CLIENT UPDATE

VAS CLARIFIES A NUMBER OF KEY ISSUES RELATED TO LEASE CONTRACTS

MOSCOW
Alyona N. Kucher
ankucher@debevoise.com

Natalia A. Putilina
naputilina@debevoise.com

Ivan V. Podbereznyak
ivpodbereznyak@debevoise.com

On January 25, 2013, the Plenum of the Higher Arbitrazh Court of the Russian Federation ("VAS") issued Decree No. 13[1] (the "Decree"), in which it clarified a number of important issues related to lease contracts (in the first instance those involving the lease of immovable property) that had long remained unresolved.[2] In particular:

- It confirmed that part of a property may be leased provided it is properly described in the contract;
- It provided unequivocal guidance on whether a lease for future property is permitted;
- It further resolved the matter of whether immovable property could be leased prior to being commissioned (e.g., to undertake repairs or fit-out), provided that the operation of such property is not in breach of the requirements of town planning legislation;

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1 Decree on Amendments to Decree No. 73 of the Plenum of the Higher *Arbitrazh* Court of the Russian Federation, dated November 17, 2011, on Certain Issues of the Practical Application of the Rules of the Civil Code of the Russian Federation on Lease Contracts.

2 Technically speaking, the Decree is a supplement to Decree No. 73 of the Plenum of the Higher *Arbitrazh* Court of the Russian Federation, dated November 17, 2011, on Certain Issues of the Practical Application of the Rules of the Civil Code of the Russian Federation on Lease Contracts ("Decree No. 73"). According to unofficial information from the Private Law Administration of VAS, it is expected that if further clarifications are required on leases, such clarifications will be issued in the form of amendments to Decree No. 73.

- It placed a prohibition on the lease of an unauthorized construction;
- It introduced the rule that a lessee cannot refuse to pay rent and demand the refund of rent already paid merely on the ground that the lessor does not hold ownership title to the leased property;
- The implications of not effecting state registration of long-term lease contracts were changed: in such cases, the lease will be deemed null and void only in respect of third parties, but not in respect of the principal parties. The contract will remain in effect between the parties (provided that the parties have reached agreement on all of the material terms of the contract);
- It confirmed that the rent may be changed more than once a year by agreement between the parties;
- It introduced a new rule that if the rental is changed unilaterally (if such option is provided for in the contract) the lessor must be guided by changes in the respective average market rates. Otherwise such "non-market" increase will be deemed abuse by the lessor of his right, and the courts must dismiss any claims to recover any portion of the rent in excess of the relevant average market rate;
- It changed the rule on premature termination of a lease contract by a lessor if the rental is not paid on time. Previously, the lessor forfeited the right to terminate the contract if the lessee managed to pay the rent before the contract was terminated. The Decree established that failure to pay the rent on time was a sufficient ground for termination of the lease.

Below, we review the key provisions of the Decree.

LEASE OF PART OF A PROPERTY

The Decree resolves the age-old problem of whether or not part of an object can be leased. This issue has been of particular relevance for the lease of immovable property.

Confusion arose from the fact that civil law did not expressly provide for the lease of part of an object.[3] For a long time, the view was held (and mostly supported by court practice) that a lease contract could not be signed for part of an immovable object without such part being carved out into a separate immovable object. This made the contractual construction of leasing of part of an object meaningless, since after carve-

[3] See Art. 607 (Objects of a Lease) of the Russian Civil Code.

out such part of the object became, for all legal purposes, a new discrete immovable object, and it was now a matter of leasing of a whole object, rather than its part.

However, there was a need in civil law for such concept of a lease contract for part of immovable property, because in many cases the parties were interested in leasing just a portion of a property (e.g., lease of space in a shopping mall, lease of part of the roof or façade of a building for placement of advertising, lease of a portion of premises to situate an ATM, lease of a work space, etc.). As a general rule, the carve-out of such parts into separate discrete immovable objects would, for practical reasons, be unfeasible.

