



Overview of Changes in the Regulation of Shared Equity Construction

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Amendments to the regulations governing shared equity construction came into force on 25 December 2018¹. Alongside changes in the requirements for developers, there has been a significant shake-up of the rules governing financial arrangements for projects carried out using funds attracted from private individuals.

This overview examines the most significant changes affecting the market as a whole.

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¹ The following have been amended: Federal Law No. 214-FZ "Concerning Participation in Shared Equity Construction of Apartment Buildings and Other Items of Immovable Property and Concerning the Introduction of Amendments to Certain Legislative Acts of the Russian Federation"; the Housing Code of the Russian Federation; Federal Law No. 127-FZ "Concerning Insolvency (Bankruptcy)"; Federal Law No. 218-FZ "Concerning the State Registration of Immovable Property"; Federal Law No. 218-FZ "Concerning the Public Company for the Protection of Rights of Citizens Who Are Participants in Shared Equity Construction in the Event of the Insolvency (Bankruptcy) of Developers and Concerning the Introduction of Amendments to Certain Legislative Acts of the Russian Federation"; Federal Law No. 175-FZ "Concerning the Introduction of Amendments to the Federal Law " Concerning Participation in Shared Equity Construction of Apartment Buildings and Other Items of Immovable Property and Concerning the Introduction of Amendments to Certain Legislative Acts of the Russian Federation" and Certain Legislative Acts of the Russian Federation"

Opening of Escrow Accounts

As from 1 July 2019, developers will have no option but to use escrow accounts when raising funds from investors for the shared equity construction of apartment buildings or other facilities that have not been put into use at the time the funds are raised. The requirement for funds to be paid into an escrow account will now apply to projects in which a shared equity agreement signed with any investor is submitted for state registration after 1 July 2019².

There is an exception to this rule for shared equity agreements concluded in relation to an apartment building and/or another facility that meet criteria set by the Government regarding the level of completion of the project and the number of shared equity agreements concluded. The Government has yet to set those criteria.

A developer not covered by that exception must open an escrow account with an authorized bank from a list to be approved by the Central Bank on a monthly basis. Where a developer has used a targeted loan to fund the construction of an apartment building or other facility, investors' funds must be paid into escrow accounts with the authorized bank that provided the targeted loan. If the targeted loan has been refinanced, money from investors who concluded an agreement with the developer after the date of the refinancing agreement must be paid into an escrow account with the refinancing bank.

Settlement Account

A developer must hold a separate settlement account with an authorized bank for each construction permit. Developers may not hold more settlement accounts than they have construction permits.

The developer, technical supervisor and general contractor must open bank accounts with one and the same authorized bank and use only those accounts for settlements with each other.

The requirement for a technical supervisor and a general contractor to open a settlement account with the same authorized bank as the developer does not apply where they have agreements with a developer that received a construction permit before 1 July 2018.

Details of the opening or closure of a settlement account of a developer that received a construction permit before 1 July 2018 must be posted online by that developer, stating the number of the account and the name and details of the authorized bank (taxpayer identification number, main state registration number), not later than one working day after the opening or closure of the account occurred.

Requirements for a Developer

The requirements regarding a developer's experience have been eased, making it sufficient for a developer to have had experience (at least 3 years) of participation in the construction (creation) of apartment buildings with a total aggregate floor area of no less than five thousand square metres.

In addition, new financial stability ratios will come into effect from 28 March 2019 for developers that do not place investors' funds in escrow accounts, including:

- ▶ the liability coverage ratio
- ▶ the targeted use of funds ratio

For developers who received a construction permit after 1 July 2018, there is also an internal funds ratio.

Conclusion of Shared Equity Agreements

After receiving a permit to put an apartment building and/or another facility into use and before that building and/or other facility undergo state cadastral registration, a developer has the right to conclude shared equity

² Previously, this requirement would only have applied to projects in which the first shared equity agreement was submitted for state registration after 1 July 2019

agreements in relation to shared equity units that are not the subject of other shared equity agreements.

Such agreements are not subject to requirements regarding the payment of contributions to a compensation fund and the use of an escrow account.

This change does not apply to developers that received a construction permit before 1 July 2018.

Targeted Loans

The newly amended Law on Shared Equity Construction now includes a definition of targeted credit (a targeted loan) and stipulates that a developer has the right to borrow funds in the form of a targeted loan from any founder/participant of the developer.

