

Morgan Lewis

SPARK

From our team to yours

As Russia and countries around the world continue to deal with the repercussions of the ongoing COVID-19 pandemic, we continue to hope that you and your family are safe and healthy as you receive this update. Please know that, through all of this, our team remains focused, connected, and ready to support you and your colleagues in any way that we can. And we hope that this quarterly update provides you a useful tool to keep up with changes during the fluctuations between remote to nonremote (and, for some, back to remote) working.

Morgan Lewis Spark is a quarterly update highlighting new and amended Russian legislation of importance to companies operating in the Russian energy and mining sectors.

During the third quarter of 2020 there have been a number of continuing legislative developments, including significant amendments to the Tax Code regarding oil and gas operations, amendments introducing an integrated approach to the selection and implementation of projects for the construction of renewable energy generation facilities, and corporate law amendments adjusting certain time frames related to corporate governance due to difficulties caused by COVID-19 and introducing additional exit rights for LLC participants.

The next edition of **Morgan Lewis Spark** will be published following the end of the fourth quarter. We will continue to watch for Russian legislative developments and sum up the key ones of 2020. (Note this key preview for next time: Just last week there appeared a draft Subsoil Law amendment and accompanying draft regulation—which will allow splitting, spinning off, or consolidation of license areas. This proposed further liberalization has been long discussed and in development.)

If you have questions regarding any of the updates in Morgan Lewis Spark, please reach out to us. We'll be delighted to discuss any of this with you.

Be well.

Q3 | 2020

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MORGAN LEWIS NEWS

In our new [Navigating THE NEXT](#), find resources to help companies navigate the steady stream of workplace policy shifts, guide corporations and investors to the latest aid available for rebuilding, decipher the intersection of global laws for multinational companies, and interpret the meaning of the latest developments.

Keep up to date on the status of international sanctions with our latest update: [US and EU Russia Sanctions Update—Overview And Energy Sector Focus \(And Emerging Russian Countersanctions\) – October 2020](#).

LEGISLATIVE OVERVIEW THIRD QUARTER 2020

We have set out below brief summaries of some of the key legal developments and amendments occurring in the second quarter of 2020 that may be of interest to energy and mining companies doing business in Russia.

Feel free to contact our team in Moscow if you have any questions or if you would like to find out more.

OIL & GAS

Financial Security for Preventing and Eliminating Oil Spills

In July 2020, President Putin signed amendments to the Law on Environmental Protection aimed at preventing and eliminating spills of oil and oil products in Russia. We discussed them in detail in the [Q2 Edition of Morgan Lewis Spark](#).

The amendments come into force starting January 1, 2021. Their implementation requires adoption of a number of bylaws, including with respect to financial security requirements.

The amendments require that a company operating a project must put in place sufficient financial security to ensure full compensation of damages caused to the environment; to the life, health, and/or property of individuals; and to legal entities. The Ministry of Natural Resources has prepared corresponding draft guidelines for the calculation of the required financial security.

According to the draft guidelines, the amount of financial security is to be determined based on a number of parameters, including the scope of work that must be performed in accordance with a plan for prevention and elimination of oil and oil products spills and the cost per unit of such works (services). The financial security can

We hosted AIPN's live webinar "Russia's Oil and Gas Industry at a Crossroads - Energy Transition, Decarbonization and Hydrogen" with guest speaker Tatiana Mitrova, Director, Skolkovo Energy Centre. The webinar is [available online](#).

Watch for an upcoming Russia/CIS AIPN Chapter event in November. If you are interested in becoming a member of AIPN, let us know and we can help you.

be provided as a bank guarantee, an insurance contract, a reserve fund, or a letter of guarantee.

[Draft Decree of the Russian Ministry of Natural Resources: "On the Approval of the Methodology for Calculating Financial Security for Measures Provided Under the Plan for the Prevention and Elimination of Oil and Oil Products Spills, Including Full Compensation of the Damage Caused to the Environment, Life, Health and Property of Individuals, Property of Legal Entities as a Result of Oil and Oil Products Spills"](#)

Liberalization of Shelf Access: Draft Law Is Taking Shape

Recent press reports indicate that there is a compromise achieved in principle among the relevant ministries on the long-debated proposal for legislative liberalization of access to hydrocarbon deposits on the continental shelf. At the moment, continental shelf licenses are available only to certain Russian state-owned oil and gas companies or, in limited cases, joint ventures in which such a company is the majority shareholder (with some exception for specifically designated Baltic Sea fields). This has forced many of the ventures to rely on complex, risk-based service operator structures to date.