Despite all the uncertainty, in practice people still signed lease contracts for parts of immovable objects. As a rule, these were short-term contracts (i.e., for a term of less than one year), because, on the whole, the registration authorities supported the view that the lease of a portion of immovable property was not permitted and usually declined to register long-term lease contracts (i.e., leases for a term of 1 year or more).

Court practice on lease contracts for part of an object has developed in several stages. At first, most courts took the fairly hardline stand that such lease contracts should be deemed null and void.[4] In time, the position of the courts (in particular, VAS) began to grow more liberal. At first, it involved only parts of a property (e.g., roofs and façades). At this point, VAS took the line that contracts for the use of a portion of real estate were not leases, but contracts not defined in the Civil Code of the Russian Federation ("Russian Civil Code").[5] This gave rise to a multitude of questions on how to classify such contracts correctly and whether any provisions at all on leases, as set forth in civil law, applied to such contracts. (We should note that things were taken to an extreme in the suggestion that such contracts should be deemed services contracts.) VAS subsequently applied the rules of the Russian Civil Code on leases to such contracts for the use of roofs and façades by analogy, but did not expressly call these contracts leases.[6]

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4 See, e.g., Ruling of the Federal *Arbitrazh* Court (FAC) of the East-Siberian District, dated January 15, 1998, No. A33-1392/97-C2-F02-1378/97-C2; Ruling of FAC of the North Caucasus District, dated November 26, 2001, No. F08-3848/2001 in Case No. A32-7005/2001-32/148.

5 See paragraph 1 of Information Letter No. 66 of the Presidium of VAS on a Review of Dispute Resolution Practice in Relation to Lease, dated January 11, 2002.

6 See paragraph 7 of Decree No. 64 of the Plenum of VAS on Certain Issues of Dispute Resolution Practice Relating to the Rights of Titleholders to Premises to the Common Property of a Building, dated July 23, 2009.

Nevertheless, despite the change in the approach of the courts, until adoption of the Decree, there was still no uniform approach to this issue: some courts conceded the possibility of leasing part of an object,[7] and some did not.[8]

The view that lease contracts could be concluded for part of an object was formulated for the first time in the Decree. VAS noted that if property was leased for a term of one year or more, such lease contract would be subject to state registration, and the lease would be deemed an encumbrance over the whole of the immovable object, and not just the part that had been leased out. (See an analysis of issues of the registration of lease contracts in Section 3 of this update below.)[9]

Certain experts within the Private Law Administration of VAS assert that the Decree implies that, as a general rule, in order to lease out part of immovable property there is no need to enter a cadastral record for that part only (whether or not there is a cadastral certificate for the whole immovable object in the title documents). VAS itself has noted that if a lease contract for a part of immovable property requires state registration, then a cadastral certificate for the immovable property will only be required if such certificate is missing from the documents in the relevant file kept by the registration authority. Thus, if there is no cadastral certificate in such title documents, it would have to be provided.

Furthermore, for land plots owned by the state or a municipal body (or land plots where ownership has not been demarcated), a different rule applies: for such portion of a land plot to be leased out, preliminary cadastral registration of such portion of the land plot is compulsory.[10]

However, subleasing a part of such land plot does not require that it first undergo cadastral registration; it is sufficient that such part of the land plot be merely identified in detail in the sublease contract.

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7 See, e.g., Ruling No. 14950/10 of the Presidium of VAS, dated April 19, 2011, in Case No. A40-127386/09-122-889.

8 See, e.g., Ruling No. F03-4058/2012 of FAC of the Far East District, dated September 11, 2012, in Case No. A73-2352/2012.

9 See paragraph 9, sub-paragraphs 2 and 3 of the Decree .

10 Such approach corresponds to the legal position of VAS as expressed during the hearing of a specific case where the lease of a portion of a land plot was deemed permissible provided that title to the land plot was held by a state or municipal entity and provided that the relevant parts of the land plot had been allocated cadastre numbers (see Ruling No. 14950/10 of the Presidium of VAS, dated April 19, 2011, in Case No. A40-127386/09-122-889).

