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In this issue

Presidential Decree Tightens Government Control Over Russian Strategic Sector Companies

by **Laura M. Brank** and **Andrey Dukhin**

The President of Russia on September 11, 2012, issued a decree (the Strategic Company Decree) requiring Russian companies included in the list of strategic enterprises (Strategic Sectors Companies) to obtain government approval prior to carrying out certain actions with foreign governments/organizations. Many believe that the Strategic Company Decree was passed in response to growing pressure from the European Commission to obtain information on Gazprom in connection with a competition investigation into Gazprom's activities in the EU, but the Strategic Company Decree will have much wider implications and will create uncertainty for companies operating in the strategic sectors in Russia.

Under the Strategic Company Decree, Strategic Sectors Companies are now required to seek government approval prior to: (a) providing information on their activities or the activities of their associated companies to foreign governments/organizations; (b) amending agreements concluded between them and/or their associated companies and foreign contractors; and (c) alienating their stake or the stake of their companies in foreign organizations, assigning rights for conducting entrepreneurial activity on the territory of a foreign state or alienating immovable property situated abroad. The Strategic Company Decree does not, however, identify which government agency would grant such consent or the procedure for doing so, thereby in effect stopping the flow of information regarding such companies and hindering other activity of such companies until a procedure is established. According to the Strategic Company Decree, the government agency responsible for granting such consents should be determined by the Russian Government by October 11, 2012.

The Strategic Company Decree exempts information that is subject to publication or disclosure under Russian law or under the requirements provided for issuance, circulation and acquisition of securities. Therefore, Strategic Sectors Companies may continue to publish their reserves and other information that may be necessary to comply with local securities law requirements.

Although the Russian government has always played a prominent role with respect to Strategic Sectors Companies, these new barriers constitute yet another nuance for companies investing in the strategic sectors in Russia. It remains unclear as to how the Strategic Company Decree will be implemented in practice, but in the interim Strategic Sectors Companies will need to consider whether disclosure of information or changes to business activities will require government consent. We will, of course update you on further developments affecting Strategic Sectors Companies.

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ETFs Finally Come to Russia


by **Evgenia Korotkova** and **Kirill Skopchevskiy**

Recent changes to the legislation on investment funds will finally provide the much needed basis for the formation of exchange-traded funds (ETFs) under Russian law. Until recently, all investment funds in Russia were either open-, closed-ended or blended type, and investors were bound by a rigid agreement with an investment manager, thus limiting the investors' ability to promptly react to changing market conditions. The new amendments to the Russian Federal Law "On Investment Funds" set forth in Federal Law No. 145-FZ "On Amendments to Certain Legislative Acts of the Russian Federation," dated July 28, 2012, introduce the concept of an ETF and outline the principal rules that will apply to trading in ETFs.

The amendments, which became effective on September 1, 2012, delineate four categories of persons dealing with ETFs in Russia: owners of shares (units) in an ETF; persons authorized by an ETF manager (the Authorized Person, whose functions are discussed below); designated stock exchanges; and market makers.

The principal difference between an ETF and a traditional Russian unit investment fund is that the owner of a share in the ETF has the right to demand that an Authorized Person buy all or a portion of the owner's shares in an ETF, as well as the right to sell the shares on a designated stock exchange on the terms set out in the ETF management rules (the Rules), which must be registered with the Russian securities regulator, the Federal Service for Financial Markets. An Authorized Person who is also the owner of the shares in an ETF has the right to demand that the ETF manager buy out either all of the Authorized Person's shares in the ETF on the terms set out in the Rules, thereby terminating the agreement between the Authorized Person and the ETF manager, or a portion of the ETF's shares held by the Authorized Person.

Authorized Persons, who may either act as intermediaries between the owner of shares in an ETF and the buyer/seller of the shares, or may themselves be the owners of the shares in an ETF, must be specifically named in the Rules. The Rules must also name the Russian stock exchanges where shares in an ETF are admitted to trade and where the market makers are obliged to maintain the price, supply, demand and the volume of shares in the ETF. The same entity can act as an Authorized Person and a market maker for a particular ETF. Prior to the state registration of the Rules and the admission of the ETF shares to trade, a stock exchange must enter into an agreement with the persons who will act as market makers for a particular ETF. Russian ETFs can be traded on a foreign stock exchange, subject to the rules of such foreign stock exchange.

In order to maintain the price level for a particular ETF, the Rules provide that the price for which a market maker may purchase/sell the shares in an ETF cannot deviate by more than 5% from the estimated price of these shares, which must be stated in the Rules.

It remains to be seen how popular ETFs will become with investors, particularly those based outside of Russia who already have access to Russia-focused ETFs, such as, for example, the Market Vectors® Russia ETF and the Market Vectors® Russia Small-Cap ETF. However, analysts cautiously expect that the new legislation will increase investment in the Russian securities market, as well as provide greater protection to investors due to the greater transparency of ETFs as compared to traditional funds currently present in the Russian market.

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RF Legislation Expands Government Control Over Cyberspace

by **Andrey Dukhin**

A number of federal laws have been amended recently to address inappropriate and harmful website content available in Russian, such as websites providing details on how to commit suicide, prepare illegal drugs and naming places where drugs can be purchased, or which include images featuring the sexual abuse of children, and sites that solicit children for pornography (Offensive Material). Site owners will be required to shut down websites containing Offensive Material and

in cases where this is not possible, internet providers will be responsible for blocking access to the offensive sites.

On July 28, 2012, Federal Law No.139 - FZ "On Introducing Amendments to the Federal Law "On the Protection of Children Against Information that Harms Their Health and Development" and Other Legislative Acts of the Russian Federation" (the Law on Amendments) came into force.[1] The Law on Amendments introduced a number of changes including:

- Creating a unified register of domain names (Register), which would include internet sites with Offensive Material and information prohibited in the Russian Federation, such as information on extremism or terrorism, etc.;
- Introducing five categories for rating website content, limiting access for minors to inappropriate information. The categories are separated by age ranges for children (a) under 6 years old, (b) over 6, (c) over 12, (d) over 16, and (e) over 18 (i.e. prohibited for children). Content producers or distributors are required to clearly mark their content with the appropriate age category logo; and
- Provisions for expert opinions to rate informational content have been clarified and expanded.

