurrence of any circumstances that fall under the definition of force majeure
- Compensation by the contractor of damages due to any delay in the construction process in an amount established in advance

- Distribution of unforeseen risks connected with the construction site (i.e. delay or suspension of construction due to a reason stemming from geological or technical conditions of the construction site)
- The contractor's obligation to obtain all approvals and permits from state authorities for implementing the investment project and commissioning the real estate, being the result of the investments, in accordance with the requirements of current legislation

### **3.6.8 Insurance Agreement**

An insurance agreement concluded by and between the project company and an insurance company should cover all risks of losses to the project company in connection with implementing the investment project and its liability to third parties. For instance, in case of any force majeure circumstances (natural disasters or catastrophes) which entail losses or other risks related to implementation of the investment project, the project company's assets may become insufficient for performing its loan agreements. Therefore, it is crucial to thoroughly study the insurance conditions and possibilities at the earliest possible stage of the investment project.

Due to restrictions established by current Russian legislation, an insurer may only be a Russian insurance company holding an appropriate license. Insurance coverage shall, in particular, include:

- Insurance against material damage to the investment object and other objects connected therewith (for example, objects of the natural environment)
- Insurance against material damage to other assets of the project company (for instance, equipment and vehicles)
- Insurance for liabilities of project company employees to third parties
- Insurance for liability for environmental damage caused by the project company
- Insurance against risks connected with using the real estate being the investment result

### **3.6.9 Agreement with a Management Company**

Upon completion of the construction of real estate, the project company may transfer the operation of the real estate to a specialized management company working in the Russian market.

Such a management company may be a company independent of the project company and investors which, depending on the extent of the rights granted thereto, will conclude lease (or sublease) agreements with separate lessees of the premises.

Depending on the activity scheme chosen by the project company, such agreements may be concluded in various forms:

#### **Long-term lease agreement for the entire real estate structure (or a portion thereof)**

Where:

- The project company receives fixed revenue in the amount of the rent under the agreement concluded with the management company and is not a party to the sublease agreements concluded with the direct lessees of the premises
- The risks associated with the operation of the real estate structure are fully borne by the management company

For more detailed information on lease agreements see section 3.6.10 "Lease Agreement".

#### **Agency agreement on operation of the real estate structure**

In this case, the management company acts as the project company's agent and functions as an intermediary while concluding agreements with lessees. The management company's remuneration may be determined on the basis of criteria established by the agency agreement. The owner may retain the functions of strategic decision-making and the functions of controlling management quality, while the functions of day-to-day management of the real estate structure are delegated to the management company.

The main set of services rendered by a management company includes:

##### **1) Management services:**

- Technical and administrative management, including control over the fulfillment of the conditions of concluded sublease agreements, current servicing of clients
- Marketing and advertising aimed at attracting lessees
- Management of financial proceeds from lessees and management of operating expenses

- Organization of the financial reporting system

## 2) Operational, servicing and maintenance services:

- Regular inspections of the real estate structure
- Engineering and technical maintenance of all supply systems (heating, ventilation, water and electricity), including regular preventative maintenance and direct repairs of equipment in case of failure
- Logistics – purchases of materials and equipment required for servicing the Structure
- Development of a system of contractual relations between all work producers and the owner determining areas and degrees of responsibility, as well as choosing operational organizations and concluding agreements with them for the maintenance, servicing and provision of utilities services
- Cleaning of the building and the adjoining areas
- Ensuring safety – installing a security alarm system, an access control system, developing a restricted entry system and engaging qualified security personnel

## 3) Insuring and managing risks

### 3.6.10 Lease Agreement and Preliminary Agreements

#### Preliminary lease agreements

In accordance with requirements of Russian legislation, only the owner of real estate may lease it out. Therefore, it is possible to conclude a lease agreement and transfer a property only upon completion of the construction of the property and registration of the project company's title to the building (premises). In this connection, in practice it is often necessary to conclude a preliminary lease agreement as early as at the stage of construction of the property, with the main lease agreement concluded after the construction is completed and the title registered.

When determining the subject of lease in a preliminary agreement it is recommended to include a detailed description, plan, and reference to the cadastre number. Furthermore, a preliminary agreement must state the term within which the parties are obligated to conclude the main agreement, otherwise the term established by law – one year – will apply, after which the parties' obligations terminate.

Parties often supplement a preliminary agreement with several additional conditions regulating the parties' relations prior to the conclusion of the main lease agreement. For example, these could include conditions on carrying out finishing works, making security payments, and paying penalties in case of failure to conclude the main agreement. Pursuant to the common legal position, a preliminary agreement does not imply carrying out actions other than concluding the main agreement on the conditions agreed upon. In this regard, disputes emerge in connection with making payments within the framework of preliminary agreements, including those of a security nature.

In order to minimize the risks associated with concluding a preliminary agreement, it is necessary to prepare the agreement rigorously and carefully develop the wording.

## **Lease agreements**

A lease agreement for real estate located in Russia may be regulated only by Russian legislation. A lease agreement is subject to mandatory state registration and enters into force as of such registration (with the exception of agreements concluded for a term of less than one year).

Information on the procedure for concluding a lease agreement for a building or structure and its material conditions is provided in section 1.5.5. of this brochure "Procedure for Acquiring Rights to Lease Buildings and Constructions".

From the practical standpoint, the following factors in particular must be taken into consideration:

- A transfer of real estate to a lessee must be documented by a transfer act signed by the parties.
- Given that a lease agreement subject to state registration enters into force as of its state registration, generally rent may be calculated starting from this moment. However, in practice, due to the length of the procedure for registering the transfer of a property, it often occurs before its completion. Current legislation allows an agreement to include provisions on whose basis rent may be calculated as early as from the moment of the transfer of the real estate to the lessee.
- Current legislation establishes a limitation on the frequency of changing the rent. The conditions of an agreement that stipulate the fixed amount of the rent or the mechanism for calculating it may not be changed more than once per year.
- It is necessary to pay particular attention to the wording of provisions on termination of a lease agreement. As a general rule, premature termination of a lease agreement at the request of one of the parties is possible only through a judicial

procedure. However, law provides for the possibility for an agreement to additionally stipulate the grounds for the lessor to repudiate the agreement and terminate it extrajudicially.

- Pursuant to law, a change of property owner does not entail amending or terminating the lease agreement. Consequently, if the property is sold, the lessor's obligations transfer to the new owner.

# Contacts

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