LEASE OF FUTURE PROPERTY

General

Prior to enactment of the Decree, the courts interpreted the relevant provisions of the Russian Civil Code such that, as at the date of the execution of a lease contract, the lessor already had to be the titleholder of the property being leased out. Otherwise, the courts ruled such lease contracts (i.e., lease contracts for future property) invalid.[11]

In practice, however, there was a need for lease contracts for future property: in the first instance to receive advance payment from lessees to finance building work, and also so that the future lessee could gain access to the premises to begin fit-out without waiting for completion of state registration of the lessor's ownership title. In such cases the parties would enter into separate agreements for the provision of access to the premises without actually calling them lease contracts. (As a rule, these agreements were called agreements on the commercial use of premises.) Another widespread practice was the execution of preliminary lease contracts that included a clause on the provision to the lessee of access to the premises to conduct a fit-out.

From the legal point of view, both constructions were very vulnerable. Agreements on commercial use were, effectively, lease contracts and, therefore, at risk of being reclassified and deemed invalid as lease contracts for future property. As for preliminary contracts incorporating a clause on the provision to the lessee of access to the property – the concept of a preliminary contract does not assume any obligations between the parties other than the execution of the principal lease contract at a future date. Consequently, such provisions on the granting of access to premises incorporated in preliminary contracts could also be ruled invalid by the courts.

It should be noted that, at one time, a similar problem existed in respect of contracts for the sale of future real estate. However, in mid-2011, VAS declared that such contracts were permissible.[12] It was then expected that VAS would take a similar approach to the lease of future real estate. This VAS did in the Decree, stating that if a lessor did not yet hold title to a leased property at the time of execution of a lease

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11 Ruling of VAS No. VAS-11180/12, dated October 1, 2012, in Case No. A23-4080/2011; Ruling of VAS No. VAS-6384/10, dated May 27, 2010, in Case No. A79-6404/2009; Ruling of FAC of Volga-Vyatka District, dated November 2, 2010, in Case No. A29-4382/2010).

12 Decree No. 54 of the Plenum of VAS, dated July 11, 2011, on Certain Issues of Dispute Resolution Practice Relating to Real Estate to be Created or Acquired in the Future.

contract, this in itself did not mean that the lease contract was invalid. The important thing was that the lessor acquired title by the time the lease contract was due to be performed (i.e., upon transfer of the property to the lessee).

If for some reason the lessor were not to perform its obligation to lease out the object, and if it were also not the titleholder to the object,[13] then the lessor would have to compensate the lessee for losses incurred through breach of the contract (and the lessee would also have recourse to any other legal remedies provided for in the contract, such as contractual penalty).[14]

As regards the permissibility of lease contracts for future immovable property, we believe that in practice this will lead to a substantial reduction in the need for preliminary lease contracts. Until now, preliminary lease contracts were standard practice in the commercial real estate business (even despite certain risks relating to the validity of such preliminary contracts). With the emergence of a new instrument – the lease contract for future real estate – in the vast majority of cases there will no longer be a need for preliminary lease contracts.

The VAS Decree also separately clarified the following cases that seem, on the face of it, similar to lease of future real estate, but that will be subject to special regulation: leasing out another's property, leasing out uncommissioned property, lease of an unauthorized construction, and certain other cases.

Leasing out another's property

The basic problems with leasing out another's property involve inequitable conduct on the part of lessees, who would allege that lease contracts signed by an unauthorized person were invalid, and determining what rights the titleholder had to reclaim property and from whom, in the context of the lease arrangement.

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13 Alternatively, in accordance with Article 398 of the Russian Civil Code, the lessee would be entitled to force the lessor to lease the object in question to the lessee (provided that the lessee's demand to lease the object arose earlier than any demands of other potential lessees of such object or, if it cannot be established whose demand arose earlier, the lessee filed a claim earlier than any other lessees) .