Developers that received a construction permit before 1 July 2018 remain subject to the restriction on the raising of targeted loans whereby only the developer's parent company may act as the lender.

Targeted Use of Funds

The new rules afford broader scope for the use of funds paid into a developer's settlement account. A developer that received a construction permit after 1 July 2018 may now also use funds in its settlement account for the following purposes:

- ▶ credit-related payments, interest and principal payments on targeted loans (other than a forfeiture (fine, penalty) for breach of the terms of a targeted loan agreement)
- ▶ payment of costs associated with the maintenance of residential and non-residential premises and parking spaces, including utility payments, from the day on which a permit to put them into use is received, if no ownership interest has been registered for the premises concerned

A new condition is laid down with regard to the placement of temporarily disposable funds on deposit with an authorized bank: the deposited funds and interest accrued on them must be paid back to the settlement account of the developer from which they were transferred.

Monitoring by an authorized bank of correspondence between the stated purpose and amount of payments will cease after the following conditions have all been met:

- ▶ the apartment building and/or other facility has been put into use
- ▶ state registration of ownership has taken place in relation to one shared equity unit within each apartment building and/or other facility built under one construction permit
- ▶ supporting documents have been provided to the authorized bank

State Monitoring

Scheduled inspections of developers have been eliminated under the new rules. There are, however, new grounds for regulatory bodies to carry out unscheduled on-site inspections:

- ▶ the expiry of the time limit for carrying out an instruction to remedy a violation of statutory requirements relating to the attraction of funds from individuals for the construction of apartment buildings and/or other facilities, if that instruction has not been carried out
- ▶ the discovery, in the course of analysing a developer's quarterly reports on activities involving the raising of funds from shared-equity investors, accounting statements and the project declaration, of indications of violations of mandatory requirements prescribed by laws governing participation in the shared equity construction of apartment buildings and/or other facilities
- ▶ a deviation of six months or more from the projected schedule for the execution of a construction project
- ▶ a request from a public prosecutor to carry out an unscheduled inspection by way of checking compliance with the law in response to information received by public prosecution bodies

Liability of a Developer's Beneficiaries

Changes in the rules governing the liability of beneficiaries mean that a beneficial owner now

bears subsidiary liability together with the developer for losses caused to investors through their fault.

Posting of Information on the Housing Construction Information System

New requirements have been introduced regarding the posting of information on the Unified Housing Construction Information System. The changes affect developers, the State Registration Service (Rosreestr) and the operator of the unified state register of expert reports.

In particular, developers that received expert reports on planning documentation and engineering survey results before 1 July 2018 are required to post the planning documentation and survey results on the Unified Housing Construction Information System.

Rosreestr's duties now include posting information on the cancellation of an entry in the Unified State Register of Immovable Property concerning the state registration of a shared equity agreement.

The operator of the unified state register of expert reports is obliged to post on the system:

- ▶ information on expert reports on planning documentation and engineering survey results and on the planning documentation and engineering survey results that were submitted for expert appraisal
 - ▶ expert reports on planning documentation and engineering survey results and the planning documentation and engineering survey results based on which those reports were prepared
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New Powers of the Investor Protection Fund

For the purpose of assessing whether a developer is capable of fulfilling obligations to shared equity investors, the Fund has been granted powers to inspect developers, including by carrying out on-site inspections, for which

purpose they may engage appraisers and civil engineering experts.

Such inspections may be carried out in relation to developers that meet criteria set by the Government and in relation to companies within the same group as those developers.

Non-Commercial Organization of the Fund

To finance and implement measures needed to complete unfinished construction projects and infrastructure facilities for the construction of which money was raised from shared equity investors, the Fund may set up a non-commercial organization, constituted as a fund, to which the developer's assets would be transferred, including rights in plots of land with inseparable improvements situated on them, infrastructure facilities, plots of land (rights in plots of land) intended for the siting of infrastructure facilities and obligations to investors.

Required Loan Provisions

Effective from 5 February 2019, the amount of required provisions for loans granted to developers that use escrow accounts may be determined on the basis of the borrower's level of creditworthiness, assigned on the basis of criteria set by the Bank of Russia.

There are four levels of creditworthiness:

- ▶ high
- ▶ adequate
- ▶ satisfactory
- ▶ weak

The amount of required provisions will vary from 1 to 100% depending on the assigned level.

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