The Procedure for Including a Website Into the Register

In order to be blocked, a website must first be on the Register. The Law on Amendments outlines two ways for getting a website on the Register (a) by a decision of the federal service that controls and supervises mass information, mass communications, information technologies and networks in relation to a certain website spreading harmful information and/or (b) by a court decision.

Once the website is on the Register, the hosting operator must inform the owner of the site that it must remove the offensive page from the website within 24 hours after the Register operator has notified the hosting provider regarding the offensive site. Within 24 hours after receiving this notification from the hosting provider, the owner of the website must delete the offensive page. If the notified owner of an offensive site does not delete the offensive page within 24 hours of being so notified, the hosting provider must block access to it.

[1] Certain provisions of the Law on Amendments will enter into force on November 1, 2012.

If the above actions required from the hosting provider or the owner of the website are not performed, the web address of the site with harmful information will be included on the Register. Within 24 hours of being included on the Register, the hosting provider of the website will be obliged to restrict access to the website. The decision to include a website on the Register may be appealed in court within three months.

A website on the Register can be removed from the list on the basis of (a) a court decision or (b) an application from the internet provider, hosting provider or owner of the website, provided that the harmful information has been removed. Once approved for removal, the website should be removed from the Register within three days.

The Law on Amendments was adopted to address the increasing number of websites with prohibited content and to limit the availability of such sites to children. However, there is a certain level of ambiguity as to the practical implementation of the Law on Amendments, which should be clarified during the implementation of the amendments.

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Russian Authorities Reconsider Their Approach to Increasing the Charter Capital of Financially Unstable Companies

by **Elena Ivankina**

Until recently, Russian authorities mandated that financially unstable joint stock companies (JSCs) which are required to decrease their charter capital or be liquidated under Russian law, may not subsequently increase their charter capital. However, in 2012 this view was finally reconsidered when the Federal Service on Financial Markets (the FSFM) addressed this issue in its Informational Letter No. 12-DP-03/12363 on March 27, 2012 (the Letter).

The FSFM has confirmed that if a JSC whose assets have fallen below its charter capital increases its charter capital, the increase *per se* will not be considered a violation of Russian law. This change in the FSFM's position allows greater flexibility

for JSCs to resolve their financial problems, as this issue frequently arises in Russia. It should be noted, however, that the Letter does not have any binding effect on Russian courts. Thus, it is yet to be determined when Russian courts will adopt this new approach and reflect it in court practice.

Actions Required to Be Taken if Net Assets Are Negative or Insufficient

Under Russian law, the value of the net assets of a JSC may not be lower than the amount of the charter capital of that JSC. This requirement applies to JSCs starting from the second fiscal year after incorporation and for each consecutive fiscal year. If the value of the JSC's net assets falls below the amount of the charter capital, Russian law provides for certain corporate actions that a JSC must take in order to rectify the deficiency. These actions vary depending on whether the amount of the charter capital meets the statutory requirements for the minimum amount of charter capital:

- **If the Net Assets Exceed the Minimum Statutory Threshold**
  If, at the end of the second or any subsequent fiscal year, the net asset value of a JSC falls below the amount of its charter capital (the Year of the Decrease) but still exceeds the minimum amount of the charter capital required by law, the JSC is required to take the following actions. First, the JSC must ensure that the annual report of the JSC includes information on the state of its net assets and the measures that the JSC intends to take to increase its net assets. Further, during the year following the Year of the Decrease (the Reporting Year), the JSC is required to monitor, and if necessary, report on the status of its net assets. In particular, if at the end of any quarter of the Reporting Year the difference between the net assets and the amount of the charter capital exceeds 25%, the JSC must publish information on the decrease of its net assets. Publishing the information is required in order to inform the JSC's creditors that there has been a decrease in its net assets and to provide them with the option to demand acceleration of the obligations of the JSC or, if early performance is impossible, termination of such obligations and compensation for damages. If, after the Reporting Year, the issue with the net assets remains unresolved, the JSC should either decrease its charter capital or call for its liquidation. The decision on the course of action of the JSC must be adopted within six months after the end of the Reporting Year.
- **If the Net Assets Fall Below the Minimum Statutory Threshold**
  If the amount of a JSC's net assets falls below the minimum amount of the charter capital required by law, then the JSC must call for its liquidation. The decision to liquidate must be adopted within six months after the end of the Year of the Decrease.

New Approach to Increasing the Charter Capital

Previously, it was not entirely clear whether a JSC, which under Russian law was required to decrease its charter capital or be liquidated in such instances, could increase its charter capital and issue new shares in order to rectify the situation. The FSFM took a conservative position and deemed such actions in violation of Russian law, even denying state registration of the issuance of new shares based on those grounds.

However, the FSFM has recently reconsidered its position, as reflected in the Letter. The FSFM has clarified that financial difficulties should not affect the legal standing of a JSC.

Under Russian law, the failure to remedy the financial state of a financially troubled JSC may only trigger the following consequences: (i) the creditors of the company may demand acceleration of the obligations or, if early performance is impossible, termination of such obligations and compensation of damages; and (ii) tax authorities and other authorized persons may claim liquidation of the JSC in court. However, it should be noted that the risk of liquidation in court is generally remote. As a general rule, courts tend to deny such claims from the tax authorities if a JSC is duly performing its obligations to creditors, pays its taxes, etc. If such JSCs do not commit any gross violations of law, the courts consider the insufficient/negative level of net assets to be evidence of a distressed financial state, which should not automatically entail liquidation.

The FSFM emphasized that even if a JSC is required to decrease its charter capital or to be liquidated, it may still adopt corporate resolutions, enter into transactions and take other actions to improve its financial state. Moreover, Russian bankruptcy laws expressly provide insolvent companies with the right to increase their charter capital, which is considered a measure aimed at improving their financial state. Accordingly, a joint interpretation of the requirements of Russian bankruptcy and corporate law suggests that if a JSC that is facing financial difficulties decides

to increase its charter capital, such actions *per se* should not be considered in violation of Russian law.