14 See paragraph 10, sub-paragraph 3 of the Decree.

The Decree addresses these issues. It also limits itself to this context and is not concerned with the grounds and procedure for reclaiming an object from the unlawful possession of another.[15]

As far as the first issue goes, in practice it was often the case that a lessee would use property and then, after a certain time, would refuse to pay rent, referring to the fact that the lessor did not hold title to the property.[16]

The Decree states clearly that, in the event of such disputes, the lessor is not under any obligation to prove that he holds good title to the property being leased out. Therefore, the lessee cannot cite the invalidity of the lease contract and use this as a ground to refuse to make rent payments and claim a refund of payments already made.[17]

In relation to the second issue (the rights of the titleholder to an object upon its recovery from unlawful possession), VAS indicated that the provisions of the Russian Civil Code on settlements upon the return of property from unlawful possession would apply (Art. 303 of the Russian Civil Code). The owner of the object would be entitled to recover the income received from lease of the property, and if the lessor had been acting in bad faith (i.e., was aware or should have been aware that he did not have the authority to lease out the object), then the owner of the object would be entitled to recover any income that the lessor had received or should have received for the whole period during which the object had been occupied. If the lessor had acted in good faith, then only the income that the lessor had received or should have received from the time he became aware or should have become aware of the unlawfulness of leasing out the property may be recovered.

VAS effectively broadened the scope of this provision of the Russian Civil Code on settlements upon the return of property from unlawful possession and stated that "a similar claim may be brought by an owner against a lessee who, in signing a lease contract, was aware that the other party did not have the legal authority to lease out the property". Furthermore, VAS stated that "if an unauthorized lessor and the lessee

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15 See, in this regard, in particular, Decree No. 10/22 of the Plenum of the Supreme Court of the Russian Federation and the Higher *Arbitrazh* Court of the Russian Federation, dated April 29, 2010.

16 This argument was taken from a specific case that was heard by the Presidium of VAS, in which the lessee – who did not perform his obligation to pay rent – cited the fact that he had received the property from a person who was not the titleholder of the property (Decree of the Presidium of VAS No. 13898/11, dated March 6, 2012, in Case No. A41-18028/10).

17 See paragraph 12, sub-paragraphs 1 and 2 of the Decree.

acted in bad faith, then they will be jointly and severally liable to the owner in respect of such claim".

Lease of immovable property prior to being commissioned

The Decree clarifies that it is possible to lease out immovable property prior to its being commissioned.[18] In this situation, VAS states that the existence or absence of a commissioning permit *per se* does not affect the obligations of the parties to a lease contract as between themselves or the ability of the lessee to occupy the lease property (e.g., to conduct repairs or fit-out).[19]

We also note that, in the case described above, there are theoretically two possible situations: such property may already be registered as a separate piece of real estate (so-called construction in progress) or it may not be registered. The Decree does not specify whether it refers in this case to the lease of construction in progress registered as a separate piece of real estate or to the lease of construction in progress that has not been registered as a separate piece of real estate.

It is our view that the Decree should cover both situations, because it is of fundamental importance that VAS has provided for the possibility of occupying real estate (within prescribed limits) before it has been commissioned.

VAS also emphasized that the operation of immovable property prior to its being commissioned should not breach town planning legislation. In the event of any such breach the offenders (lessor and/or lessee) could be held administratively liable.[20] VAS also states that the activities of such persons may be suspended on the grounds and in the manner prescribed by the Code of Administrative Offenses of the Russian

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18 Even before VAS issued the clarification, the courts had maintained the view that the lack of a commissioning permit upon the transfer of a property to the lessee did not give rise to invalidation of the lease contract. See, e.g., Ruling of FAC of the Moscow District, dated December 27, 2012, in Case No. A40-29392/12-53-268. However, in times gone by the courts have supported the position that lease contracts for immovable property executed before a commissioning permit is obtained are void by virtue of Article 168 of the Russian Civil Code. See, e.g., Ruling of FAC of the Far East District No. F03-1643/2012, dated May 4, 2012, in Case No. A59-3135/2011; Ruling of FAC of the North-West District, dated March 11, 2009, in Case No. A56-12329/2008.

19 Paragraph 11, sub-paragraph 2 of the Decree. In addition, it is anticipated that town planning legislation will be developed to provide for a considerable simplification of the formalized procedure for obtaining a commissioning permit (Resolution No. 1487-r of the Government of the Russian Federation on Approval of an Action Plan/Roadmap for Improving the Business Climate in the Construction Industry, dated August 16, 2012.

