

CLIENT UPDATE

OVERVIEW OF LEGISLATIVE AMENDMENTS AND RECENT HIGHER *ARBITRAZH* COURT PRACTICE RELATED TO SUBSOIL USE

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At the end of 2012 important changes were made to Russian subsoil legislation pertaining to the use of subsoil sites of federal importance, including those on the continental shelf and those under the inland sea and territorial waters of the Russian Federation (a number of these changes came into force at the beginning of 2013).

In addition, in January 2013 Russia's MNR¹ published a revised draft decree of the Russian Government that identifies the bodies authorized to expropriate land plots required for subsoil use, and also contains regulations governing the submission and consideration of the respective applications of subsoil users.

Set out below is a brief summary of these adopted or planned legislative changes, as well as the recently formulated position of the HAC² on early termination of subsoil use rights in cases where the subsoil user is not guilty of failure to comply with the material terms of the license/licensing agreement.

¹ Ministry of Natural Resources and Environment of the Russian Federation.

² Higher Arbitrazh Court of the Russian Federation.

FORM OF BIDDING FOR THE RIGHT TO USE SUBSOIL SITES OF FEDERAL IMPORTANCE

With effect from **January 11, 2013**, following the entry into force of Federal Law No. 323-FZ dated December 30, 2012, the provisions on bidding for the right to use subsoil sites of federal importance contained in the Subsoil Law, the Continental Shelf Law, and the Gas Supply Law have been amended.³

Pursuant to these amendments, **bidding for the right to use subsoil sites of federal importance** may be conducted **solely in the form of an auction**.⁴ This means that now the sole criterion for selection of the winning bidder to obtain the right to use a subsoil site of federal importance is the amount of the proposed one-off payment for the right to use the respective subsoil site.

According to the President of Russia, the need to legislate for the cancellation of tenders for the right to use subsoil sites of federal importance arose because such tenders had demonstrated a “lack of transparency as well as inefficiency”.⁵

PREVENTION AND CLEAN-UP OF OFFSHORE OIL AND PETROLEUM PRODUCT SPILLS

On December 30, 2012, the President of Russia signed into law Federal Law No. 287-FZ amending the Continental Shelf Law and the Law on Inland Sea Waters, Territorial Waters and Contiguous Zone of the Russian Federation⁶ which is aimed at **reducing the adverse impact on the marine environment in the event of an oil or petroleum product spill** on the continental shelf or in the inland sea or territorial waters of the Russian Federation.

These amendments **come into effect from July 1, 2013** and provide for, *inter alia*, the following:

- adoption by operating organizations⁷ of an offshore oil and petroleum product spill prevention and clean-up plan that has received state environmental approval;

³ Law of the Russian Federation No. 2395-1 on Subsoil dated February 21, 1992 (the “**Subsoil Law**”), Federal Law No. 187-FZ on the Continental Shelf of the Russian Federation dated November 30, 1995 (the “**Continental Shelf Law**”) and Federal Law No. 69-FZ on Gas Supply in the Russian Federation dated March 31, 1999 (the “**Gas Supply Law**”).

⁴ For rights to use subsoil sites not classed as subsoil sites of federal importance bidding may, as before, be conducted either in the form of an auction or tender.

⁵ Please see: <http://eng.state.kremlin.ru/face/4150> .

⁶ Federal Law No. 155-FZ on Inland Sea Waters, Territorial Waters and Contiguous Zone of the Russian Federation dated July 31, 1998.

⁷ An operating organization is an organization that operates/uses artificial islands, installations, structures or underwater pipelines (including for transportation and storage of oil and petroleum products), and performs drilling operations for regional geological study, and geological study, exploration and production of hydrocarbons, on the continental shelf and in inland sea or territorial waters.

- the requirement that operating organizations have financial security in place (e.g. a bank guarantee, insurance policy or reserve fund), and that they have the material and technical resources, personnel and organizational capability to undertake oil and petroleum product spill prevention and clean-up;
- compensation in full by operating organizations for any damage caused to the environment (including aquatic biological resources), the life, health or property of individuals, or the property of legal entities as a result of oil and petroleum product spills, and reimbursement of expenditures incurred by federal executive bodies for manpower and resources to clean-up any oil and petroleum product spills;
- the subsoil license holder's (subsoil user's) subsidiary liability for compensation for any damage caused to the environment (including aquatic biological resources), the life, health or property of individuals, or the property of legal entities as a result of oil and petroleum product spills (if the operating organization has been engaged by the subsoil user under a contract); and
- amending licenses for the use of subsoil sites on the continental shelf or under the inland sea or territorial waters to include conditions requiring subsoil users to use certain technology and methods for the clean-up of oil and petroleum product spills offshore in frozen conditions.