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Significant Changes to Summary Proceedings in Russian Arbitrazh (Commercial) Courts Adopted


by **Yuri Makhonin** and **Maryana R. Batalova**

Russian law allows arbitrazh (commercial) courts to grant summary judgments when the claim is uncontested, acknowledged by the respondent or when the claim amount is not financially significant.

Federal Law No. 86-FZ "On Amending the RF Arbitrazh Procedure Code Due to the Development of Summary Proceedings" (the Summary Proceedings Law)[2] was adopted in June of this year and will substantially change the implementation of summary proceedings in arbitrazh courts. In this article, we review the most important and interesting changes to summary proceedings that were introduced by the Summary Proceedings Law.

Disputes That Qualify for Summary Proceedings

The following disputes may be subject to summary proceedings:

- claims to recover funds not exceeding 300,000 Rubles (appr. $10,000) for legal entities and 100,000 Rubles (appr. $3,000) for individual entrepreneurs;
- certain administrative and public relations disputes, particularly, administrative liability cases where the sole penalty is an administrative fine not exceeding 100,000 Rubles (appr. $3,000) and cases on recovery of mandatory payments and sanctions not exceeding 100,000 Rubles (appr. $3,000);
- claims based on documents submitted by the claimant establishing the respondent's monetary obligations, regardless of the claim amount, which the respondent has acknowledged but did not fulfill, and/or on documents confirming contractual debt; and
- claims based on a notary protesting a bill for non payment, to accept or to date acceptance.

Upon mutual consent of the parties, other disputes may also be considered in summary proceedings, if there are no intervening circumstances, such as a third party joining the process, the risk of disclosing a state secret or a breach of the lawful rights of third parties, the necessity to appoint an expert or to hear witness statements, the risk of a miscarriage of justice where summary proceedings are granted or the necessity to clarify additional circumstances and research additional evidence. The Summary Proceedings Law does not regulate how the parties may give consent for their case to be decided by summary proceedings (for example, if that consent can be included in a contract or if consent must be granted immediately before referring the case to the court or during the court proceedings).

Certain categories of cases, such as corporate disputes and class action lawsuits may not be considered in summary proceedings.

The Procedure for Considering a Case in Summary Proceedings

As a general rule, judges must consider summary proceedings cases individually within two months after a claim has been filed with an arbitrazh court.

The judge considering a summary proceedings case establishes the deadlines for the parties to submit their objections to the claim and evidence in the case. If a party submits an objection, new evidence or other documents after the expiration of the term set forth by the judge, these documents will not be considered by the judge and will be returned, unless the submitting party is able to justify the delay for not submitting its documents within the established term for reasons outside of its control.

Information technologies and the internet are widely used in considering summary proceedings cases. To grant access to electronic case material a judge will send the parties information giving them access to the electronic database with the case materials. After the supporting documents are submitted to court for consideration, they are placed on a secure webpage on the official website of the arbitrazh court; this page is only accessible to the case participants.

[2] The Summary Proceedings Law will come into force on September 26, 2012.

After the term expires for submitting evidence and documents, the judge considering the case in summary proceedings issues a judgment without summoning the parties for a hearing. No preliminary court hearing is held, no transcripts are recorded and consideration of the case may not be stayed or continued.

The Procedure and Timeframe for Appealing a Summary Judgment

A summary judgment is subject to immediate enforcement. However, an appellate court has the authority to suspend enforcement of a judgment if the appealing party either provides evidence of the irreversibility of the decision's enforcement or provides counter security.

The term for appealing a summary judgment is brief. It may only be appealed in the appellate court within 10 business days after it has been issued. In addition, an appeal may only be considered in an appellate court by a judge individually on the basis of the evidence available in the court files.

The judicial act in a case considered in summary proceedings may also be appealed to an arbirazh court of the cassation instance, but only on the basis of a limited number of procedural grounds, such as improper composition of the court, undue influence by persons not involved in the proceedings, or failure to sign a decision or the signing of a decision by a judge not named in the decision.

Conclusion

The amended summary proceedings are yet another step towards introducing expedited procedures in Russia. This procedure should decrease the burden on judges and should facilitate faster and more efficient resolution of small claims and/or uncontested disputes. In addition, the procedure will minimize court expenses, particularly expenses for lawyers and travel, allowing the parties to resolve commercial disputes in all courts in Russia by electronically submitting documents through the Internet.

It's possible that summary proceedings may become widely used in the sphere of banking and finance, allowing for the recovery of debt from borrowers to a fast and efficient manner. We would expect that banks and financial institutions may try to include clauses mandating the use of this procedure in their standard contracts.

On the other hand, the Summary Proceedings Law may lead to a significant restriction of procedural rights that are currently available to parties to a dispute. Certain disputes that may be considered in such proceedings could be very important for the businesses but the involved parties would not have the opportunity to properly present their case in court.

However, if a party does not want to have its case heard in summary proceedings, it may prevent its case from being heard in such manner by:

- expressing its objection to the procedure (in cases when such consent is mandatory); or
- creating circumstances preventing the consideration of a case in summary proceedings (involving third parties to the proceedings, petitioning for the appointment of an expert or summoning witnesses, or referring to a potential miscarriage of judgment, etc.).

We will, of course, only know how efficient and rational these proceedings are once the Summary Proceedings Law has had a chance to be implemented in practice.

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NCO's Engaging in Political Activity to be Treated as Foreign Agents Under New Law

by **Tatiana Kozlova**

On July 20, 2012, the Russian President signed a highly controversial law that will impose heavy restrictions on foreign funded non-commercial organizations which participate in "political" activity. Potential state oversight will include frequent audits and spot checks and will require NCOs to publicly identify themselves as "foreign agents."

These developments are set forth in Law No. 121-FZ "Amendments to Certain Legislative Acts with Regard to Regulating the Activity of Non-Commercial Organizations Fulfilling the Functions of Foreign

Agents" (the NCO Amendment Law), amending the "Law on Public Association, the Law on Non-Commercial Organizations and Other Legislative Acts." The NCO Amendment Law has received a significant amount of coverage in the press and is also frequently referred to as the law on non-governmental organizations (the NGO Law).