20 See Art. 9.5(5) of the Code of Administrative Offenses of the Russian Federation (this article provides for the imposition of an administrative fine on individuals ranging from RUB 500 to RUB 1,000; on company officers from RUB 1,000 to RUB 2,000; on legal entities from RUB 10,000 to RUB 20,000).

Federation. We note that, at present, this Code does not provide for such penalty for operation of immovable property without a commissioning permit as suspension of activities.

We also note that, in respect of the lease of property that has not yet been commissioned, VAS did not specify how such lease contracts are to be treated, and what happens to the obligations of the parties to such contracts after commissioning of the property and the acquisition of title thereto by the lessor. It is our view that the correct approach would be to deem the uncommissioned property, on the one part, and the commissioned property, on the other part, as two separate objects.

Consequently, the more balanced approach, in our view, would be to execute two separate lease contracts (for two different leased properties): lease of the uncommissioned property for strictly defined purposes (e.g., to conduct a fit-out), and lease of future property (to be occupied for the purpose for which it was intended). Instead of making two separate agreements, a more practical approach could be to enter into a single lease agreement combining the two elements (i.e., lease of the uncommissioned property and a future lease).

Lease of unauthorized construction and other cases

VAS stated explicitly that a lease contract for future property could not be executed with regard to unauthorized construction.[21] Such contract would in any event be void, since parties bound by civil law cannot assume obligations in relation to unauthorized construction. Furthermore, VAS emphasized that such contract would be deemed void even if it had been executed on condition of the subsequent recognition of the lessor's ownership title to the unauthorized construction.

In addition, VAS examined cases of the disposition of land plots that had been made available by their respective landholders on the basis of the right of permanent perpetual use. In accordance with the Land Code of the Russian Federation (the "Land

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[21] In accordance with Art. 222 of the Russian Civil Code, unauthorized construction is defined as "a residential building or other structure or construction or other real property erected on a land plot that has not been allocated for these purposes as prescribed by law or other regulatory acts, or erected without obtaining the required permits or with material violations of town planning and building standards and rules". See also Information Letter No. 143 of the Presidium of the Higher *Arbitrazh* Court of the Russian Federation "Review of Court Practice on Certain Matters Related to the Application by *Arbitrazh* Courts of Article 222 of the Civil Code of the Russian Federation", dated December 9, 2010.

Code"), no disposition (including sale, lease, etc.) of such land plots is permitted.[22] VAS referred to this prohibition and indicated that a lease contract for a future land plot signed by a person with a right of permanent perpetual use of such land plot and intending to buy out the land plot and subsequently lease it to someone would be deemed void.[23]

It is not quite clear why VAS has taken such a tough stance on this issue. On the one hand, the Land Code does indeed prohibit the disposition of land plots granted to persons under a right of permanent perpetual use. On the other hand, we believe that such prohibition is aimed at the disposition of the right of permanent perpetual use at the present time, and not disposition of a land plot in the future should the right of permanent perpetual use be converted into title or leasehold.

We recall that, in accordance with the introductory act to the Land Code, the majority of landholders of land plots with the right of permanent perpetual use were supposed to have converted their right to leasehold or to have acquired ownership title to such land plots by July 1, 2012. (Holders of land plots with transportation, communications and utilities lines situated on them are supposed to do this by January 1, 2015.)

Given that VAS has allowed the lease of future objects, this prohibition (especially if a landholder with the right of permanent perpetual use intends to buy out the respective land plot and subsequently lease it to someone) is not all clear.

STATE REGISTRATION OF LEASES

Amendments to civil legislation in respect of state registration of leases

It is anticipated that the provisions of the Russian Civil Code on leases will undergo some revision in the course of the reform of civil legislation. In particular, the deletion from leases of elements of proprietary right (such as the right of first offer to renew a lease contract (Art. 621.1 of the Russian Civil Code) and follow-on right in the event of the transfer of ownership title to real property (Art. 617.1 of the Russian Civil Code)) is being discussed, the idea being that a lease should consist purely of clauses that are

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22 Thus, Art. 20.4 of the Land Code of the Russian Federation implicitly provides that contracts that envisage the disposition (including future disposition) of a land plot owned by a person on the basis of the right to permanent perpetual use are not permitted.