In view of insufficient progress in continental shelf development, discussions for access liberalization have been ongoing among the Ministry of Natural Resources, the Ministry of Energy, the Ministry of Far East Development, as well as others, along with the participation of interested energy companies. The reported compromise is to allow the continental shelf projects (in the Arctic and Pacific areas) to be developed with state company minority participation of not less than 50%-1 vote. The most recent draft law text is not yet publically available, and various other details of the proposal remain unclear. It is reported that the draft law is expected to be introduced to the Government in December.

Russia Streamlines Oil & Gas Taxation

A pack of draft laws significantly revising the fiscal landscape for Russian upstream projects was approved at third reading by the Duma on September 30, 2020 and by the Federation Council on October 7, 2020 and signed by the President on October 15, 2020 (“Fiscal Amendments”). These Fiscal Amendments will come into effect on January 1, 2021 (but not earlier than one month after official publication).

The Fiscal Amendments change various parameters of the main upstream fiscal regime components—namely, the Mineral Extraction Tax (MET), the recently introduced Excess Income Tax (EIT), and the Export Customs Duty (ECD)—by amending Tax Code Chapters 25.4 and 26 and Customs Tariff Law Article 3.1. They come as a result of the Finance Ministry’s continued efforts amidst economic challenges to achieve greater contribution from the oil and gas industry to the national budget, while oil companies (supported by the sectoral ministries) have been trying to secure more fiscal incentives needed for development projects in challenging conditions as the production in well-established fields declines.

Highlights of the Fiscal Amendments include:

- removal of ECD exemptions for high-viscosity oil and oil produced from certain fields (designated per physical characteristics)
- various amendments to the rules of calculating the EIT, such as:
 - inclusion of the Sakhalin Oblast (onshore) and the North Caucasus Federal District areas, as well as certain areas within the Republic of Komi and the Samara and Orenburg Oblast into the list of subsoil areas where the licensees are eligible to apply EIT;
 - introduction of a 50% cap for historical costs carryover for the years 2021 through 2023; and
 - amendment of various formulae for calculating ratios and variables used in determining the EIT-based resulting payable amount;
- various amendments to the MET calculation, including linking certain MET deductions to a production incentive agreement, which the subsoil licensee seeking such deduction has to conclude with the Finance Ministry and the Ministry of Natural Resources no later than July 1, 2021.

In general, the Fiscal Amendments appear to reflect the approach of moving away from ECD and a contemplated gradual replacement of MET with EIT. While these amendments are believed to increase the overall fiscal burden on E&P activities, some of the companies may be less affected by (and perhaps even benefiting from) these

amendments than the others—taking account also of the recently adopted MET breaks for upstream operations in the Arctic, which are set to become effective concurrently with the Draft Fiscal Amendments (see below in the Development of the Arctic section). As these new rules are quite complex, specialized tax advice should be sought for analysis of their effect on any particular project or set of facts.

MINING

New Associated Minerals Amendments Adopted

In September 2020, a federal law on stimulating the geological study and extraction of associated minerals during exploration and production of hydrocarbons came into force. It allows all subsoil users, not only state companies, to extract associated minerals under a subsoil license together with the main mineral.

In our 2nd Quarter 2020 edition of [Morgan Lewis Spark](#) we discussed these amendments in more detail. For more, see our Q2 Edition of [Morgan Lewis Spark](#).

Tax Changes

While most of the Fiscal Amendments discussed above relate to hydrocarbon E&P projects, a few revised provisions of the Tax Code also apply to the extraction of hard minerals. In particular, a 3.5 ratio applicable to MET payable is introduced for extraction of certain types of ore, metals, and some other hard minerals. Again, specialized tax advice should be sought for analysis of the effect of these amendments on any particular project or set of facts.

POWER AND RENEWABLES

Use of Renewable Energy in Retail Markets

On August 29, 2020, Prime Minister Mishustin signed a decree introducing amendments to certain legislative acts aimed to stimulate the use of the renewable energy in the retail markets. The decree became effective from September 1, 2020, save for several provisions that gradually come into effect at later times.

The amendments aim to introduce an integrated approach to the selection and implementation of projects for the construction of renewable energy generation facilities in the retail markets and contribute to achievement of the goals of the Paris Agreement and the Sustainable Development Goals stated by the UN General Assembly.

