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William R. Siegel

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The Law "On the State Registration of Rights in Real Property": Encouraging or Deterring Foreign Investment in the Russian Federation?

*William R. Siegel**

I. INTRODUCTION

The Law "On the State Registration of Rights in Real Property" of July 21, 1997 (the "Registration Law" or "the Law") constitutes a major step towards the achievement of an effective national registration system and, concomitantly, a viable real estate market for foreign investors in the Russian Federation ("RF"). Prior to this law, foreign investors could not rely upon a formal system of state registration to protect their interests in real property.¹ To remedy this problem, the Registration Law creates a system that, at least on paper, is comparable to Western registration systems in its consistency, accessibility and certainty. However, the Russian reform process has consistently shown that plans which appear sensible and practical on paper are not always achievable in practice. Thus, one must view the Registration Law, like all ambitious reform plans in Russia, with a skeptical and cautious eye.

* J.D., Northwestern University, 1999; A.M., Harvard University, 1996; B.A., Wesleyan University, 1992. I wish to thank my parents, Richard H. and Madeleine Siegel, for encouraging my interest in Russia.

¹ Articles 131, 164 and 219 of the RF Civil Code of 1994 all state that ownership and other rights in real property will only be valid and protected by the relevant state institutions if they are registered in the "single state register." *See* RF Civil Code [hereinafter GK RF]. However, as is discussed below, the fact that no law creating a "single state register" was enacted until July 21, 1997 — almost three years after the Civil Code first made reference to it — demonstrates the great uncertainty underlying foreign investment in Russia. *See* RF Law No. 122-FZ "On the State Registration of Rights in Real Property" (on file with the author) [hereinafter Registration Law].

Under this heightened scrutiny, several aspects of the Registration Law appear problematic. First, the Law does not establish an adequate dispute resolution mechanism to deal with competing claims of authority among federal and subfederal governmental entities.² The absence of such a prescribed process could be particularly troublesome for foreign investors who have to deal with a wide variety of registration procedures throughout the different regions and jurisdictions of Russia. This trouble will merely add to the costs of doing business in an already tenuous investment climate. Second, the Law perpetuates the inefficiencies and corruption of the pre-existing system by not requiring the registration of those rights in real property recognized as legitimate prior to the new Law.³ This means that even though rights in real property obtained in transactions prior to the Law will be enforced by the state, there will be no public record of these rights. Thus, parties involved in future transactions with these unregistered properties will have the same difficulty in achieving security of title as they had before the Law. And third, by making the long-term lease subject to state registration, the Law solidifies the lease rather than private ownership as the dominant form of transaction in the Russian commercial real estate market; an outcome which could further delay, if not prevent, the right of legal entities to own land for commercial purposes.⁴ This development provides an additional disincentive to those foreign investors who are reluctant to make large investments in countries where they cannot obtain the security of at least owning the land on which their assembly plants, office buildings or hotels sit.

The Russian Federation should strive to create a registration system for rights in real property that is simple, consistent, accessible and certain. First, the rules and procedures should be as simple as possible in order to prevent the emergence of a cumbersome, rent-seeking bureaucracy that could accompany the creation of this new system. Second, these procedures should be administered in a consistent manner so that foreign and domestic real estate investors can plan the certain and expected steps they must take to gain security of title for their properties. Third, the registration system should be accessible and devoid of unnecessary secrecy in order to provide sufficient public notice of rights in real property. Such notice would serve to discourage competing claims to property that lack evidentiary support. Fourth, this system should provide a certainty of title enforced by the state so that investors in real property — whether from Russia or abroad — can be confident in the security of their investments. The creation of such a system would benefit foreign and domestic investors alike and provide a significant boost to the developing Russian market.

² See Registration Law, *supra* note 1, arts. 9, 33.

³ See *id.* art. 6.

⁴ See *id.* art. 2.

In analyzing the Registration Law's impact on foreign investors, this comment first discusses the U.S. title assurance system. This comment then lays out the features of a model title assurance system that would be appropriate for Russia. Next, this comment discusses the particular features of the Registration Law that will benefit foreign investors in Russian real estate. Finally, this comment highlights the provisions of the Law that may deter foreign investment in the Russian Federation.

II. WHAT KIND OF TITLE ASSURANCE SYSTEM FOR RUSSIA?

A. The U.S. Registration System

Investors in U.S. real estate seldom have to worry about defending their investments against competing title claims.⁵ In the United States, a comprehensive registration system for interests in real property is the main vehicle for achieving title assurance.⁶ Unlike in Russia, the U.S. system has developed at the subfederal level and, as a result, varies by jurisdiction, often at the county level.⁷ Despite this patchwork system, the U.S. title assurance system usually provides landowners with enough information to prove a chain of title. Records are maintained in the office of a county clerk or, in the absence of such a position, in the appropriate municipal or federal office.⁸ These records are filed most often in the name of the various titleholders rather than on a tract basis.⁹ The goal of the U.S. system is to provide those asserting title with enough evidence to prove the validity of their claim; a claim that, if proven, will be enforced by corresponding municipal and county institutions.¹⁰ Thus, the U.S. system is accessible because these records are open to all persons, regardless of whether someone is a party to one of the transactions along the chain of title. The system is also certain because if a chain of title is proven with sufficient evidence, then the assertion of this title will be enforced by the state.