23 See paragraph 10, sub-paragraph 5 of the Decree.

binding in nature. We note that these amendments to the Russian Civil Code have not yet been adopted.[24]

In this regard, lawmakers had planned to abolish the requirement for state registration of lease contracts, because following the logic of these changes to the Russian Civil Code, (i) state registration, first and foremost, protects the interests of third parties in relation to the elements of proprietary right of a lease, (ii) such elements of proprietary right of a lease will be eliminated and, consequently, (iii) there will no longer be a need for state registration of a lease.

Following this line of reasoning, lawmakers adopted Federal Law No. 302-FZ on Amendments to Chapters 1, 2, 3 and 4 of Part One of the Civil Code of the Russian Federation, dated December 30, 2012, pursuant to which amendments were introduced to the Russian Civil Code which, *inter alia*, abolished the rules requiring state registration of a range of agreements related to the disposition of real property (including lease contracts for real estate).[25]

However, these amendments brought no changes to the rule established in Federal Law No. 122-FZ on State Registration of Rights to Real Property and Transactions Therewith, dated July 21, 1997, (as amended) ("Law on State Registration"), which states that state registration is required not only for the lease contract itself, but also for the lease as an encumbrance on immovable property.[26] Technically speaking, the above amendments were not concerned with defining a lease as an encumbrance on immovable property requiring state registration, and did not introduce any other rules in this regard.[27]

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24 These draft amendments had a first reading in the State Duma on April 27, 2012. See http://asozd2.duma.gov.ru/main.nsf/%28SpravkaNew%29?OpenAgent&RN=47538-6&02. After the State Duma voted on November 16, 2012 to divide the draft of the Russian Civil Code into bundles and to adopt these separately throughout 2013, this draft has not been changed but, to date, it has not yet undergone any subsequent readings.

25 See Art. 2.8 of Federal Law No. 302-FZ, dated December 30, 2012. These provisions of the law came into effect from March 1, 2013 and apply to agreements executed after the entry into force of the law.

26 See the definition "restrictions/encumbrances" in Article 1 of Federal Law No. 122-FZ on State Registration of Rights to Real Property and Transactions Therewith, dated July 21, 1997 (as amended). In accordance with this definition, a lease is an encumbrance on immovable property.

27 The State Duma Committee on Civil, Criminal, Commercial and Procedural Legislation subsequently explained that a lease is subject to registration as an encumbrance on immovable property. See Letter No. 3.3-6/94 of the State Duma Committee on Civil, Criminal, Commercial and Procedural Legislation, dated January 22, 2013, on State Registration of Transactions with Immovable Property in the Context of the Entry Into Force from March 1, 2013 of Federal Law No. 302-FZ on Amendments to Chapters 1, 2, 3 and 4 of Part One of the Civil Code of the Russian Federation, dated December 30, 2012. We note, however, that such clarifications are not binding.

It was, thus, assumed that the abolition of state registration would follow from the elimination of the elements of proprietary right from a lease. However, in practice, the requirement for state registration of a lease was abolished before the amendments to the Russian Civil Code relating to lease took effect, but it was neither complete nor consistent. So, in order to avoid any further confusion, it was decided to revert to the former regulatory environment in respect of state registration of lease contracts.

Therefore, the State Duma passed Federal Law No. 21-FZ on Amendments to Certain Legislative Acts of the Russian Federation and Repeal of Certain Provisions of Legislative Acts of the Russian Federation, dated March 4, 2013, which restored the rule on state registration of lease contracts for immovable property to the Russian Civil Code.[28]

In contract to the inconsistent legislative amendments described above, the Decree comprises a logical regulatory framework that most closely adheres to the logic of making a lease purely contractually binding in nature.

Provisions of the Decree relating to state registration of a lease

The clarification on issues of state registration provided in the Decree relates to a situation that was quite widespread in practice. This was a situation where the parties would sign a lease contract for immovable property for a period of one year or more, but such contract, for one reason or another, was not subsequently registered. In accordance with the civil law provisions in force prior to the above amendments to the Russian Civil Code, such lease contract would not take effect. The parties could duly perform such contract (the lessee would have unimpeded access and use of the leased property and would pay rent as agreed by the parties), i.e., effectively consider themselves bound by the contract.

