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Buying and Selling Real Estate in Russia

ILN REAL ESTATE GROUP



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KEY FACTS OF REAL ESTATE ACQUISITIONS UNDER RUSSIAN LAW

I. Types of real estate

- land plots;
- buildings, facilities, and other objects closely connected with land (i.e., objects that cannot be removed without detriment to their designation);
- constructions or developments under construction;
- objects qualified as real estate by operation of law (registrable aircraft, ships, inland-waterways vessels);
- residential and non-residential premises;
- car parking space.

Land plots and buildings and constructions constitute two separate types of real estate objects, according to Russian law. In practice, this means that a land plot and a building located on it represent two separate real estate items and can be owned by different parties and even on different titles (for example, right of ownership to the building and right of lease to the underlying land plot owned by another party). State registration of title to buildings, constructions on the one hand and underlying land plots on the other hand, is carried out separately, as well. However, there is a principle of “unanimous destiny of land plot and objects closely connected to it” commonly known in Russian law according to which the building inseparably follows the underlying land plot (see for more details section VII).

II. Right of ownership to real estate (title to real estate)

There are the following types of real estate ownership:

1. Public ownership:

- state ownership comprising

- federal ownership (real estate owned by the Russian Federation);
- ownership of constituent entities of the Russian Federation;
- municipal ownership;
- non-delimited public ownership (i.e., public ownership, which is not explicitly attributed to the ownership of certain particular public owners – federal or regional).

Land plots in state or municipal ownership can be sold only by tender held in the form of auction or without tender in certain cases provided by the law (generally when land plots provided for non-commercial, personal, agricultural purposes).

If title to the public non-delimited land plot is not registered, it does not prevent disposal of such land plot. Generally, such land plots are disposed by local authorities, executive authorities of constituent entities of the Russian Federation or federal executive authorities in cases provided for in the law.

2. Private ownership:

- individual ownership;
- co-ownership (simultaneous enjoyment of right of ownership to the same real estate item by several persons):
 - joint ownership – co-owners enjoy right of ownership to the real estate item in whole, without the opportunity to separate the co-owner’s shares;
 - shared ownership – each co-owner has precise separable share of ownership to the real property.



III. Data and documents on titles to real estate

Prior to making a real estate transaction, parties are supposed to obtain authentic and up-to-date information on the real estate item that is subject to transaction, evidence of existing titles, encumbrances, and other property details.

Right of ownership and other property rights to real estate, encumbrances of these rights, their commencement, transfer, and termination are subject to state registration in the Unified State Register of Real Estate (hereinafter – the “**Register**”). It includes the following information: the real estate objects; rights on real estate; protected and special-use areas; register books; tax map; document journals.

The Register is managed by the Federal Service for State Registration, Cadastre and Cartography (hereinafter – the “**Rosreestr**”). The official website of the Rosreestr - <https://rosreestr.ru>. Reference information on the real estate item such as location address, area, cadastral number, existence of registered rights and encumbrances is available to any third party on the website of the Rosreestr.

Upon the request of interested party, the following information can be provided in an extract from the Register:

- description of real estate item, including its location address, area, cadastral number, and permitted use;
- data on title holders;
- data on registered encumbrances;
- data on third parties’ claims in respect of real estate items, legally asserted claims, and objections in respect of registered rights;
- data on existence of decision on withdrawal of real estate item for state or municipal needs.

A request for provision of extract from the Register can be filed with the Rosreestr in hard copy in person or by post, in electronic form by e-mail or by filling up a request form on the website of the Rosreestr or in hard copy filing with the multifunctional center. The extract from the Register can be provided in hard copy or in electronic form as well, and the respective form should be specified in the request. An extract shall be provided by the Rosreestr within 3 days from the receipt of request.

The document confirming the fact of the real estate title registration is a certificate of state registration of the right to this property.

IV. Sale and purchase of real estate

1. Preliminary agreement

Prior to entering into the main sale and purchase agreement (hereinafter – “SPA”) the parties are entitled to conclude a preliminary agreement.

Under a preliminary agreement, parties agree to conclude the SPA in the future on terms specified in the preliminary agreement.

A preliminary agreement should contain conditions, which allow the determination of a subject matter and other material terms of the SPA and should be concluded in the form provided for the SPA.

A preliminary agreement should specify a term for entering the SPA. If no term is specified, the SPA should be concluded within one year from the date of conclusion of the preliminary agreement.

Should one party to the preliminary agreement fail to conclude the SPA, the other party is entitled to apply to the court to enforce conclusion of the SPA by the other party within 6 months from the date of non-fulfillment of the obligation to conclude the preliminary agreement. The party failing to conclude the SPA



shall reimburse damages resulting from such failure to the other party.

2. SPA

Under an SPA of real estate, a seller is obliged to transfer a real estate item (land plot, building, construction, apartment, or other real estate) to the ownership of a purchaser, and the purchaser is obliged to accept the real estate item and pay a certain sum of money (price) to the seller.