According to the amendments, in 2021 the executive authorities of the constituent entities of Russia that develop schemes and programs for the long-term

development of the electric power industry of the corresponding territories must ensure that the schemes and programs reflect information on:

- (a) generating facilities in the retail electricity market that are qualified generating facilities operating on renewable energy sources as of September 1, 2020; and
- (b) the projects related to generating facilities operating on renewable energy sources, which were selected through competitive procedures carried out prior to December 31, 2020, for inclusion into the constituent entities' scheme of electric power industry development.

Further, the amendments introduce a procedure for inspecting qualified generating facilities operating on renewable energy. Such inspection will be carried out by the Market Council (a nonprofit organization acting as the regulator of the wholesale and the retail electricity markets and the capacity market)—not more than once every three months but at least once every four years. The duration of such inspection cannot exceed 60 calendar days. The inspection includes examination of documents as well as of the qualified generating facility at its location.

[Decree of the Russian Government No. 1298 dated 29 August 2020: "On the Issues of Stimulating the Use of Renewable Energy Sources, Amending Certain Acts of the Government of the Russian Federation and Invalidation of Certain Provisions of Some Acts of the Government of the Russian Federation"](#)

ENVIRONMENTAL PROTECTION

Concept to Support Projects Addressing Climate Change and Carbon Unit Trading

At the end of August 2020, the Ministry of Economic Development put forward a draft concept paper—to be reviewed and approved by the Government—which aims to support the systematic development of climate-related projects in Russia. It envisages development of a transparent framework system for the proper recording of projects aimed at addressing climate change and taking credit of "carbon units"—i.e., units reflecting the reduction of harmful emissions achieved by a project. The framework may be based on the rules set forth in existing international treaties (e.g., the Kyoto Protocol) or "voluntary international standards." The carbon units could be issued by project developers and become tradeable subject to compliance with a verification and registration process regulated by a set of standards and administered by authorized bodies. At this point, the concept is not yet at draft stage, and, if/when approved, is only a roadmap for development of the regulatory framework required for carbon unit trading.

DEVELOPMENT OF THE ARCTIC

Another Set of Incentives for Arctic Zone Residents

Russia continues its efforts to incentivize business activities in the Arctic zone. In the [Q1 Edition of Morgan Lewis Spark](#) we discussed the Decree on the Basics of the State Policy of the Russian Federation in the Arctic for the Period until 2035, which outlined the framework and main goals to expedite economic development of the Arctic region, and a number of amendments to the Tax Code introducing tax incentives providing certain tax breaks for oil and gas projects in the Arctic.

In further pursuit of this Arctic development initiative, in July 2020 President Putin signed a new framework law on state support of entrepreneurial activity in the Arctic zone (the Arctic Framework Law) and a number of corresponding amendments to the Tax Code and other supporting legislation.

State Support of Entrepreneurial Activities in the Arctic Zone

The Arctic Framework Law introduces a framework for state support for businesses in the Arctic zone. The Arctic zone will be treated as a special economic zone, and the procedures of a free customs zone regime will apply subject to the Eurasian Union Customs Code.

This new law outlines a wide range of state support measures for Arctic investors, including shortened and simplified scheduled state inspections with respect to the Arctic zone residents (generally, maximum 15 days, with a maximum 40 hours per year for small-sized business entities, and maximum 10 hours per year for micro-sized business entities); federal, regional, and municipal tax breaks and partial rebates on insurance contributions to state extra-budgetary funds; and various other measures such as subsidies to offset interest rates on loans and to offset the payment of coupon yields on bonds issued as part of the implementation of an investment project.

In order to benefit from the state support, residents of the Arctic zone must enter into an investment agreement with the Arctic zone management company, a specialized company charged with administering the Arctic zone resident regime.

Tax Breaks for Arctic Zone Residents

Tax measures for residents of the Arctic zone provided in this law are included in corresponding amendments to the Tax Code. The new rules took effect from October 1, 2020 (save for the MET tax breaks).

Reduced VAT Rate

Pursuant to the Tax Code amendments, a zero VAT rate will apply with respect to:

- (a) icebreaker escort services for vessels in the Northern Sea Route waters, and
- (b) accommodation of goods under the procedures for the free economic zone in the Arctic zone.

Reduced Profit Tax Rate

The Tax Code amendments introduced a zero tax rate for the federal component of the profit tax payable by residents of the Arctic zone, the priority development areas, and the free Port of Vladivostok, in addition to a reduced rate for the regional component of the profit tax rate. With respect to the Arctic zone residents, the zero tax rate will apply for a period of 10 years from the first profit received.

