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Russia's legal climate: another perspective

The Khodorkovsky ruling is regrettable, but it's important to look at the broader picture and note the significant improvements Russia has made in its business environment.

BY LAURA M. BRANK

Three or four times a year, I travel to the United States to visit clients or attend conferences focused on investing in Russia. Each time, I am startled by the widespread skepticism and even hostility directed toward Russia's business climate, expressed in questions such as, "Do they have any laws in Russia?" or "How can anyone do business there? I hear it's completely corrupt." Clever and knowledgeable businesspeople, who are objective about the pros and cons of doing business elsewhere, such as in China or India, cite a notorious case or two and write off the enormous Russian market altogether. As a lawyer intimately familiar with many of the major foreign

investments made in Russia during the past 16 years, as well as some of the more public disputes, I find the lack of balanced views about conducting business in Russia frustrating — and ultimately detrimental to American business.

Let me be clear. Russia, of course, has serious ongoing problems with corruption and fair and effective enforcement of laws, which must continue to be addressed. The recent regrettable decision by a Russian court to extend Mikhail Khodorkovsky's



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prison term by six years is one glaring example. But this case, which is very much about an internal political struggle, should not be the primary basis upon which to judge the Russian legal or business environment. With Russia on the verge of finally joining the World Trade Organization, it's important to look at the broader picture and note the significant progress the country has made in improving its business climate, particularly during the past two years.

The fact is, Russian law and business practices are developing rapidly. New laws and court decisions have been largely pro-business, pro-foreign investment and Western-oriented. Moreover, one upside of the global economic crisis is that it served as a strong reminder to the Russian government of Russia's connection to the world economy, and of the need to attract foreign capital in an increasingly competitive global market. Interestingly, the economic crisis

For example, one of the major problems following the 1998 economic crisis in Russia was the blatant disregard for shareholder rights, particularly those of minority shareholders. Much was done after the crisis to address some of the major shortcomings in the legal system. There have been, of course, various well-publicized recent attempts to deprive shareholders of their rights and to strip assets from companies. But such attempts have been far fewer and less successful, thanks to changes to both the corporate laws and the laws governing the judiciary, which have reduced the ability of litigants to "influence" judges.

CREDITOR RIGHTS

Similar improvements have occurred with respect to creditor rights. After the 1998 financial crisis, creditors, particularly Western creditors, were shut out of bankruptcy cases, their claims not recognized or severely undervalued. Onerous auction proceedings and pervasive corruption often delayed the outcome and reduced the value of the assets in question. Significant changes to the bankruptcy laws and to the laws governing secured transactions after the 1998 crisis and again at the end of 2008 granted creditors greater rights and protections, including improvements to the out-of-court foreclosure procedures and to the system for granting priorities to competing claims during bankruptcy. Moreover, courts generally have ruled in favor of creditors by refusing to recognize numerous challenges brought by Russian companies seeking to use the economic crisis as a basis for not fulfilling their financial obligations.

Other recent changes to Russian laws are designed to open the economy to foreign investment, although important changes to the law on investments in so-called strategic companies must still be adopted. Russia has, however, eased immigration barriers for highly qualified foreign professionals by introducing a new law granting preferential work permits to foreign professionals earning more than \$65,000 and freeing employers in certain cases from Russian work-permit quotas. The law also expedites

the work-permit process for such workers, increases the term of work permits to three years and applies to them the same attractive 13% income tax rate paid by Russians.

Most important, foreigners have begun to successfully enforce their rights in Russian courts. Companies such as E.I. du Pont de Nemours and Co., Heineken International and Knauf Insulation have all recently won intellectual property cases in Russian courts. In fact, not only do foreigners often win cases against their domestic counterparts in Russian courts, they also frequently prevail in cases against government agencies, such as the tax authorities. Our litigation team, for example, won more than 20 cases last year against Russian parties, including several cases against government agencies.

These recent victories demonstrate that the legal reforms during the past 20 years are more than cosmetic. They are achieving positive real-world results. Although there is still much to be done to reduce corruption, strengthen the judiciary and further protect shareholders and business interests in Russia, it is important to keep things in perspective. Despite well-publicized negative cases such as that of Khodorkovsky, positive change is under way in Russia, and a new generation is emerging that has a more Western view toward the rule of law and its importance — not only to democratic principles, but to economic success.

Laura M. Brank is a partner in the Moscow office of Dechert, where she heads its Russia practice.



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coincided with the beginning of President Dmitry Medvedev's term. This has brought a new focus and changed outlook to the government generally. The laws adopted during the past two years have aimed at better protecting shareholders' and creditors' rights and stimulating the economy by, among other things, reducing unnecessary government interference in business. They have also sought to diversify the economy away from its dependency on oil and other natural resources. Yet this real progress has gone largely unnoticed in the West.