Material terms of the SPA:

– Subject matter of the SPA

The SPA should provide for the data uniquely identifying the real estate item that is subject to transfer to the purchaser under the SPA, including cadastral number, data on the location of real estate on a land plot or as a part of another real estate item. If no such data are specified, the SPA should be deemed not to have been concluded.

– Price

The SPA should provide for the price of the real estate item; otherwise, the SPA should be deemed not to have been concluded.

– Specific provision for sale of residential premises

An SPA of residential premises should provide for list of persons retaining rights to use such premises after transferring them to the purchaser under the SPA with specification of such rights.

Other important provisions:

– Payment conditions

If payment of price under the SPA occurs after the transfer of real estate to the purchaser (sale on credit), additional provisions such as method, terms, and amount of payment should be provided for in the SPA. In case a real estate item is sold “on credit,” it shall be considered

mortgaged in favor of the seller until the full price is paid by the purchaser, unless otherwise provided by the SPA.

– Provisions in respect of real estate transfer

The seller is obliged to transfer the real estate item to the purchaser, and the purchaser is obliged to accept the real estate item from the seller. The transfer of real estate by the seller and its acceptance by the purchaser should be evidenced by a transfer and acceptance act signed by the parties. The parties to SPA may also stipulate a certain provision in the SPA that the SPA itself constitutes the transfer and acceptance act. The risk of loss of the real estate item passes to the purchaser at the moment when the transfer and acceptance act is signed; until then, the real estate item is at the seller’s risk.

Form of the SPA:

The SPA should be executed in writing by means of drawing up one document signed by the parties, otherwise the SPA is deemed invalid. Obligatory notarization of the SPA of real estate is not provided for in the law. The parties can notarize the SPA at their own will.

The SPA is subject to state registration and the title is considered transferred from the moment of such registration.

Rights to land plot when the building/constructions is being sold:

Under the SPA of building, construction, or other real estate item, the purchaser along with the title to such real estate item simultaneously acquires rights to a land plot where such building or construction is located, and which is required for their use.

If a seller has a title to a land plot where real estate being sold under the SPA is located and which is required for its use, the purchaser



acquires a title to such land plot unless otherwise provided by the law.

3. Due Diligence

Within the due diligence procedure, the following legal risks are subject to examination, based on the following documents:

- Legal risks in respect of parties' powers to make transactions:
 - constituent documents;
 - registration certificates;
 - powers to sign the SPA;
 - necessary approvals, permits and consents;
- Legal risks in respect of title to real estate item:
 - certificate of state registration of title. Since July 15, 2016, the issuance of certificates of state registration of title has been discontinued. Currently, the state registration of title and transfer of title is certified by another document - an extract from the Register;
 - extract from the Register;
 - documents of title (for example, SPA);
- Legal risks in respect of prior owners:
 - documents - grounds for acquisition of titles by all prior owners;
- Legal risks in respect of compliance of real estate item with the purchaser's requirements:
 - act on ranging of a land plot within particular category of land;
 - land management file/demarcation plan;
 - expert findings and competent authorities' reports;

– Legal risks in respect of existing encumbrances:

- lease (with a term of more than a year);
- mortgage;
- easement;
- attachment;
- pending court proceeding;
- preservation order.

4. Warranties

The party provided untrue warranties on circumstances significant for conclusion of the SPA, its performance or termination (including in respect of subject matter of the SPA, powers to conclude the SPA, compliance of the SPA with the applicable law, existence of necessary licenses and permits, its financial condition or in respect of third party) shall compensate to the other party on its request damages resulted from the untruthfulness of warranties or pay a penalty provided by the SPA. The party relying on untrue warranties also has a right to unilaterally terminate the SPA unless otherwise provided for in the latter.

Typical warranties in respect of real estate are the following:

- the seller is the registered sole owner of the real estate item;
- the real estate item does not have any encumbrances;
- the condition of the real estate item does not have any quality defects and does not need any repair works;
- there are no pending court proceedings in respect of the real estate item;
- all governmental approvals and permits for construction of the real estate item have been obtained;



- the seller has obtained all corporate approvals for acquisition and disposal of the real estate item;
- there are no third parties' claims in respect of the real estate item.

5. Parties' liability under the SPA

The seller's liability

Should the seller fail to transfer a real estate item to the purchaser, the latter has a right to:

- unilaterally terminate the SPA;
- request the transfer of the real estate item through a court order;
- claim for reimbursement of damages.

Should the seller transfer the real estate item of inadequate quality to the purchaser, the latter has a right at its own choice to:

- claim for pro rata decrease of the purchase price;
- demand the seller removes the defects at its own expense within a reasonable term;
- claim for compensation of the purchaser's expenses resulted from removal of defects.

In case of substantial non-compliance with the quality requirements, the purchaser has a right to unilaterally terminate the SPA and claim for repayment of the purchase price from the seller.