The rate applicable to the portion of the profit tax payable to the regional budget cannot exceed 5% within 10 years from the year of first profit, but cannot be less than 10% within the following five years. The reduced rates will not apply to Arctic zone residents engaged in extraction of minerals, production of LNG, or processing of hydrocarbons into petrochemicals.

Reduced Mineral Extraction Tax (MET) Rate

Taxpayers with the status of Arctic zone resident will also have the right for a tax deduction from the amount the MET charged with respect to the extract of oil shale, peat, commercial ores (ferrous, nonferrous, and rare metals), various types of nonmetallic resources and diamonds, and many others, excluding coal and crude hydrocarbons (both oil and gas). These amendments will become effective from January 1, 2021.

The MET tax deduction will apply only if extraction took place in a new subsoil block, provided that such block is located completely within the boundaries of the Arctic zone and the percentage of depleted mineral reserves for such subsoil block is less than or equal to 0.001 of the block's total reserves per the state balance of mineral resource reserves as of January 1, 2021, or these reserves are not included in the state balance of mineral resource reserves as of January 1, 2021.

The amount of the MET tax deduction is calculated as the amount of the taxpayer's actual expenditures for the acquisition, construction, manufacture, and delivery of fixed assets and the bringing of these assets into operational condition within the period from January 1, 2021 to the last date of the tax period (inclusive). The fixed assets are limited to roads, transport, engineering, and energy infrastructure required for the extraction of the mineral resource, as well as production facilities for processing (concentration, conversion) of this mineral resource.

The amount of the MET tax deduction is capped at 50% of the tax payable in the tax period in which the deduction

is applied. The tax deduction will apply from January 1, 2021 to December 31, 2032, inclusive.

[Federal Law No. 193-FZ dated 13 July 2020](#): "On State Support of Entrepreneurial Activity in the Arctic Zone of the Russian Federation"

[Federal Law No. 194-FZ dated 13 July 2020](#): "On Amendments to Certain Legislative Acts of the Russian Federation in Connection with the Adoption of the Federal Law" On State Support of Entrepreneurial Activity in the Arctic Zone of the Russian Federation"

[Federal Law No. 195-FZ dated 13 July 2020](#): "On Amendments to Part Two of the Tax Code of the Russian Federation in connection with the adoption of the Federal Law" On State Support of Entrepreneurial Activity in the Arctic Zone of the Russian Federation"

CORPORATE LAW

New Timeframes and Rules for Conducting Certain Corporate Procedures in 2020

Effective from July 31, 2020 certain legal acts relating to corporate procedures in limited liability companies (LLCs) and joint-stock companies (JSCs) have been amended (the Amendments). The Amendments suspend certain provisions of corporate laws (the Federal Law on LLCs and the Federal Law on JSCs) and change the timeframes and rules for conducting certain corporate procedures in 2020 in light of COVID-19 and the measures for the prevention of its transmission.

In March 2020, Russia amended the Federal Law "On Joint Stock Companies" to address the COVID-19 emergency and allow shareholder meetings in 2020 to be conducted by absentee voting if the agenda includes certain items. (For more information, read our [client alert](#).) In the Amendments, the March changes are further developed and extended. According to the Amendments, the general meeting of participants in an LLC in 2020 may be conducted by absentee voting if the agenda includes the items on approval of annual reports and accounting balance sheets.

The timeframes for preparing documents relating to general meetings of shareholders (GMSs) for JSCs has been extended. Additionally, the Amendments revised the minimum period for submitting proposals to the annual GMS agenda (for 2020, at least 27 days prior to the date of the annual GMS) and for putting forward candidates to the board of directors and other bodies of a JSC (i.e., collegial executive body, internal audit committee, ballot committee, and sole executive body).

[Federal Law No. 297-FZ dated 31 July 2020](#): "On Amendments to Article 12 of the Federal Law "On Amendments to Certain Legislative Acts of the Russian Federation Regarding the

Unification of the Contents of Annual Reports of State Corporations (Companies), Public Non-Profit Companies, and on Establishment of the Aspects of Regulating Corporate Relations in 2020 and on Suspension of Provisions of Certain Legislative Acts of the Russian Federation” and on Suspension of Provisions of Certain Legislative Acts of the Russian Federation”

New Rules on Exit of a Participant from an LLC

On July 31, 2020, President Putin signed two federal laws amending the Civil Code and the Federal Law on LLCs with respect to the exit procedures for LLC participants. The laws, *inter alia*, clarify the date when the participatory interest (or part of the participatory interest) in the company will be deemed transferred by an exiting participant, simplify the procedure for recording information on the exit of a participant, and allow more options for the participants of an LLC to structure the exit rights. The new laws became effective from August 11, 2020.