Notably, there has been a lot of discussion over the possible implications of the NCO Amendment Law on organizations whose aim is to protect/report on human rights, such as Amnesty International, Human Rights Watch, Transparency International, etc., as well as the effect on recent social activism in Russia and the government crack down on protests and public meetings.

Under the NCO Amendment Law, a Russian NCO which receives funding from foreign sources and engages in any type of political activity is required to:

- identify itself as a "foreign agent" by registering with a "foreign agents" register; and
- abide by much stricter state control of its finances and other business activities.

"Foreign agent" NCOs (as well as their structural subdivisions) will be obliged to file: (a) a report on the expenditure of funds received from foreign sources on a quarterly basis, (b) a report on the composition of their managerial bodies on a semiannual basis, and (c) annual audit reports. They also must publish the above information on the internet or in other mass media sources on a semiannual basis.

The term "political activity" is defined very broadly. Under the NCO Amendment Law, an NCO is deemed to be participating in political activities in Russia if, irrespective of the purposes and objectives specified in its foundation documents, it participates (including by means of financing) in organizing and holding political events in order to influence the state authorities to make decisions aimed at changing existing state policy, as well as in forming public opinion with the same purpose.

An NCO will face criminal prosecution for a failure to comply with the requirements envisaged by the NCO Amendment Law.

Specifically:

- if an NCO willfully fails to submit documents required for it to be entered in the "foreign agents" register, its representatives will be subject to penalties of up to 300,000 rubles (appr. $10,000), or compulsory community service of up to 480 hours. In addition, if circumstances permit, more severe penalties may be imposed, i.e., correctional labor or imprisonment for up to two years.
- if an NCO encourages people "to refuse fulfilling their civic duties, or to commit other unlawful acts," it will be subject to a penalty of up to 200,000 rubles (appr. $7,000), or up to three years of restricted freedom (without imprisonment), or compulsory labor for up to three years, or imprisonment for the same period for its officers. The individuals in charge of such an NCO will be subject to similar penalties.
- religious or public associations that encourage or involve violence or other activities harmful to the health of others, including the individuals managing such associations, will be subject to a penalty of up to 300,000 rubles (appr. $10,000), or up to four years of restricted freedom (without imprisonment), or compulsory labor for up to four years, or imprisonment for the same period.

Activities relating to the following are exempt from the NCO Amendment Law:

- science, arts and culture;
- public healthcare and social assistance;
- protection of mothers and children;
- promotion of a healthy lifestyle, physical culture and sports;
- environmental protection; and
- charitable activities and activities promoting philanthropy and volunteerism.

The NCO Amendment Law enters into force 120 days after publication, i.e., on November 11, 2012.

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Draft Law to Raise Quota of Foreign Ownership in the Charter Capital of Insurance Companies


by **Elena Ivankina** and **Elvira Danilova***

Under Russian law, there is currently a statutory 25% cap on total foreign ownership in the aggregate charter capital of Russian insurance companies (the Quota).

If the Quota reaches its limit, the activity of Russian insurance companies that are either subsidiaries of foreign investors or controlled by foreign investors through ownership of more than 49% of their charter capital may be significantly affected. For example, such companies will not be able to receive new insurance licenses, increase their charter capital by means of foreign investors or subsidiaries or sell their shares to foreign investors.

The Quota is calculated by the RF Federal Service for Financial Markets (the FSFM) as of January 1 of each year as the ratio of the total capital owned by foreign investors in the charter capital of Russian insurance companies to the aggregate charter capital of such insurance companies taken as a whole (including Russian insurance companies).

The results of the Quota calculation for 2012 became available on March 6, 2012, when the FSFM issued Informational Letter No. 12-DP-11/8908 (the Informational Letter). According to the Informational Letter, as of the beginning of 2012, the Quota was not exhausted and was 18.1%. According to FSFM calculations, in 2012, foreign investors are free to invest RUB 11,607,500,000 in the charter capital of Russian insurance companies.

However, the amount available for investment calculated by the FSFM is not final and may change throughout the year. For example, in early June 2011, the Head of the FSFM, Mr. Dmitry Pankin, announced that the Quota for 2011 was met. Nevertheless, in 2011 some insurance companies still managed to receive approvals from the FSFM to increase their charter capital by the means of foreign investors because of the flow of foreign capital in the Russian insurance market and a subsequent increase of the amount available for foreign investment.

The Quota has restricted investment in the Russian insurance market and the barrier to entry was discussed during negotiations related to Russia's joining the World Trade Organization. To address the issue, a new draft law was submitted to the RF State Duma (the lower chamber of the RF Parliament). According to the draft law, the Quota would be increased from 25% to 50% for foreign ownership. The draft law is being considered in the first reading and, if passed in it first reading, would still need to undergo further approvals.

In general, the participants of the Russian insurance market welcome the potential increase in the Quota and consider it a very positive development. Increasing the Quota to 50% should increase investment in the sector and allow new foreign capital in existing entities.

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New Kazakhstan Law on Trunk Pipelines

by **Victor Mokrousov**

Kazakhstan has made a number of significant changes to its energy laws in recent years. It replaced the Subsoil Law and the Petroleum Law with a new Subsoil Law in 2010, which provided the government with greater authority in the regulation of extractive industries. This year was marked with the adoption of two new statutes: the Law on Gas and Gas Supply (on January 9) and the Law On Trunk Pipeline (the Law) on June 22. This article outlines some of the more important aspects and innovations of the latter.

Governance

The Law does not establish a clear test as to which pipelines may be deemed "trunk pipelines." However, the Law does determine which pipelines are not trunk pipelines: these are pipelines intended for

the transportation of products within the owner's territory for internal purposes, in particular, within the contractual territory of a subsoil user, as well as distribution pipelines.

The Law applies to trunk oil pipelines, gas pipelines and oil products pipelines. However, the Law applies to gas pipelines only to the extent not regulated by the Law on Gas and Gas Supply. In addition, the procedures for accessing gas transportation services (in contrast with oil transportation services) are still governed by the natural monopoly laws and regulations.

The Law does not contain any special provisions on tariffs. Tariffs are still regulated pursuant to the law on natural monopolies.