However, if any disagreements arose between the parties (e.g., with regard to the rental amount) and such disagreements were brought before a court, the court would have found such contract null and void, and applied the rules on unjust enrichment to the parties, thus depriving the parties of the right to any other legal remedies that may

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[28] The relevant amendments were made to Art. 2.8 of Federal Law No. 302-FZ, dated December 30, 2012.

have been provided for in such lease contracts (such as the right to sue for contractual penalty).[29]

This meant that both parties were not sufficiently protected: the lessee could lose the use of the leased property (in the event of breach on the part of the lessor), and the lessor could receive less than the agreed rent, but be unable to seek the legal remedies against the lessee provided for in the contract (in the event of breach on the part of the lessee).

VAS changed this approach and stated in the Decree that if the parties have reached agreement on all of the material terms of a lease contract, but such lease contract does not undergo state registration, the lease contract shall be deemed null and void only in relation to third parties. For the parties to the contract, the property should be used and the corresponding payment effected in accordance with the obligations assumed by each party to such contract. Therefore, such lease contract will remain in effect for the parties, but the lessee will not have the right of prior claim in relation to third parties. This means, among other things, that the lessee will not be able to take advantage of the associated "proprietary effects" of a lease.

VAS emphasized that, in the event of a dispute in respect of such lease contract, the provisions of the Russian Civil Code on unjust enrichment do not apply.[30]

RENTAL PAYMENTS

Provision to revise the rent more than once per year

VAS explained that the rent may be revised more than once per year by agreement between the parties to a lease contract. Despite such provision seeming obvious, until the Decree was adopted, there was a certain ambiguity about whether or not the parties could (even by mutual agreement) revise the rent more than once a year.[31]

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29 See, e.g., Ruling of FAC of the West-Siberian District, dated November 29, 2012, in Case No. A46-3015/2012; Ruling of FAC of Volga-Vyatka District, dated August 19, 2011, in Case No. A43-20984/2010.

30 Thus, lessees that argue in court that a contract is null and void in order to be released from having to pay rent and penalty under a lease contract that has not undergone state registration will not be able to use the lessor's unjust enrichment as an argument in support of their position. (See, e.g., Ruling of FAC of the Far East District No. F03-9691/2010, dated January 31, 2011, in Case No. A51-23536/2009.)

31 This ambiguity arose, in part, from the interpretation of paragraph 11 of Information Letter No. 66 of the Presidium of VAS "Review of Dispute Resolution Practice in Relation to Lease", dated January 11, 2002 , in accordance with which the clause of a contract providing for the rental payment mechanism (a fixed price or formula for calculating the price) must remain unchanged for a year.

VAS also indicated that the rule whereby rent may be revised unilaterally not more than once per year (provided that such right of unilateral revision is even provided for in the contract) remains.

In addition, VAS included new clarification that the right of a lessor to unilaterally revise the rent may be restricted.

Thus, paragraph 22 of the Decree states that if a lease contract provides for the right of a lessor to unilaterally revise the rent, and the lessor exercises such right to increase the rent disproportionately to the rise in average market rates over the relevant period in respect of the lease of similar property in the local area and exceeds them to a substantial degree, then such action will be construed as abuse by the lessor of its right. In such case the court will be obliged to dismiss any claim to recover any portion of the rent in excess of the relevant average market rate.[32]

Premature termination of a lease contract if rent is not paid on time

Paragraph 23 of the Decree introduces another new rule. This refers to the right of the lessor to petition for premature termination of a lease contract in a court of law if the lessee does not pay the rent by the due date laid down in the contract more than two consecutive times.