Besides these registration procedures, the U.S. title assurance system provides investors with additional means for achieving title security. For example, many deeds include warranties, which provide transferees of property with a contractual guarantee that a title is valid.¹¹ In addition, title insurance has emerged as an important component of the U.S. title assurance system. Investors in U.S. real estate "are accustomed to using title insurance in any transaction involving the acquisition of real property rights

⁵ C. Dent Bostick, *Land Title Registration: An English Solution to an American Problem*, 63 IND. L.J. 55, 62 (1987).

⁶ See *id.*

⁷ See *id.*

⁸ *Id.*

⁹ *Id.*

¹⁰ *Id.*

¹¹ *Id.* at 63.

. . . ."¹² By providing investors with the security of knowing that they will be sufficiently compensated if their title proves defective, title insurance protects investors from the uncertainties of the title determination process. Thus, title insurance essentially transfers the risk of proving legitimate title from the investor to the title insurance company.¹³

B. Learning from the U.S. Example

The U.S. example shows how a title assurance system that is accessible in its procedures and certain in its results can provide a necessary cornerstone for a country's real estate market. In particular, the U.S. title assurance system is effective because it provides the security of title desired by investors. However, in striving to create sufficient security of title for real estate investors in Russia, lawmakers would be imprudent to establish a title assurance system that is identical to the U.S. system. Rather, Russia should craft a system that is tailored to its own bureaucratic realities and its traditional approaches to land and commerce. Nevertheless, Russia can learn from the flaws and inefficiencies of the U.S. system in its effort to build a title registration system that will create the security of title necessary to attract foreign investment.

Ideally, investors in the Russian real estate market would be faced with a comprehensive title assurance system which guaranteed them a maximum level of security of title for their investments. Like the U.S. system, an ideal Russian title assurance system would have registration procedures and records that were accessible to all parties. In addition, the procedures of this ideal system would result in a finding of title that was supported by ample evidence and enforced by the state.

However, unlike the U.S. system, an ideal system would recognize only a limited number of interests in land. Title registration in the United States is burdened by the wide range of ownership (fee simples, life estates, joint tenancies, etc.) and possessory rights recognized by various subfederal jurisdictions. The complexity of U.S. property law adds to the confusion and, thus, the cost of the title search process.¹⁴ If the number of interests in real property were reduced, then the registration and record-keeping of these interests would be more manageable and less costly.

In addition, an ideal title assurance system would be administered by a bureaucracy that is better trained to fulfill its duties than the U.S. bureaucracy. In the United States, the selection of officials to administer the title assurance system is too often based upon political criteria rather than a

¹² Hugh A. Brodkey, *Land Title Issues for Countries in Transition: The American Experience*, 29 J. MARSHALL L. REV. 799 (1996).

¹³ Bostick, *supra* note 5, at 62.

¹⁴ *Id.* at 69.

person's professional training or competence.¹⁵ Thus, the nature of this bureaucracy adds to the U.S. system's inefficiency and cost.

C. The Obstacle of Russian History

The successes and failures of Russia's economic reforms demonstrate that governmental programs and practices cannot merely be transplanted from one country to the next. Rather, the manner in which a country's government operates is most often a reflection of its traditions and cultural attitudes. Thus, any reforms which are in complete opposition to these traditions and attitudes run a great risk of failure.¹⁶

Russia faces a particularly difficult task in creating a title assurance system to undergird its commercial real estate market because for most of the 20th century the private or commercial ownership of land in Russia was prohibited. As a result, there is little, if any, history to fall back on or to serve as a guide by which to construct this new system of procedures and institutions. Prior to the Bolshevik Revolution, only the wealthiest and highest classes of society could own land.¹⁷ Once the Communists took over, one of their first steps was to nationalize the land and exterminate an entire class of landowners.¹⁸ In fact, over the next seven decades of Soviet rule, land remained the exclusive domain of the state, and was excluded from what little private commercial activity was permitted.

With the collapse of the Soviet system in December 1991, the role of private entities in the Russian economy began to change. The most important change concerning the right of nonstate actors to own and possess rights in real property occurred when the RF Constitution was passed by nationwide referendum in December 1993. Article 36(1) of the RF Constitution states that "[c]itizens and their associations shall have the right to possess land as private property."¹⁹ While Article 36(3) stipulates that the "terms and rules for the use of land shall be fixed by a federal law," it remains unclear whether both commercial entities and individuals were included under the rubric of "[c]itizens and their associations" under Article 36.²⁰

¹⁵ *Id.*

¹⁶ This is demonstrated by the large public outcry which greeted the Yeltsin government's price liberalization and privatization programs in 1992. See RICHARD SAKWA, *RUSSIAN POLITICS AND SOCIETY* 233 (1993). Among the most common complaints in the popular press about these programs was that they were designed by Western academics who gave no consideration to Russia's unique history and attitudes towards wealth and private property. *Id.* at 215. Thus, a reform program that might be successful in a small South American country would not necessarily achieve the same results in Russia. *Id.*

¹⁷ William G. Frenkel, *Private Land Ownership in Russia: An Overview of Legal Developments to Date*, 3 PARKER SCH. J.E. EUR. L. 257 (1996).

¹⁸ *Id.*

¹⁹ RF Constitution (1993).

²⁰ *Id.*; Frenkel, *supra* note 17, at 259.