Title and Government Preemptive Right

A trunk pipeline may be state owned or privately owned. In the latter case, the owner must be a legal entity registered under the laws of the Republic of Kazakhstan.

Share or other equity interest in legal entities that are owners of a trunk pipeline as well as shares in the parent companies of such entities are deemed strategic objects (properties), and regulated by other laws accordingly.

The Government has a preemptive right to participate by at least 51% in the project of a newly created trunk pipeline. The Government may waive this right or decide to participate by less than 51%. The Government does not have a preemptive right in the expansion of an existing trunk pipeline.

Access Rights

If there is free capacity, a trunk pipeline owner or its operator must ensure equal conditions of access to that capacity for all eligible shippers.

If a pipeline capacity is limited, the capacity for oil transport is offered in the following order:

- to a shipper shipping oil to oil refineries in Kazakhstan;
- to a pipeline owner for transportation of its own products or the products of its affiliates;
- to a shipper fulfilling Government decisions and/or obligations under international treaties;
- to a shipper recruited for investment into the construction of a trunk pipeline and/or for the expansion of capacity within a line or facility where the investments were made, until the full recovery of its investment;
- to a shipper undertaking obligations to provide mandatory minimum annual oil volumes for transportation; or
- to a shipper transporting oil, the quality of which is adequate to comply with the technical requirements for the quality of oil to be transported by pipeline systems of other states.

National Operator

A national operator is a legal entity, the controlling stake in which belongs to the state, a national management holding or a national company. The national operator is designated as such by the Government and has the following rights:

- to render, within Kazakhstan, operator services for the trunk pipeline, where 50% or more of the voting shares (equity interest) of its owner directly or indirectly belong to the state, a national management holding or a national company; and
- to organized transportation via pipeline systems of other states of products transported from the Kazakhstan using a trunk pipeline owned by the national operator.

These rights may be exercised only by a national operator, unless the Government decides to grant these rights to another entity, in order to implement international treaties. In this case, 50% or more of the voting shares (equity interest) of such person must be owned by the state, a national management holding or a national company.

Other Innovations

The Law permits transporters to exchange products with one another (swaps) if there is a free capacity in one pipeline and a lack of capacity in another pipeline. These operations are allowed to ensure the delivery of oil to domestic oil refineries.

The Law contemplates the creation of a quality bank as a mechanism to carry out mutual settlements between shippers due to the differences in the quality of the product.

Conclusion

The Law is the first statute in Kazakhstan specifically designed to govern the development and operation of trunk pipelines. Investors in the petroleum sector should generally welcome greater clarity on access

rights, as well as the statutory recognition of swaps and quality bank arrangements.

Despite containing a number of innovations, such as the priority right of the Government to participate in pipeline projects from the outset, the Law does not represent a major shift in Kazakhstan policy. Adoption of the Law follows the overall trend of providing the government greater power in its dealings with petroleum investors.

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Amendments to Kazakhstan Competition Law

by **Aikerim Kaziyeva**

The Kazakhstan government has introduced a draft law to Parliament called "On Amendments and Additions to Certain Legislative Acts on Competition in the Republic of Kazakhstan" (the Proposed Competition Law). The Proposed Competition Law is intended to make significant changes to competition law and related transactions.

This article summarizes the most substantial changes and amendments provided in the Proposed Competition Law.

Increase in the Threshold of Transactions Subject to Antimonopoly Agency Approval

Under the current legislation, even relatively small-scale transactions are viewed as "economic transactions" subject to prior authorization by the Antimonopoly Agency if the following requirements are met:

- the total book-value of the assets of the market entities that are under reorganization (group of persons), or the total book-value of the assets of the acquirer (group of persons), and of the market entity shares (participation interest, unit shares) with the right of vote in whose charter capital are acquired, or their total volume of realization of goods for the last financial year exceeds two million times the monthly calculated index (MCI)[3] (appr. $21.6 million) on the day the application is submitted, or
- one of the transaction participants is an entity that has a dominant or a monopoly position in the particular market.

Under the proposed legislation, the threshold is increased to ten million times the MCI (appr. $108 million). Accordingly, certain transactions that were subject to prior authorization by the Antimonopoly Agency have been freed from that requirement.

New "Notice" Requirement (Substituting "Approval" Requirement) in Certain Economic Transactions

Under the current legislation, transactions are subject to authorization by the Antimonopoly Agency if the following requirements, among others, are met:

- an acquisition by a market participant of rights allowing such market participant to (a) issue mandatory executive orders to another market participant upon performance of its business activities, or (b) serve as the executive body of another market participant; and
- participation of the same individual(s) in the executive bodies, board of the directors, supervisory boards or other management bodies of two or more market participants if such individuals carry out management of the business activities of the said market participants.

Under the Proposed Competition Law, if one of the above requirements is fulfilled and the above-mentioned thresholds are met, it is only necessary to file a notice to the Antimonopoly Agency. Such notice should be submitted within 45 days after the completion of the respective transactions. The practical effectiveness of the proposed amendment should be further considered.

Definitions of "Direct" and "Indirect" Control Have Been Introduced

The existing competition law does not provide definitions for the terms "direct" and "indirect," which is a challenge for market participants that are planning M&A transactions. Since clear definitions are required to determine whether transactions will require prior approval of the Antimonopoly Agency.

[3] Monthly calculation index (MCI) is a variable index established by the Republican Budget Law for the purpose of calculating social benefits, taxes, other obligatory budgetary payments, fines, which as of the date of this article has the value of KZT 1,618 (or appr. $10.85 at the current exchange rate).

The Proposed Competition Law introduces the following definitions for direct and indirect control:

Direct control – is the ability of a legal entity or physical person to determine the decisions of another legal entity through one or more of the following:

- ability to perform functions of a governing body of the latter legal entity;
- the right to define terms for the business operations of the latter legal entity;
- control of 50% or more of the total voting stock (participation interest) in the initial capital contribution of the latter legal entity.

Indirect control – is the ability of a legal entity or an individual to direct the decisions of another legal person via one or several other legal entities that have direct control between themselves.

Definition of ''Group of Persons'' Has Been Amended

Under the current legislation, implementation of transactions (economic transaction), if such transactions occur within one group of persons, it is not recognized as an "economic concentration."