The seller shall transfer the real estate item free of third parties' rights unless the purchaser agrees otherwise. Should the seller violate said obligation, the purchaser has a right to:

- unilaterally terminate the SPA;
- claim for decrease of the purchase price.

Should the property be seized from the purchaser on grounds that existed before entering the SPA, the seller shall compensate damages to the purchaser unless they can prove

that the purchaser knew or should have known about these grounds.

The purchaser's liability

Should the purchaser fail to accept the real estate item, the seller has a right to:

- request the acceptance of the real estate item by the purchaser;
- unilaterally terminate the SPA.

Should the purchaser fail to pay the purchase price the seller has a right to:

- request the payment of the purchase price;
- unilaterally terminate the SPA.

Contractual liability

The seller and the purchaser can agree upon contractual liability for violation of particular provisions of the SPA.

6. Share deal

Another method for acquiring real estate is a share sale – acquiring a share in a company holding title to real estate. A share deal can be performed by acquiring shares in a Russian joint stock company or by acquiring participatory interest in a Russian limited liability company. In a share deal, the purchaser acquires the target company with all its rights, obligations, and liabilities.

Real estate acquisition through a share deal may be preferable for the purchaser due to tax and other advantages of such a transaction. Sale of shares in a joint stock company or participatory interest in a limited liability company is not subject to VAT according to Russian legislation. Besides, share sales can be governed by foreign law selected by the parties to transaction, while asset deals are subject only to Russian law. A share deal allows parties to avoid state registration of transfer of real estate items belonging to the target company.



V. State registration

Transfer of title under the SPA is subject to state registration. State registration is normally done within 7-9 business days from receipt of documents required for state registration (7 for filing directly with the Rosreestr office and 9 for filing with the multifunctional center).

To register the transfer of title, the parties shall submit the following documents to the registration authority:

- an application for registration;
- an SPA or agreement/document – the ground for title transfer;
- documents confirming the applicants' authority (corporate documents, power of attorney, etc.);
- confirmation of payment of state duty;
- corporate and other approvals (if applicable).

Should one party to the SPA avoid state registration of the SPA, the other party has a right to apply to court to render a decision on state registration of title transfer. The party avoiding state registration of the SPA without a reasonable basis shall reimburse damages resulting from such avoidance to the other party.

The purchaser acquires the right of ownership from the moment of state registration of title transfer.

VI. Restrictions on sale of land

Russian law provides for several restrictions on ownership of particular types of real estate:

- Land plots taken out of circulation and owned by the Russian Federation cannot be privately owned and subject to real estate transactions (land plots occupied with state nature reserves and national parks; facilities of the Armed Forces of the Russian Federation, other armed forces, the Federal

Security Service, the state guard authorities; nuclear facilities and storage facilities for nuclear and radioactive materials, etc.);

- Land plots of limited circulation and subject to state or municipal ownership cannot be privately owned unless otherwise provided for in the law (land plots within specially protected territories, forest lands; lands occupied with space infrastructure objects; lands underlying the sea and river ports, hydro-technical utilities, etc.).

Certain restrictions on ownership of land are provided for in respect of foreign citizens:

- Foreign individuals, apatrides and foreign legal entities cannot have a title to land plots located at the border territories the list of which is established by the President of the Russian Federation and at other territories as provided for in the law (within the borders of seaports);
- Foreign individuals, apatrides, foreign legal entities and legal entities with a share of more than 50% belonging to foreign individuals, apatrides and foreign legal entities cannot have a title to land plots classified as agricultural lands and can only possess such land plots on lease terms.

VII. The principle of “unanimous destiny of land plot and objects closely connected to it”

Despite the legal distinction made between land plots and buildings located on them and considering them as separate property interests, one of the basic principles in the sphere of land law is the principle of “unanimous destiny of land plot and objects closely connected to it” which is as follows.

A person, when acquiring a title to a building or construction located at the land plot belonging to the owner of such building or construction, acquires the title as well to such land plot



necessary for use of building or construction, unless otherwise provided by the law.

A person, when acquiring a title to a building or construction located at the land plot belonging to another person, acquires the right as well to use the respective part of such land plot necessary for use of building or construction on the same terms and to the same extent as prior owner did.

An owner of building or construction located at the land plot belonging to another person has a preemptive right to buy or lease such land plot.

Foreign individuals, apatrides, foreign legal entities – owners of buildings or constructions located at the land plot belonging to another person, have a preemptive right to buy or lease such land plot. However, the President of the Russian Federation can provide for the list of buildings and constructions that are not subject to the aforementioned rule.

VIII. State duties/transfer taxes payable on the purchase of real estate

– State duty:

State duty is payable for state registration of title transfer in the amount of 22 000 Rubles for legal entities and 2000 Rubles – for individuals.

– Value added tax (VAT):

The VAT is payable on sale of real estate at the rate of 20 % of full purchase price.

VAT is not imposed upon:

- sale of residential houses or premises and shares in such houses and premises;
- sale of land plots and shares in land plots;
- sale of shares in charter capital of companies holding title to real estate.

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