It is also unclear whether foreigners, as commercial entities or individual investors, can own land. For example, while Article 35(2) of the Constitution states that "[e]veryone shall have the right to have property, possess, use and dispose of it both personally and jointly . . .," there is no provision in the Constitution which states whether the word "[e]veryone" includes foreign entities or individuals.²¹

The implementation of Part One of a new Civil Code in October 1994 only added to the confusion of whether private entities and individuals, both foreign and Russian, could own real property in the Russian Federation. Articles 131, 164 and 219 of the Civil Code all state that ownership and other rights in real property are valid only if they are registered in the "single state register maintained by legal agencies."²² Similarly, Article 165 of the Civil Code states that the failure to register any rights in real property will invalidate that right as well as the transaction which created or conveyed it.²³ However, at the time this Civil Code was implemented, no such "single state register" even existed. In fact, this rather puzzling scenario — in which investors were obligated to comply with procedures which did not even exist — existed for nearly three years until President Yeltsin signed the Registration Law. Such is the adventure of doing business in Russia.

III. THE REGISTRATION LAW: IMPLICATIONS FOR FOREIGN INVESTORS

A. A Review of the Law: Its Key Provisions and Procedures

The Registration Law establishes, in general terms, the procedures by which rights in real property may be recognized and, thus, enforced by the Russian state. The sections which include the fundamental concepts and rationales underlying the Law and the definitions of key terms are particularly important. A review of these definitions and concepts allows for a deeper understanding of how the Law impacts foreign investment in Russia.

The underlying principles and concepts of the Registration Law are laid out in Article 2.²⁴ The basic objective of the Law is enunciated in this article's first sentence, which states that the "state registration of rights in real property and transactions with it . . . is a legal act of the acknowledgment by the state of the origin, limitation (encumbrance), transfer and termination of rights in real property."²⁵ This article states further that "[s]tate registration is the only evidence of the existence of a registered right."²⁶ If the state recognition of rights in real property, whether they be of Russian or foreign entities, is indeed achieved over time, then foreign investors will

²¹ RF Constitution.

²² GK RF.

²³ *Id.*

²⁴ See Registration Law, *supra* note 1.

²⁵ *Id.* art. 2(1).

²⁶ *Id.*

be able to ensure the security of title for their investments and the Law itself will be considered a success. However, if the provisions of the Registration Law are overly broad or contradictory in their phrasing or in the procedures which they establish, then the resulting system is likely to be manipulated by local elites. As a result, foreign investors would be further discouraged from incurring the great risk of investment in Russia.

Investors in the Russian real estate market are likely to ask who is subject to the Registration Law and what types of rights in real property must they register. Article 5 defines those subject to the Law as the "owners of immovable property and holders of other rights to it."²⁷ This group of "owners" and "holders of other rights" includes "citizens of the Russian Federation, foreign nationals and stateless persons, Russian and foreign legal entities, international organizations, foreign states, the Russian Federation and its subjects and municipal bodies."²⁸ This provision represents a significant change from an earlier draft version of the Registration Law which exempted federal and municipal ownership from registration.²⁹

To answer any questions about which interests must be registered, one must know specifically what types of property are included within the Russian notion of real property.³⁰ Article 1 provides this information by defining real property as "land plots, subsoil lots, separated water resources and all the facilities connected with land so that their movement without disproportionate prejudice to their purpose is impossible."³¹

In order to understand exactly how these rights in real property will be registered, one must also have an understanding of a cadastre number. Article 1 of the Law defines a cadastre number as a "unique, never repeated . . . number of an object of realty, which is conferred on it during cadastral or technical record-keeping."³² For example, the cadastre number of a building or structure consists of both the cadastre number of the land plot on which the building sits and the inventory number of the building itself.³³ The cadastre numbers will be designated by the appropriate judicial body within each registration area which is charged with the responsibility under local and federal law of registering rights in real property.³⁴

²⁷ *Id.* art. 5.

²⁸ *Id.*

²⁹ See *Real Estate, Development and Construction White Paper on Real Estate Reform in the Russian Federation*, American Chamber of Commerce in Russia, June 1996 at 13 (on file with the author) [hereinafter *Real Estate, Development and Construction White Paper*].

³⁰ This comment assumes that "real property" and "real estate" are synonyms.

³¹ Registration Law, *supra* note 1.

³² *Id.*

³³ *Id.*

³⁴ These registration areas correspond to the 89 individual subfederal jurisdictions within the Russian Federation, more commonly known as oblasts, krais and republics. RF Constitution, art. 65.

Under Article 12 of the Registration Law, these cadastre numbers and other materials relating to the registration of rights in real property will be contained within a single state register of rights.³⁵ This register will be divided into sections which will be opened when a party initiates the process for registering an object of immovable property.³⁶ These sections will include "information about the existing and terminated rights" to these objects as well as "data on the said objects and information about right-holders."³⁷ These individual sections will also be divided into three subsections.³⁸ The first subsection will contain a "brief description of each object of immovable property" and other related information such as the property's address.³⁹ The second subsection will include information about the individuals or entities who have registered these rights in real property as their own.⁴⁰ For example, the address of the right-holder and the type of right, such as a lease or ownership, registered would be included in this second subsection.⁴¹ The third subsection will contain information about any limitations, such as servitudes or mortgages, on a right in real property as well as the term of this limitation and a reference to the particular transaction or document that created this limitation.⁴²