In this regard, please note that a group of persons, as a number of individuals and/or legal entities, includes the following:

1. a person who has the right to directly or indirectly (through third parties) control more than 25% of the voting stock of a legal entity;
2. a legal entity or several affiliated legal entities that can control the decision-making of a third person, including the decision-making with respect to performing business activities, or that can act as an executive body thereof;
3. an individual, his or her spouse, and/or close relatives that can control the decision-making of a third person, including decision-making relating to performing business operations, or that can act as an executive body thereof; and
4. persons, each belonging to the same group pursuant to any of the conditions stipulated in paragraphs 1–3 above, and other persons belonging to the same group with each of the said persons pursuant to any of the conditions stipulated in paragraphs 1–3 above. Such group of persons is treated as one market participant. Thus, the provisions of the law on competition pertinent to market participants are also applicable to groups of persons.

Furthermore, under the existing law, the additional acquisition of shares, if the acquirer controlled more than 25% before the acquisition, does not require prior approval, since the target entity (affiliated company) is considered to be in the same group as the acquirer.

Under the Proposed Competition Law, the threshold set forth in paragraph 1 above is increased to 50%. Provided that the Proposed Competition Law is adopted, affiliated entities that were previously considered a group of persons due to control of more than 25% of the voting stock, but not meeting the 50% threshold, will no longer be considered as part of one group of persons. This in turn, could lead to an increase in the number of notifications to the Antimonopoly Agency on the acquisition of the voting stock in an affiliated company (acquisition of the controlling share (51%) that effectively allows such market participant to issue mandatory executive orders to its affiliate on performance of its business activities even if before the acquisition the acquirer controlled more than 25%, but less than 50% of the entity's voting stock in its affiliate.

Anti-Competitive Policy Prohibition of Vertical Agreements

The Proposed Competition Law prohibits entering into vertical agreements between market participants that:

- fix or fix resale of products, except when the seller imposes a maximum resale price on the purchaser;
- prohibit the purchaser from selling the products of the seller's competitor. This prohibition does not extend to agreements on distribution of products sold under a trademark or another means of individualization stipulated by the seller or the manufacturer.

The new rules provide a basis for legal protection of the rights of consumers and purchasers from dominance of sellers in the circumstances described. We will continue following the developments of the draft law and will update you as it progresses through the legislative process.

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U.S. Adopts New Disclosure Rules for Natural Resource Companies Designed to Fight Corruption Overseas

by **Ruslan V. Koretski**

On August 22, 2012, the U.S. Securities and Exchange Commission (SEC) adopted new disclosure rules affecting oil and gas and mining companies listed on U.S. exchanges or otherwise reporting to the SEC, which may impact their operations in places like Russia. The new rules, mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, require "resource extraction issuers" to annually disclose certain payments made to the U.S. or foreign governments in connection with the commercial development of oil, natural gas and minerals (the Disclosure Rules). The Disclosure Rules, which are expected to apply to over 1,100 U.S. and foreign companies, are aimed at curbing corruption in oil-producing countries. The Disclosure Rules, by increasing transparency, are intended to work in tandem with the Foreign Corrupt Practices Act, which is also designed to fight corruption overseas.

The Disclosure Rules are to be set out in the new Rule 13q-1 and Form SD of the Securities Exchange Act of 1934. Compliance with the Disclosure Rules is required for fiscal years ending after September 30, 2013 and the first report need only disclose those payments made after September 30, 2013.

Companies That Must Disclose

The Disclosure Rules apply to "resource extraction issuers," which are U.S. and foreign companies listed on U.S. exchanges or otherwise reporting to the SEC that are (i) required to file an annual report with the SEC; and (ii) engaged in commercial development of oil, natural gas, or minerals. The disclosure requirements also cover indirect payments made by a subsidiary or another entity controlled by the resource extraction issuer. The resource extraction issuer will need to make a factual determination of whether it exercises control of an entity based on a consideration of all relevant facts and circumstances.

Payments That Must Be Disclosed

The Disclosure Rules require resource extraction issuers to disclose payments (i) made to the U.S. federal government or a foreign government; (ii) made to further the commercial development of oil, natural gas or minerals (which the SEC defines broadly as exploration, extraction, processing and export, or the acquisition of licenses for any such activity); and (iii) that equal or exceed $100,000 (made as a single payment or a series of related payments) during the most recent fiscal year.

Payments that must be disclosed include (i) taxes (including corporate profits, corporate income and production, but not VAT, personal income tax or sales tax); (ii) royalties; (iii) fees (including license fees, rental fees, entry fees and concession fees); (iv) production entitlements; (v) bonuses (including signature, discovery and production bonuses); (vi) dividends (other than those paid to a government as a common or ordinary shareholder); and (vii) infrastructure improvements. The Disclosure Rules do not cover social or community payments, such as payments to build a hospital or a school. If a payment subject to disclosure is made in-kind, the resource extraction issuer may report it at cost or, if the cost is not determinable, fair market value, provided that it presents a brief description of how the monetary value was calculated.

The term "foreign government" is defined broadly to include not only the foreign government directly (including a subnational government; department, agency or instrumentality of a foreign government), but also any company that is at least majority-owned by a foreign government. In the case of Russia, which has many active state-owned companies, this would for example include state-owned oil and gas giants such as Gazprom, Rosneft and Gazprom-Neft, and thus payments, which fall under the Rules, made to such companies, would need to be disclosed in accordance with the Disclosure Rules.

Any disclosure under the Disclosure Rules would need to be made on a project-by-project basis (rather than a country-level disclosure), describing the type, category and amount of payments, currency, financial period, the business segment that made the payments, the government that received the payments, the country in which the government is located and the project to which the payments relate. Although the term "project" is left undefined, the SEC views each contractual arrangement with a government as sufficient basis to consider it a project.