The amendments envisage that the company’s charter can authorize certain specific participants or categories of participant to exit the company. For example, such right can be granted to participants directly mentioned in the charter, or holding an interest above or below a certain amount. The right to exit can be conditional on certain circumstances specified in the company’s charter. In addition, the exit right can be granted to a participant upon a unanimous decision of the general meeting of participants.

[Federal Law No. 251-FZ dated 31 July 2020: “On Amendments to Article 94 of Part One of the Civil Code of the Russian Federation”](#)

[Federal Law No. 252-FZ dated 31 July 2020: “On Amendments to the Federal Law “On Limited Liability Companies” in Terms of Improving the Procedure for Entering Information on the Exit of a Participant of a Limited Liability Company from the Company into the Unified States Register of Legal Entities”](#)

FOREIGN INVESTMENTS IN STRATEGIC SECTORS

Amendments to the Federal Law “On the Procedure for Making Foreign Investments in Business Entities of Strategic Importance for Ensuring the National Defense and State Security”

On July 31, 2020, President Putin signed amendments to the Federal Law “On the Procedure for Making Foreign Investments in Business Entities of Strategic Importance for Ensuring the National Defense and State Security” (FSIL), tightening the Government’s control over transactions of foreign investors in respect of shares

in Russian companies having strategic importance for national defense and state security (strategic companies).

Effective from August 11, 2020, the definition of “control” of a foreign investor over the strategic company, the criteria by which it can be determined whether the strategic entity is under control, and the list of transactions subject to preliminary approval under the FSIL have been amended.

The concept of “control” has been amended to include voting rights (i.e., voting shares or participatory interests) pledged or otherwise temporarily transferred to any third party (parties). This closed a previous technical loophole in the law.

Thus, when determining whether a strategic company is under the control of a foreign investor, or whether a transaction requires prior approval under the FSIL, it is important to check whether the foreign investor has temporarily transferred its voting rights (or some of them) in the strategic company to another person(s) in addition to direct ownership by such foreign investor.

Additionally, the FSIL now provides a nonexhaustive list of contractual structures that can be used to facilitate the temporary transfer of voting rights, including:

- (a) agreement for the fiduciary management of assets;
- (b) pledge agreement;
- (c) repo agreement;
- (d) security payment; and
- (e) other agreements or transactions.

Federal Law No. 255-FZ dated 31 July 2020: “On Amendments to the Federal Law “On the Procedure for Making Foreign Investments in Business Entities of Strategic Importance for Ensuring the National Defense and State Security”

Russia's Regime of Foreign Investment Restriction in Strategic Sectors

Russia’s regime of foreign investment restriction in strategic sectors is particularly complex and features special, stricter rules in the mineral resources (oil and gas and mining) sector for investments by companies having foreign government ownership control. We hope that [this PowerPoint presentation](#), developed from our years of practical experience in this area and recently updated, may serve as a handy reference for our readers.

COVID-19 UPDATE

In June, after two months of stay-at-home orders, the country has commenced the process of returning back to “normal” business. But the last few weeks have seen an increase in reported cases and hospitalizations. More information on COVID-19 legislative actions in Russia, and around the globe, can be found on [our website](#).

COVID-19: Moscow Steps Up Workplace Restrictions, Introduces Reporting Requirements as Infection Rises

In response to the COVID-19 pandemic, President Putin authorized the heads of Russian regions to determine the lockdown rules depending on the epidemiological situation in a particular territory. In this alert we address the most recent restrictions introduced by the Mayor of Moscow, including new reporting requirements. For more, read our [client alert](#).

Morgan Lewis

ABOUT US

Morgan Lewis is recognized for exceptional client service, legal innovation, and commitment to its communities. Our global depth reaches across North America, Asia, Europe, and the Middle East with the collaboration of more than 2,200 lawyers and specialists who provide elite legal services across industry sectors for multinational corporations to startups around the world. For more information about us, please visit www.morganlewis.com.

PRIMARY CONTACTS



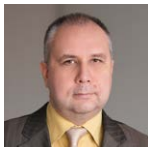
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