Once an interest in real property has been registered in accordance with the procedures described above, the holder of this interest will have the right to possess proof of this registration.⁴³ Article 14(1) states that the "origin and transfer of rights in real property shall be certified by certificate of state registration."⁴⁴ In addition, the "state registration of contracts and other transactions shall be certified by a special registration inscription on the document which expresses the content of the transaction."⁴⁵ While the forms for both the certificate and registration inscription have not been established, the Law points out that the certificates and inscriptions previously used by subfederal jurisdictions will be valid.⁴⁶

The registrar of rights in real property is charged with administering this registration process within each registration area.⁴⁷ Although the Registration Law states that the specific responsibilities of a registrar are still to be established by RF law, Article 15(1) stipulates that the appointment and

³⁵ See Registration Law, *supra* note 1.

³⁶ *Id.* art. 12(2).

³⁷ *Id.*

³⁸ *Id.* art. 12(6).

³⁹ *Id.*

⁴⁰ *Id.*

⁴¹ *Id.*

⁴² *Id.*

⁴³ *Id.* art. 14(1).

⁴⁴ *Id.*

⁴⁵ *Id.*

⁴⁶ *Id.* art. 14(2).

⁴⁷ *Id.* art. 15(3).

dismissal of each registrar at the subfederal level must be "authorized by the government of the Russian Federation, by agreement with the executive bodies of the subjects of the Russian Federation."⁴⁸ This provision ensures that, at least on paper, the federal government in Moscow will not have absolute control of the registration procedures. Rather, local, nonfederal elites will play some role (the extent of which has not been established) in the appointment of registrars in their respective jurisdictions. By virtue of this power (regardless of how large it turns out to be), the Registration Law guarantees an important role for local officials in the registration process as a whole.⁴⁹

The Registration Law also requires that registering parties submit the appropriate documents that "establish the presence, origin, termination, transfer and limitation . . . of rights in real property."⁵⁰ These documents should include a description of the property, the "type of registered right," and seals and signatures of a notary and the parties to the transaction.⁵¹ The Law stipulates that these documents be submitted in two copies, and that one copy of each document be returned to the party upon registration.⁵²

B. How the Registration Law Benefits Foreign Investors

The Registration Law is the first and most important step in the creation of a title assurance system in the Russian Federation. The Law will benefit foreign investors because, for the first time, there is now an established system by which these investors may, at least on paper, achieve security and certainty of title through procedures which are consistently applied and accessible to a wide range of nonstate actors.

In light of Russia's long history of state ownership of land, any foreign investor considering whether to invest in the Russian Federation would likely investigate what possible measures could be taken to protect an investment in real property from state expropriation or competing claims by other parties. As discussed above, a nationally-recognized registration system allows investors to comply with recognized procedures that, if followed, will result in certainty of title. However, in the absence of a nationally-recognized state registration system, national and local elites, and the bureaucracies which they oversee, play a central role in the administration of a system which is more arbitrary than certain. Moreover, in an arbitrary system, such as existed in Russia prior to the Registration Law, investors are likely to be discouraged by the heightened transaction costs

⁴⁸ *Id.* art. 15(1).

⁴⁹ A more extensive discussion of how center-periphery tensions might impact the registration process and foreign investors follows below.

⁵⁰ See Registration Law, *supra* note 1, art. 18(1).

⁵¹ *Id.*

⁵² *Id.* art. 18(5).

from bribery payments, which flourish in uncertain processes controlled by local elites and bureaucracies.

Thus, to lessen the uncertainty of the existing system, the Registration Law sets out to create a title assurance system in which those with interests in real property can achieve a certainty of title that will be enforced by the state. Article 2(1) of the Registration Law states that "[s]tate registration is the only evidence of the existence of the registered right . . ." and that disputes regarding these rights may be resolved solely through "legal proceeding[s]." ⁵³ This article sends an unambiguous and much-needed message to foreign investors: if they comply with the procedures of the Law and achieve registration of their interests in real property, their interests in real property will be recognized and protected by the state.

Another positive feature of the Registration Law for foreign investors is that it provides nonstate actors with access to examine registration-related materials. Such access is particularly important for foreign investors wishing to do a due diligence title search before risking a large sum of money in the Russian real estate market. Under Article 7(1) of the Registration Law, the "[s]tate registration of rights shall be open" and the "body which carries out the state registration of rights shall be obliged to submit information contained in the Single State Register of rights . . . to any person." ⁵⁴ This openness is particularly surprising considering earlier Russian legislation and a prior draft of the Registration Law. The RF Law "On Information, Informatization and Protection of Information" of January 25, 1995 (the "Information Law") restricted information, such as registration records, which, under Russian law, were solely the property of the entity which created or filed such documents. ⁵⁵ Like the Information Law, an earlier version of the Registration law prevented access to "transactional information" except for those parties who "own[ed]" this information. ⁵⁶

However, the final version of the Registration Law creates a more open title assurance system, though the extent to which this system has been opened is still somewhat unclear. Article 7(3) states that these records will be open only to "the right-holders themselves; to . . . persons who have received a power of attorney from a right-holder; to executive officers of the local self-government bodies" and to other government, tax and judicial officers. ⁵⁷ According to Article 8(1), the information contained in these records "shall be given for a charge unless the Law requires otherwise." ⁵⁸ The ambiguity in these provisions indicates that it is too early to know for sure whether these provisions provide foreign investors with sufficient access to

⁵³ *Id.* art. 2(1).