Previously, the accepted practice was that if the lessee managed to effect the rental payment before the contract was terminated, the lessor forfeited the right to terminate the contract.[33]

VAS changed this rule. For a lease contract to be terminated, it is now sufficient that the rent payment not be made by the due date. Therefore, should the lessee fall behind on rent payments more than two consecutive times, the lessor will have the right to insist that the contract be terminated, regardless of whether the lessee discharges the debt or not. The only restriction on the lessor in this case is the period during which the lessor must make this demand. In accordance with the Decree, failure to present a demand for termination of a lease contract within a reasonable period after the lessee

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32 This clarification applies only in cases where rent is not regulated by the state.

33 See, e.g., Ruling of FAC of the Far East District No. F03-5744/2008, dated December 18, 2008, in Case No. A73-13355/2007-72; Ruling of FAC of the North-West District, dated December 23, 2010, in Case No. A05-6662/2010; Ruling of FAC of Volga-Vyatka District, dated August 7, 2009, in Case No. A43-30501/2008-13-753; Ruling of FAC of the Central District, dated April 7, 2011, in Case No. A14-6472/2010-128/8.

has paid its arrears in rent deprives the lessor of the right to demand termination of the contract.

We note that the Decree makes no reference to a similar right of the lessor in the event of a unilateral repudiation of a lease contract in accordance with civil law procedure. Nevertheless, accepted court practice allows the parties to agree and set forth in a contract a fairly broad spectrum of grounds for unilateral repudiation of a lease contract (and they do not necessarily have to be associated with breach by the lessee of the provisions of the contract).[34] Thus, it is our view that the parties may provide for similar (or even tighter) rules in a lease contract.

OTHER MATTERS

VAS also provided clarification on a number of other matters that arise in the course of lease of property:

- As regards so-called "double leases" (when two contracts are signed in respect of one and the same property)[35] VAS stated that such contracts are deemed valid, and any disputes between titleholders and lessees are resolved in accordance with Art. 398 of the Russian Civil Code (i.e., in accordance with the rules for the performance of an obligation in kind).[36] In this case, the lessee to whom the property was not transferred is entitled to claim compensation from the lessor for losses incurred and any penalty laid down in the contract (paragraph 13 of the Decree).
- If a leased object is not properly identified in a lease contract,[37] but the contract is effectively being performed by the parties (e.g., the object has been transferred to the lessee and there has been no dispute between the parties as to failure to duly

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34 In its Resolution No. 13057/09, dated February 16, 2010, in Case No. A40-87811/08-147-655 the Presidium of VAS confirmed that a contract could be unilaterally repudiated / unilaterally terminated if this was set forth in an agreement between the parties.

35 This rule does not apply in cases where lessees have the enjoyment of different parts of one and the same object, or where alternate lessees have the enjoyment of an object during alternating periods.

36 Pursuant to this provision, in the event of failure to perform an obligation to transfer an individually defined thing the respective creditor (in this case, the lessee) has the right to demand removal of the thing from the debtor (in this case, the lessor) and transfer to the creditor. This right lapses if the thing has already been transferred to a third party. If the thing has not yet been transferred, priority rests with that creditor in whose favor the obligation arose the earliest, and if this cannot be determined, the one that filed a claim earlier than any other.

37 In accordance with the position of the Private Law Administration of VAS, if real property has duly undergone cadastral registration and been assigned a cadastre number, specifying the cadastre number in the contract will be deemed sufficient identification of the leased property.

perform the obligations of the lessor in respect of transfer of the leased property), then this prevents the parties from challenging such contract, including arguing that such contract is invalid or null and void (paragraph 15 of the Decree).

- VAS also considered matters related to the renewal of lease contracts for state and municipal property without announcing a tender pursuant to Art. 17.1, sub-paragraphs 9-11 of Federal Law No. 135-FZ on Protection of Competition, dated July 26, 2006, and reviewed a set of issues in connection with rent-controlled lease contracts.
- If the lease contract for a land plot has expired at the time of filing of an application for state registration of title to construction in progress, this should not adversely affect the state registration of the construction in progress (paragraph 24 of the Decree). At the same time, if a legal expert review by the registration authority finds that a construction in progress does not exist as a discrete object (e.g., the foundation work on the property has not been completed in full, etc.), it is lawful to decline to complete state registration.

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We would be happy to answer any questions you may have regarding the above.

June 18, 2013