EXPROPRIATION OF LAND PLOTS REQUIRED FOR SUBSOIL USE

On January 25, 2013, the MNR published a revised draft of the decree of the Russian Government on Adoption of the Procedure for the Submission and Approval of Applications and Approval of the Expropriation of Land Plots Required for Operations in Connection with Subsoil Use.⁸ The enactment of such legal act by the Russian Government is envisaged in Article 25.1 of the Subsoil Law.⁹

The revised draft decree refers the matter of the approval of the expropriation of land plots for the purposes of subsoil use (other than land plots required for subsoil use at subsoil sites of local importance, which are expropriated pursuant to the decision of the competent

⁸ Please see: <http://www.mnr.gov.ru/regulatory/detail.php?ID=130113> . Previous versions of the draft decree were published by the MNR on October 3, 2011 and November 6, 2012 (see: http://www.mnr.gov.ru/regulatory/detail.php?ID=127676&sphrase_id=247086 ; <http://www.mnr.gov.ru/regulatory/detail.php?ID=129489>) .

⁹ Pursuant to Art. 25.1 of the Subsoil Law, "land plots for operations in connection with subsoil use are expropriated from their owners, users, possessors and lessees following adoption of decisions on the expropriation thereof upon the applications of subsoil users... The Russian Government shall be responsible for establishment of the procedure for the submission and approval of applications for the expropriation of land plots".

executive bodies of the constituent entities of the Russian Federation) to Rosnedra,¹⁰ with the subsequent processing of the expropriation of the land plots referred to Rosimuschestvo¹¹ (or its regional offices), and includes regulations governing the submission and approval of applications from subsoil users for the expropriation of land plots (if there is no other way to obtain rights thereto).

EARLY TERMINATION OF THE RIGHT TO USE SUBSOIL WHERE THE MATERIAL TERMS OF A LICENSE HAVE NOT BEEN COMPLIED WITH THROUGH NO FAULT OF THE SUBSOIL USER

At the end of 2012 the HAC stated that in order to terminate subsoil use rights for reasons of a breach of/failure to perform the material terms of a licensing agreement by a subsoil user¹² **there is no requirement to prove that the subsoil user is at fault.**¹³

Explaining its reasoning, the HAC noted that the early termination of the right of subsoil use on such grounds:

- constitutes a **termination of contractual relations** in the manner envisaged by the Subsoil Law on the grounds of default by a subsoil user as a business entity acting at its sole risk in the performance of its obligations under the contract (the licensing agreement); and
- **does not amount to an administrative penalty** (imposition of administrative sanctions), the enforcement of which requires proof of the fault of the person in respect of whom such measure is applied.¹⁴

Therefore, the HAC classified a licensing agreement between a subsoil user and Rosnedra as a civil law contract and deemed that it was lawful to terminate the right of subsoil use in the event that a subsoil user had failed to perform the material terms of such licensing agreement

¹⁰ Federal Agency for Subsoil Use.

¹¹ Federal Agency for Management of State Property.

¹² In accordance with Art. 20.2(2) of the Subsoil Law, the right of subsoil use may be early terminated, suspended or restricted in the event of breach by a subsoil user of the material terms of a license by the bodies that issued the license.

¹³ Please see: HAC Ruling No. BAC-9662/12 on referral of a case to the HAC Presidium dated September 14, 2012 (the HAC Presidium sat on November 27, 2012; the relevant Ruling of the HAC Presidium has not yet been published).

¹⁴ In so doing the HAC cited paragraph 20 of Ruling No. 10 of the HAC Plenary dated June 2, 2004 on Certain Issues Arising in Court Practice in the Course of Hearing Cases on Administrative Offenses, which sets forth that suspension/cancellation of a license does not constitute a sanction within the meaning of the Administrative Offenses Code of the Russian Federation, but is rather a special precautionary measure expressly associated with the specific features of an activity, the performance of which could affect constitutional rights and freedoms, as well as the rights and lawful interests of third parties.

through the fault of third parties (e.g., contractors engaged to perform work in connection with subsoil use). Taking into account the HAC's reasoning as mentioned above, it remains unclear whether the conclusion of the HAC on the absence of a requirement to prove that the subsoil user is at fault may be applied to early termination of the right to use subsoil on the grounds of breach of the material terms contained in the list of subsoil use conditions included in a license (which, as opposed to a licensing agreement, is not in the form of an agreement/contract).¹⁵

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Please do not hesitate to contact us with any questions.

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¹⁵ Since March 2010, the procedure for issuing subsoil use licenses has not envisaged the conclusion of licensing agreements being integral parts of such licenses between Rosnedra and subsoil users, but has rather included a list of subsoil use conditions as an integral part of a license. However, licensing agreements continue to constitute a valid part of licenses registered prior to this time and not subsequently amended.