⁵⁴ *Id.* art. 7(1).

⁵⁵ See *Real Estate, Development and Construction White Paper*, *supra* note 29, at 12.

⁵⁶ *Id.*

⁵⁷ Registration Law, *supra* note 1.

⁵⁸ *Id.* art. 8(1).

title records. Nonetheless, it appears as if these records will at least be accessible to those foreign investors wishing to conduct due diligence in the Russian real estate market. As long as the party possessing the registered right in real estate grants a power of attorney to a foreign investor attempting to ascertain the title status, then the register would be sufficiently accessible.

In order to ensure that investors will have the necessary access to conduct due diligence and ultimately achieve certainty of title, the Registration Law takes steps so that its provisions are applied in a consistent manner at the subfederal level. Article 10 of the Registration Law states that the federal executive branch will set up the government bodies in charge of the registration process, appoint registrars and enforce the rules of the national register.⁵⁹ Thus, at least on paper, Article 10 would seem to provide sufficient oversight at the federal level to ensure that subfederal jurisdictions comply with the general procedures of the Registration Law. However, foreign investors should be aware that Russia has undergone a rapid process of federal disintegration since 1991, and that the 89 subjects (consisting of oblasts, krais, republics and federal cities) of the Federation often disregard the mandates of the federal organs when it is in their economic interest to do so. As a result, foreign investors should not assume that the Registration Law will be applied consistently across the Federation simply because the mechanisms for federal oversight appear to be in place. Instead, these investors must familiarize themselves with both the procedures spelled out in the Federal Law and the registration rules established by the subfederal jurisdiction where a particular property is located.

The Registration Law will also benefit foreign investors in two indirect ways. First, a federally-mandated registration system for rights in real property will help in the collection of real estate taxes at both the federal and local levels.⁶⁰ The description of a particular property contained in the single register will assist federal and local tax officials in the valuation of an entity's real estate interests.⁶¹ For Russia to be able to pay for its infrastructure and other social programs, such as the payment of soldiers, pensioners and the funding of its educational and cultural institutions, which are necessary for a stable investment climate, its tax regime must be based on accurate information.⁶² Thus, the information system created by the Registration Law will likely allow for increased revenues from the collection of property taxes and an improved investment climate for foreign investors. Second, the Registration Law will facilitate investment in the Russian real estate market by making it easier to "secure loans with collateral of measurable value."⁶³

⁵⁹ *Id.* art. 10.

⁶⁰ See *Real Estate, Development and Construction White Paper*, *supra* note 29, at 15.

⁶¹ See *id.*

⁶² See *id.*

⁶³ See *id.*

For example, a lending institution is more likely to allow an investor/borrower to collateralize a property for the purpose of obtaining a mortgage if it can rely on an accurate valuation of that investor/borrower's property interest.⁶⁴ A lending institution will also want to make sure that a borrower's claim to a particular collateralized property is secure. As discussed above, the Registration Law creates the apparatus to ensure that investors can achieve a security of title that is recognized and enforced by the state.

One might also argue that the greatest benefit of the Registration Law to foreign investors is the signal it sends to real estate entrepreneurs around the world. It has become somewhat fashionable over the years to belittle the prospects for foreign investment in Russia due to the weakness of state institutions and general lawlessness.⁶⁵ However, the implementation of the Registration Law, albeit some three years after the Civil Code called for its enactment, demonstrates that Russia's state institutions are aware of the necessary prerequisites for increased foreign investment. Although, as discussed below, the Law is imperfect in a number of key areas, the fact that a federally-recognized and enforced title assurance system now exists in the Russian Federation is no small feat considering the country's long (and even recent) history of prohibiting nonstate interests in real property. Thus, the Registration Law shows that Russia's state institutions are capable of addressing the needs of domestic and foreign investors.

C. How the Registration Law Impedes Foreign Investment

Despite the many positive consequences of the Registration Law which were discussed above, the Law is far from perfect. Indeed, there are several provisions and omissions which should give foreign investors cause for concern.

Perhaps the most troubling aspect of the Registration Law is its failure to prescribe a dispute resolution mechanism for the title determination process. The failure of the Law's drafters to establish a fixed set of procedures for resolving disputes over title is likely to lead to problems in a number of areas. The first of these problems will occur when disputes arise between federal and subfederal governmental organs. Under Article 10 of the Registration Law, the "federal executive body . . . [shall] exercise control over the implementation of the federal program of creating a system of state registration of rights in the subjects of the Russian Federation."⁶⁶ The "federal executive body" is also charged with "coordinat[ing] the work for setting up the bodies of justice responsible for the registration of rights; exercis[ing] control over the activity of these bodies" and, as was discussed

⁶⁴ See *id.*

⁶⁵ The author worked for a U.S. law firm in Moscow in 1997, and heard such comments from foreign and even Russian businesspeople on an almost daily basis.

⁶⁶ Registration Law, *supra* note 1.

above, "appoint[ing] registrars of rights in real property . . . and releas[ing] them from office by agreement with the executive body of a subject of the Russian Federation."⁶⁷ Thus, according to these provisions, the office of the presidency plays a central role in the implementation and operation of the registration system.