Reactions to the Rules

The Disclosure Rules have received mixed reactions from the industry. Although many human rights and business transparency groups are applauding the new disclosure requirements as the right step to curb

corruption and improve living standards in countries such as Russia, a number of industry groups have complained that the rules grant advantages to foreign competitors not listed in the U.S. (including most Russian companies) that do not have to make similar disclosures, especially if compliance with the Disclosure Rules will lead to disclosure of previously secret terms of the companies' arrangements with governments or their strategies on winning lucrative government contracts. The Disclosure Rules will also have an unintentional consequence of forcing companies to disclose information about regular payments made to business partners that happen to be state-owned companies. Since resource extraction issuers do not have to comply with the Disclosure Rules until next year, it remains to be seen how the new disclosure requirements will affect their operations in countries such as Russia.

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Legislative Update: Russia Officially Joins the World Trade Organization

by **Elvira Danilova***

Russia officially finalized all procedures required for accession to the World Trade Organization (the WTO) at the end of July 2012, becoming the 156th member of the WTO.

The Federal Law "On Ratification of the Protocol on Russia's Accession to the Marrakesh Agreement on the Establishment of the World Trade Organization of April 15, 1994" was passed by the RF Parliament, signed by the RF President and officially published at the end of July 2012.

On July 23, 2012, the RF Government officially notified the Secretariat of the WTO that all of the required domestic procedures have been finalized. In accordance with the WTO rules, Russia's accession to the WTO was completed on August 22, 2012, i.e. as of the 30th day following notification of the Secretariat of the WTO.

From September 1, 2012, Russia began performing its first obligation in accordance with the WTO protocol on decreasing average import tariffs. The average import tariffs will be gradually decreased until 2015 and will average about 6% in 2015, according to the RF Minister of Economic Development, Mr. A.R. Belousov.

**Elvira Danilova is a paralegal in Dechert's Moscow office.*

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Legislative Update: Updated Registration Procedure for Foreign Issuers

by **Evgenia Korotkova** and **Kirill Skopchevskiy**

The Russian securities regulator, the Federal Service for Financial Markets (the FSFM), has recently adopted legislation that outlines the registration procedures for prospectuses of foreign issuers which would like to admit securities for placement and/or public circulation in Russia, under Order No. 12-10/pz-n, dated March 6, 2012, (the Order). Prior to the adoption of this legislation, Russian regulations did not specify the procedure for registration of prospectuses of foreign issuers in Russia, thus effectively preventing foreign issuers from placing or publicly offering their securities to Russian investors. The Order fills this gap by specifying in detail the FSFM review process, providing a list of documents required for the registration and listing the grounds on which the registration may be denied. The Order must be officially published before it comes into legal effect; however, the exact date of publication has not yet been announced. We will keep you updated on further developments.

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Legislative Update: Increasing the Efficiency of RF Labor Legislation

by **Tatiana Kozlova**

Several changes have been introduced to the RF Labor Code over the last few months. The changes cover a wide range of issues from increasing the Russian winter holidays by two days; establishing employer accountability for salary payments and deductions on payment statements; allowing for a longer timeframe for athletes and coaches to notify their employers on terminating their employment contracts; to finally allowing for faster recovery of payments due to employees by their employers through expedited court proceedings.

Additional Holidays

January 6 and 8 are now officially included into the New Year Holidays. Starting from 2013, the New Year Holidays will last eight days, from January 1 to January 8 (including January 7, which is Orthodox Christmas). Increasing the number of days from five to seven will actually allow the duration of the New Year Holidays to be reduced, because now the last non-working day of the New Year Holidays will be January 8 and the two days during this period that fall on weekends (and were previously compensated by extending the New Year Holidays by two days) could now be transferred as holidays at a later time in the year (e.g., in May), as will be specified by the respective federal law or by a legislative act of the RF Government (Article 112 of the Labor Code was amended by RF Federal Law No. 35-FZ, dated April 23, 2012, which came into force on April 24, 2012).

Employer Accountability

Employers are now required to inform their employees of monetary compensation for delays (if any) when paying salaries as well as the following: (i) employee salaries; (ii) amount paid for annual leave; and (iii) balance due to the employer upon the employee terminating his/her employment; and/or (iv) other payments due to employees. Previously, employers only had to note the following when paying their employees; (i) constituent parts of the salary; (ii) deductions and the grounds for making them; and (iii) total amount due to the employee. (Article 136 of the Labor Code was amended by RF Federal Law No. 35-FZ, dated April 23, 2012, which came into force on April 24, 2012).

The amount of information that employers need to present to their employees is increasing, consequently, employees will have a better understanding of the structure of their monthly salaries.

Athlete and Coach Accountability

Certain categories of athletes and coaches must now notify their employers in accordance with the term provided in their employment contracts in order to voluntarily terminate their employment. Such term can exceed the general term of one month provided for athletes and coaches, if established in the local normative acts approved by the relevant RF sport federation (Articles 348.2 and 348.12 of the Labor Code was amended by RF Federal Law No. 136-FZ, dated July 28, 2012, which came into force on August 10, 2012). This may pave the way for longer notice periods for other categories of workers normally subject to longer notice periods such as bankers, lawyers and other professional workers.

Summary (Expedited) Proceedings for Recovering Payments Due to Employees

Amendments were also introduced into Article 122 of the RF Civil Procedure Code, particularly addressing court orders issued to employers under summary proceedings, which can now be issued based on the request for payment of (i) accrued but not paid amounts for annual leave, payments upon the termination of employment and other accrued amounts due to employees, and (ii) monetary compensation if any delay has occurred for salary payments, annual leave, payments due upon the termination of employment and/or other payments due to the employee (Article 122 of the RF Civil Procedure Code was amended by RF Federal Law No. 35-FZ, dated April 23, 2012, which came into force on April 24, 2012).

The procedure has been established to increase the efficiency of the courts by decreasing their workload. However, the summary procedure could potentially weaken the position of employees in defending their cases in court, because they will not be able to fully present their positions.

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Recent News

Recent Honors

Dechert is one of six law firms that have been **shortlisted** for "**International Law Firm of the Year**" at *The Lawyer*'s European Legal Awards, based on our Russia & CIS practice. The awards will be given out at the European Legal Awards ceremony to be held in Monte Carlo, Monaco, in late October 2012.

Laura Brank was recently profiled in *Chambers Women in Law* initiative. *Chambers Women in Law* profiles women who have excelled in their field and contributed to advancing women in law.

