Practice Issues of Foreign Investments Filing in Russia

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The regulation of foreign investments in Russia has become more stringent in recent years. A number of amendments have been introduced to the laws providing the legal regulatory framework for foreign investments in Russia, namely to both the Strategic Investments Law[1] and the Foreign Investments Law.[2] While the amendments to the Strategic Investments Law concern only those foreign companies investing in Russian strategic industries having importance for the national defense and state security, the most recent modification to the Foreign Investments Law affects all the foreign investors. A review of the application of these amendments over the last several years allows for the making of some intermediary conclusions based on the case law with regard to the nature and scope of the Foreign Investments Law's applicability.

According to the 2017 amendments to the Foreign Investments Law, for the purpose of ensuring national defense and state security, the Russian Prime Minister is empowered to refer a transaction of any foreign investor in respect of any Russian entity to pre-closing review by the Government Commission on Monitoring Foreign Investments chaired by the Russian Prime Minister himself (the Government Commission). Such deals are to be considered under a procedure provided by the Strategic Investments Law that is rather complicated. Therefore, the only trigger for requiring foreign investment filings under this amendment is in connection with ensuring Russia's national defense and state security. However, the statutory acts include vague wording noting that national defense and state security interests might include "the complex of terms and factors creating the direct or indirect possibility of damage to the national interests."[3]

Consequently, the Foreign Investments Law, as amended, is applicable to private foreign investors along with the sovereign investors and international organizations, to which the Foreign Investments Law was initially directed. So, if a foreign-to-foreign transaction involving change of control has a Russian dimension, for example a target has a Russian subsidiary, such a transaction may require a filing under the Foreign Investments Law at the Russian Prime Minister's discretion.

When the amendments were introduced, there were many questions regarding the scope of the transactions that would be caught. Answers to many of these questions can be found in recent case law. It turned out that the Foreign Investments Law, indeed, has a broad scope covering all types of investors and transactions concerning, directly or indirectly, any Russian legal entity, if such transactions could pose a threat to national defense and state security.

Formally, the Federal Antimonopoly Service (FAS) or another federal agency may report to the Prime Minister on a transaction, about which they became aware of from any sources. In practice the FAS is the main authority that initiates this procedure as FAS usually learns about the transaction from merger control filings submitted. For this reason, the FAS provided a partial list of so-called red flags that may be useful for foreign investors. This list is still in development. At the moment the red flags include transactions resulting in a foreign investor acquiring a non-controlling stake in a Russian strategic company and transactions resulting in a foreign investor acquiring a controlling stake in an ordinary, not strategic Russian company if such a company either takes part in Russian state programs, is a major employer in a Russian region, is a dominant undertaking, is the only Russian market player in a market with the rest being foreign players, is a manufacturer of civil products which can be used for military purposes, or other similar activities. For example, we are aware that the Government Commission has reviewed an acquisition of a non-controlling stake in a foreign target company having Russian strategic subsidiaries producing civil explosives and an acquisition of control over gold field company that is not a Russian strategic company.

It should be noted that if a transaction is subject to a foreign investment filing, the merger control clearance cannot be issued until receipt of the Government Commission approval of the transaction. If a transaction subject to the foreign investments filing is closed without clearance, the closing is null and void.

Generally, where a transaction has any red flags, the FAS notifies the foreign investor regarding the necessity to suspend the transaction and separately requests that other federal agencies (industry ministries, Ministry of Defense, Federal Security Service) provide input on whether the transaction raises any concerns from the perspective of national defense or state security and whether the Prime Minister should be informed about this transaction. After hearing back from the federal agencies, the FAS prepares documents that outline the transaction for the Prime Minister to review and make a decision as to whether it should be forwarded to the Government Commission's consideration or not. As far as we are aware, not all transactions that are brought to the Prime Minister's attention are passed to the Government Commission review.

According to the letter of the Law, the Prime Minister should exercise this discretion only before the transaction closing. Therefore, if the transaction is already closed, the Government Commission cannot consider it. However, if a foreign investor does not inform the FAS about a transaction, for example, by way of a merger control filing, there is a continuous risk that the transaction can be passed to the Government Commission review until the transaction's closing.

Regarding the timing needed for the transaction's assessment by the FAS and the federal agencies and the subsequent reviews of the Prime Minister and the Government Commission, this process can take about nine months in total to obtain the approval of the Government Commission.

The extremely broad wording of the Foreign Investments Law, as amended, raised many concerns from the point of view of both business and legal counsels. In response, the FAS commented in the media that the amendment was of an exceptional nature and should not be applicable to an ordinary transaction.

There are still many questions to answer regarding the law's applicability. A number of these questions relate to the coordination of the merger control filing and the filing under this new procedure. For example, the Competition Law does not include a formal mechanism to stop the clock for the merger filing through the issuance of a letter by the FAS, which notifies the foreign investor regarding the necessity to suspend the transaction, but in practice this takes place. Also there are no statutory provisions clearly stating that it is not possible to obtain merger control clearance before approval of the foreign investments filing. Separately, there are questions concerning the criteria pursuant to which a transaction can fall within the scope of the Foreign Investments Law as well as the remedies that can be imposed on a foreign investor by the Government Commission. Finally, it is not clear whether it is possible for a foreign investor to make a foreign investment filing prior to the Prime Minister making the decision to refer the matter to the Government Commission. In other words, a foreign investor that receives the FAS letter indicating that the investor has to suspend the transaction pending the outcome of a potential foreign investment filing requirement may want to save time and submit a precautionary foreign investment filing to the Government Commission. That way, if the Prime Minister recommends that a foreign investment filing be made, the filing would have been already submitted to the FAS for immediate review. However, the current rules do not allow the foreign investor to submit the filing voluntarily and the FAS to the start reviewing the transaction until the Prime Minister makes the referral decision.

Therefore, the foreign investments regime in Russia is still evolving. There are no official guidelines regarding the amended Foreign Investments Law's applicability. In the absence of clear criteria for bringing a transaction to the Government Commission review, legal counsel are assessing transactions on a case-by-case basis to determine whether a foreign investor's transaction poses a threat to national defense and state security. Even if it is not obvious at first glance, a detailed analysis of the transaction and its consequences for the Russian dimension is required. So, when implementing a transaction having a nexus to Russian legal entities, it is necessary to reserve the time that would be required for a Government Commission review.

[1] The Federal Law No. 57-FZ dated April 29, 2008 "On The Procedure For Making Foreign Investments In Companies Which Are Of Strategic Importance For Ensuring The Country's Defense And State Security."

[2] The Federal Law No. 160-FZ dated 9 July 1999 "On Foreign Investments in the Russian Federation."

[3] The National Security Strategy approved by the decree of the President of the Russian Federation No. 683 as of December 31, 2015.

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