Another area of potential dispute between federal and subfederal organs may arise over the determination of how much those wishing to register their rights in real property will be charged. Article 11(2) stipulates that the "charge for registration . . . shall be collected in amounts set by the subjects of the Russian Federation."⁶⁸ The Law also grants the federal government the power to establish the "maximum amount" of these registration fees.⁶⁹ Article 11(3) states that revenues received from the registration process "shall be used solely for the creation, support and development of the state registration system."⁷⁰ In addition, no more than "five per cent of these charged payments" shall be distributed by subfederal jurisdictions to the federal government.⁷¹

Considering the perpetual nature of Russia's budget crisis, it seems likely that subfederal governments desperate for revenues will likely battle Moscow for the right to determine how much to charge for registration and what portion of these fees to keep for themselves. However, the Law does not state how a conflict between the central government in Moscow and the government of one of the Russian Federation's 89 subjects would be resolved. Considering Russia's recent history of center-periphery conflict and federal disintegration, this omission should be particularly troubling to foreign investors. In the early 1990s, Russia underwent a rapid process of decentralization, as many of the federal subjects declared their sovereignty from the center in an attempt to achieve greater economic and political independence.⁷² The war in Chechnya demonstrated the extent to which this center-periphery conflict could escalate.

Thus, in the context of these sovereignty movements, it is not difficult to imagine how the center could conflict with the subjects over the registration of rights in real property. Assume, for example, that federal and subfederal organs disagree over which particular entity is the rightful owner of a steel mill in Kazan, the capital city of the Russian republic of Tatarstan. If Moscow endorses the claim of a powerful industrialist with close ties to the Kremlin and local officials in Kazan back the bid of a regional industrialist with ties the Tatar president, then the ingredients for center-periphery conflict would be in place. Assume further that the registrar in Tatarstan at-

⁶⁷ *Id.*

⁶⁸ *Id.* art. 11(2).

⁶⁹ *See id.*

⁷⁰ *Id.* art. 11(3).

⁷¹ *See id.*

⁷² *See SAKWA, supra* note 16, at 179-200.

tempts to register the interest of the regional industrialist. Moscow would surely object, but it is not clear what constructive actions it could take. Moscow might attempt to replace the registrar with someone under its control, but Article 10 of the Registration Law stipulates that the center may dismiss the registrar only in "agreement" with the "executive bodies of a subject."⁷³ Similarly, if the registrar in Kazan sided with Moscow, then Article 10, as in the previous scenario, would prevent the Tatar government from replacing this official.⁷⁴ However, the Tatar government, as it did during its sovereignty movement of the early 1990s, might withhold tax revenues from Moscow or pursue other methods to exert its considerable leverage against the center. The point of these scenarios is simply to show how the absence of a dispute resolution mechanism in the Registration Law could lay the groundwork for future conflict between Moscow and the federation subjects.⁷⁵

Thus, the task for foreign investors is to do the necessary due diligence to avoid becoming embroiled in a center-periphery conflict over title. Indeed, if foreign steel company "X" concludes a transaction with the title-claimant backed by Moscow, and foreign steel company "Y" contracts with the title-claimant backed by Kazan, then at least one, if not both, of the foreign investors would lose their rights to the steel mill. These scenarios show that, in the continuing absence of a generally-accepted means by which to resolve such conflicts, foreign entities should be wary about concluding transactions involving property for which title is, or may conceivably be, disputed.

Another troubling aspect of the Registration Law is its recognition of pre-existing rights in real property. Article 6(1) of the Registration Law states that "rights in real estate which arose before . . . the present Federal Law . . . shall be recognized as legally valid in the absence of their state registration."⁷⁶ As a result of this provision, there will be no public record of those rights in real property obtained prior to the Law. Thus, parties involved in future transactions with these unregistered properties will have the same difficulty in achieving security of title as they had before the Law. For example, under this provision, a party claiming title to a property has no way of evaluating the possibility that competing claims to this property may emerge.⁷⁷ Even though individual "A" may be recorded in the register as

⁷³ Registration Law, *supra* note 1, art. 10.

⁷⁴ *See id.*

⁷⁵ It should be noted that Article 2(1) of the Registration Law states that the "registered right to real property may be disputed through legal proceeding alone." *See id.* Beyond this assertion, the law does not stipulate exactly what type of "legal proceeding" will resolve conflicts over title. Thus, by leaving both parties to a center-periphery dispute (or any other dispute) free to pursue their own favored "legal proceeding," this provision does not address the absence of a viable dispute resolution mechanism in the Registration Law. *See id.*

⁷⁶ *Id.*

⁷⁷ *Id.*

having a valid interest in a particular property, there is nothing to prevent individual "B" from claiming the same interest even after "A" has registered its own interest in the property. Under Article 6(1), "B" could merely claim that its interest was still valid even though "A" had gone ahead and registered its interest because the Registration Law recognizes the validity of pre-existing rights in real property even "in the absence of their state registration."⁷⁸ The failure of the Registration Law to address the prioritization of competing rights in real property serves to compound the danger of this provision for foreign investors.⁷⁹

In addition, this provision may leave parties somewhat unsure of whether their unregistered rights will be as "legally valid" as those rights which have been registered. Proof of this uncertainty is the fact that, regardless of what is stipulated in Article 6(1) of the Law, many foreign entities have attempted to register their rights in real estate obtained prior to the Law in order to provide an added safeguard for their investments.⁸⁰ This uncertainty translates into increased costs for these entities. For example, while working for a U.S. law firm in Moscow in 1997, this author spent several weeks preparing the registration materials for one Western company even though the lawyers in the firm did not know for certain whether this client's leases needed to be registered. One Russian lawyer in the firm, after rereading Article 6(1) of the Registration Law, instructed that the leases be registered "just in case." Thus, uncertainties in the Registration Law resulted in higher legal fees for investors in Russian real estate.