Yuri Makhonin was selected as an accredited arbitrator in the Court of Arbitration for Sports at the Chamber of Commerce and Industry of the Russian Federation. The Court of Arbitration for Sports is the highest ranking adjudicatory forum for settling sports-related disputes in the CIS and is one of the four international arbitration courts working under the supervision of the Chamber of Commerce and Industry of the Russian Federation. At present Yuri is one of the youngest arbitrators to be selected to the panel of recommended arbitrators for the Chamber of Commerce and Industry of the Russian Federation, and the only associate from an international law firm recently put on this list.

Recent Arrivals

July 16: Archil Giorgadze joined the **Tbilisi** office as a national partner in the Corporate and Securities Group. Prior to joining Dechert, Archil was the CEO and performed the duties of senior counsel at JSC Nenskra, a subsidiary of the state-owned JSC Partnership Fund established to build and develop a hydropower plant project in Georgia. Archil is a graduate of Tbilisi State University's Department of International Law and International Relations. He also holds LL.M. degrees from the Central European University in Budapest, Hungary, and from Harvard Law School in the United States.

June 20: Yelena Pestereva joined the **Almaty** office as an associate in the Corporate and Securities Group. Yelena is a graduate of Kazakh State University of World Languages and the Adilet Higher Law School. Yelena also holds an LL.M. from Georgetown University Law Center in the United States. She previously worked with the lawyers in the office prior to attending her LL.M.

August 1: Roman Nurpeissov joined the **Almaty** office as an associate in the International Dispute Resolution Group. Prior to joining Dechert, Roman worked in the Almaty office of an international law firm, focusing on tax and customs litigation, general corporate and natural resources law. He currently serves as a part-time assistant professor of law at the School of Law of KIMEP University in Almaty, teaching courses on international tax law and business litigation. Roman is a graduate of the Kazakh-American University and holds an LL.M. from Vanderbilt University Law School and a J.D. from the University of Michigan Law School.

August 1: Aikerim Kaziyeva joined the **Almaty** office as an associate in the Corporate and Securities Group. Prior to joining Dechert, Aikerim was an in-house lawyer at an oil & gas production company and an energy services company. She is a graduate of Aktobe State University and the Kazakh Humanitarian Law University and holds an LL.M. from New York University School of Law.

September 3: **Richard O'Brien**, an English-qualified associate in the Corporate and Securities Group, has joined the **Moscow** office on secondment from our London office. Richard is a graduate of St. Aidan's College, University of Durham and BPP College of Law, London. Richard will be working in Moscow for the next six months.

September 3: Elizaveta Molosnova joined the **Moscow** office as a paralegal in the Corporate and Securities and Dispute Resolution Groups. Prior to joining Dechert, Elizaveta worked at two leading Russian law firms. Elizaveta graduated from the Russian Academy of Justice in 2011.

Recent Deals

A team from Dechert recently advised on three important capital markets deals out of Georgia in an aggregate amount of US$1 billion.

Dechert advised JSC Georgian Railway in connection with the issuance of its new US$500 million 7.75% notes due 2022 and the simultaneous completion of a cash tender offer in respect of its existing US$250 million 9.875% Notes due 2015, which resulted in Georgian Railway repurchasing US$222.48 million of its existing notes. Georgian Railway is wholly-owned by the State of Georgia and is, by statute, Georgia's only railway operator.

Dechert also advised three prime international investment banks, as Joint Lead Managers, in connection with the issuance by JSC Bank of Georgia, the largest bank in Georgia, of US$250 million 7.75% due 2017. Both the Georgian Railway transaction and the Bank of Georgia Eurobond issuance were successfully completed on July 5, 2012.

In addition, in a transaction that closed on May 16, 2012, Dechert represented JSC Georgian Oil and Gas Corporation (GOGC) in connection with the issuance of its US$250 million 6.875% notes due 2017, which issuance represents GOGC's debut international capital markets transaction. GOGC is wholly-owned by the State of Georgia and has been designated as Georgia's "national oil company."

The securities issued in each of the Georgian Railway, Bank of Georgia and GOGC transactions were offered pursuant to Rule 144A and Regulation S under the U.S. Securities Act and are listed on the London Stock Exchange.

Partner **Louise Roman Bernstein** led on all three transactions, assisted by associates **Giles Belsey** and **Jennifer Buckett** and with support from Dechert's newly-established Tbilisi office.

Recent/Upcoming Events, Seminars and Speaking Engagements

June 20: **Oxana Peters** presented "Sicherheiten und Beitreibung im Vertrieb nach Russland" (Security and Legal Measures for Sales and Distribution in Russia) during a joint meeting of the legal committees of the Russo-German Chamber of Commerce and the Trade Chamber of the City of Hamburg, Germany.

October 9-10: **Laura Brank** will be speaking at the 2012 International M&A Summit at the New York Athletic Club in New York. She also recently participated as a judge for the International M&A Advisor Awards.

November 20: **Laura Brank** has been invited to speak at Peking University on legislative reform.

Recent Publications

Ruslan Koretski's article titled "Jeopardizing Competitiveness of U.S. Businesses in Russia" was reprinted by *Law360* on June 5.

Laura Brank, **Evgenia Korotkova** and **Kirill Skopchevskiy**'s article titled "Russia Finally Establishes a Central Securities Depository Increasing Transparency in the Russian Securities Market" was published in the *World Finance Review* in its September 2012 issue.

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We welcome your feedback. Please let us know if there are any topics you would like to see covered in future issues.

If you or your colleagues would like to receive Dechert's *CIS Legal Update*, other *DechertOnPoints*, or copies of the articles or presentations referred to herein, please contact **Anastasiya Shaposhnik** (+7 499 922 1163; anastasiya.shaposhnik@dechert.com) or **Kieran Morgan** (+44 0 20 7184 7853; kieran.morgan@dechert.com).

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With 26 offices throughout Europe, the United States, Asia and the Middle East, Dechert LLP is an international law firm focused on corporate and securities, complex litigation and international arbitration, financial services and asset management, energy, life sciences, labor and employment, business restructuring and reorganization, intellectual property, trade and government affairs, real estate finance and tax law.

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