Foreign investors should also be concerned about the important role of bureaucratic structures in the administration of this new registration system. Under Article 9(3) of the Registration Law, the individual bureaucracies or, as the Law refers to them, "bod[ies] of justice" within each registration area will be responsible for officially registering rights in real property, issuing documents to registrants "confirming the state registration of rights," and releasing "information about the registered rights" to interested parties.⁸¹ In addition, these "bod[ies] of justice" will verify the "validity of the document" filed by registrants and investigate the "existence of earlier registered and claimed rights."⁸²

Thus, while the Registration Law charges these "bodies of justice" within each registration area with administering the procedures of Russia's new registration system, the Law does not stipulate exactly how these functions will be carried out or what oversight role will be played by the federal government. For example, Article 9(6) of the Registration Law states that the "model statute for the bodies of justice responsible for the registration

⁷⁸ *Id.*

⁷⁹ See *Real Estate, Development and Construction White Paper*, *supra* note 29, at 12.

⁸⁰ The author makes this observation on the basis of his work in Moscow in 1997.

⁸¹ Registration Law, *supra* note 1.

⁸² *Id.* art. 9(3).

of rights shall be endorsed by the Government of the Russian Federation.”⁸³ From this language, one would be reasonable to conclude that the individual registration areas will be free to establish their own administrative procedures, subject to the endorsement of the “Government of the Russian Federation.”⁸⁴ However, Article 10 attempts to clear up this confusion by creating a new “federal executive body” that will “coordinate the setting up of the bodies of justice responsible for the registration of rights.”⁸⁵ Article 10 stipulates further that this “federal executive body,” rather than the individual “bod[ies] of justice” at the subfederal level, will “ensure the observance of the rules for maintaining a single state register of rights; provide training and advanced training to the personnel employed in the system of state registration . . . [and] exercise control over the implementation of the federal program.”⁸⁶

Judging by the language of Articles 9 and 10 of the Registration Law, the lines of responsibility between federal and subfederal organs are not sufficiently demarcated to prevent bureaucratic clashes and chaos. While Article 9 seemingly gives the individual bodies of justice the implicit right to formulate their own bureaucratic procedures subject to federal approval, Article 10 then creates a separate “federal executive body” responsible for training the local bureaucracies and “exercis[ing] control” over the “implementation” of the new registration system.⁸⁷ Based on the language of Article 9, it is difficult to imagine how federal officials will be able to train local bureaucrats in procedures formulated at the local level. The ability of this “federal executive body” to oversee the subfederal bodies of justice is complicated by the Registration Law’s failure to spell out exactly how Moscow’s oversight responsibilities are to be achieved. Another problematic aspect of the Law is that it bases Russia’s new registration system on a cadastral system which still does not even exist.⁸⁸ Thus, in the confusion over the allocation of responsibilities between federal and subfederal bureaucracies, the Registration Law does not clarify which organ will create this cadastral system and ensure that the cadastre numbers assigned to individual properties will be based on some sort of uniform system.

Thus, foreign investors should be concerned about the institutional paralysis which is likely to result from a clash between federal and local bureaucracies. Earlier, this comment discussed the possibility of conflict between federal and local elites over competing claims to valuable properties. The potential clashes discussed here are of a different nature. These interbureaucratic disputes would result not as an outgrowth of Russia’s

⁸³ *Id.* art. 9(6).

⁸⁴ *Id.*

⁸⁵ *Id.* art. 10.

⁸⁶ *Id.*

⁸⁷ *See id.* arts. 9, 10.

⁸⁸ *See Real Estate, Development and Construction White Paper, supra* note 29, at 13.

long-standing center-periphery struggle, but rather from the Registration Law's contradictory provisions which would enable separate bureaucratic structures to base their competing jurisdictional claims in law. However, the different nature of these potential disputes would not prevent a local elite from relying on the seeming discretion allowed by Article 9 to exert even greater pressure on the center.⁸⁹ In this scenario, local bureaucracies would become little more than tools in an escalating center-periphery dispute that could lead to bureaucratic deadlock and the collapse of Russia's nascent registration system.

The risk of bureaucratic paralysis poses a great danger to foreign investors in Russia because it would leave unresolved the question of which rights in real property should be registered. One of the flaws of the U.S. title assurance system is that the wide range of ownership and possessory rights recognized by various jurisdictions adds to the confusion and, thus, the cost of the title search process. In Russia, the situation is even more complex because there is great confusion, particularly among foreign entities, over exactly which kinds of ownership and possessory rights are permitted in various jurisdictions. Article 1 of the Registration Law states that "land plots, subsoil lots, separated water resources . . . buildings, structures . . . forests and perennial plantations, condominiums and enterprises as property complexes" will be subject to state registration.⁹⁰ However, the Law does not state which types of ownership and possessory rights will be recognized as legitimate by the state. In fact, the federal government has given its subfederal jurisdictions great leeway in determining which particular ownership and possessory rights they will allow. In Moscow, for example, there is no private ownership of land, but merely lease agreements between the Moscow city government and lessees, whether they are individuals or commercial entities.⁹¹ By statute, land is leased to "juridical persons and individuals" for a maximum term of five years for short leases and fifty years for long leases.⁹² Thus, the Moscow city government allows individuals and commercial entities to conclude long-term leases, but does not allow them to own land. The continuing unwillingness of the federal government to establish that commercial entities can own land throughout RF territory — regardless of what any subfederal jurisdiction may declare — solidifies the long-term lease agreement as the dominant form of transaction in the Russian real estate market. This outcome will diminish the appeal of the Russian real estate market to those foreign investors who prefer the security that comes from owning, rather than leasing, the land on which their investments sit.

⁸⁹ See Registration Law, *supra* note 1, art. 9.

⁹⁰ *Id.*

⁹¹ See Hiroshi Oda, *Law of Lease in Russia*, in *THE REVIVAL OF PRIVATE LAW IN CENTRAL AND EASTERN EUROPE* 323, 336 (George Ginsburgs et al. eds., 1996).

⁹² *Id.* at 336.

As this section has discussed, the Registration Law poses a number of problems to foreign investors in Russia. While the Law itself represents a significant first step towards the achievement of a viable title assurance system in Russia, the Law does little to eliminate troubles in a variety of areas, most notably in the sphere of center-periphery relations. Any discussion of these problems begs the question of what else is needed to facilitate the development of a viable title assurance system in the Russian Federation. If, for example, additional means for achieving title security were developed, then perhaps foreign investors would not have to rely solely on the provisions of the new Registration Law. In the United States, warranty deeds and title insurance serve this purpose, but they were developed at common law and by nongovernmental commercial entities. Thus, if such methods for achieving title assurance are to develop in Russia, they will likely have to evolve in a similar fashion, outside the governmental sphere.

Nonetheless, Russia's state institutions could still play a role in providing greater security of title for foreign investors. For example, there is a great need for federal legislation which specifically grants foreign individuals and entities the right to own land for commercial purposes. In addition, this legislation should include provisions which address how the state will ensure security of title for foreign investments in Russia. However, it is highly unlikely that this type of legislation, which would contradict the fundamental policies of the nationalist and communist factions which control the State Duma, could be passed by the Russian parliament as it is currently composed.⁹³ Thus, in the continuing absence of such legislation, foreign investors will be faced with an insecurity of title which will serve as a disincentive to investment in Russia.

IV. CONCLUSION

This comment discusses whether the Registration Law contributes to the achievement of a viable title assurance system that will encourage foreign investment in the Russian Federation. The Law should be seen as a significant step towards the creation of an effective national registration system because, for the first time in Russian history, there is now an established system by which foreign investors may, at least on paper, achieve security of title. The mere introduction of such a system, regardless of its numerous imperfections, demonstrates that Russian lawmakers are responsive to the needs of investors worldwide. Another positive feature of the Registration Law is that it provides foreign investors wishing to conduct a due diligence title search with sufficient access to registration-related materials.⁹⁴ In addition, Article 10 of the Registration Law appears to provide adequate oversight at the federal level to ensure compliance and consistent

⁹³ The Russian parliament, or Federal Assembly, is composed of an upper house, the Federation Council, and a lower house, the State Duma. RF Constitution, art. 95.

⁹⁴ See Registration Law, *supra* note 1, art. 7(1).

application of the Law within Russia's 89 subfederal jurisdictions.⁹⁵ Finally, the implementation of a registration system at the federal level will assist tax officials in the valuation of real estate interests and, thus, benefit Russia's ailing tax collection efforts.⁹⁶ Similarly, lending institutions are now more likely to allow an investor/borrower to collateralize property for the purpose of obtaining a mortgage because it will be able to ascertain a more accurate valuation of that investor/borrower's property.⁹⁷

However, the problems this law poses for foreign investors are numerous. First, the Law does not establish a dispute resolution mechanism to deal with competing claims of authority among federal and subfederal governmental entities.⁹⁸ Second, the Law perpetuates the inefficiencies and corruption of the pre-existing system by not requiring the registration of those rights in real property previously recognized as legitimate prior to the new Law.⁹⁹ And third, by making the long-term lease subject to state registration, the Law solidifies the lease rather than private ownership as the dominant form of transaction in the Russian commercial real estate market.¹⁰⁰

Thus, the Registration Law fails to provide adequate security of title for foreign investors in Russia. Although the Law represents a step in the right direction, and it signifies that at least some Russian lawmakers are aware of the need to ensure security of title, the provisions of the Law simply do not go far enough. Additional legislation is needed that would clarify whether foreign individuals and entities have the right to own land for commercial purposes in the Russian Federation. In addition, federal and subfederal governmental organs need to reach an agreement about how disputes over competing claims to title will be resolved.

⁹⁵ See *id.* art. 10.

⁹⁶ See *Real Estate, Development and Construction White Paper*, *supra* note 29, at 15.

⁹⁷ See *id.*

⁹⁸ See Registration Law, *supra* note 1, arts. 9, 33.

⁹⁹ See *id.* art. 6.

¹⁰⁰ See *id.* art. 2.

