

Russian Privatisation 2011-2013: How Is It Shaping Up?

NEW PHASE – AND NEW RULES?

There is much talk in the market of late about the anticipated privatisation of over \$29 billion of state assets to be carried out by the Russian Government over the next 3 years in order to plug budget deficits. Views differ as to whether this is simply the next phase of a process started in the early 90s, or a case of the Government sweeping the cupboard bare – assets expected to be going under the hammer include minority stakes in major state-owned companies such as Rosneft, Transneft, Sberbank, VTB Bank, SovComFlot and a few others, but may also include stakes in less desirable companies. However, what seems clear from recent changes to the privatisation legislation is that the process for this round of privatisation will be quite different from that followed in the past.

The relevant amendments (the "**Amendments**")¹ to the Privatisation Law² were adopted in May this year and came into force on 15 June, and have already attracted much interest from market participants, especially those such as investment banks who recall the lucrative opportunities afforded by earlier privatisations.

While the overall thrust of the Amendments seems to be the streamlining and modernisation of the privatisation process - their stated purpose is to modernise the privatisation process by making it more efficient and transparent, and less bureaucratic - this briefing focuses on two areas that will be of particular interest to investment banks: the right of the Government to engage an investment bank to arrange the privatisation of a particular asset; and the lifting of restrictions on the sale of Government stakes in open joint stock companies through a public offering.

INVESTMENT BANKS AS ARRANGERS

One of the key changes introduced by the Amendments is the ability of the Government to engage investment banks to arrange and manage the privatisation process on an asset-by-asset basis. This is a novel development (although not entirely new - the idea is said to have been mooted as long ago as 2004), as previously the Federal Property Agency³ and the Ministry of Defence (in respect of immovable military property) had exclusive authority to manage the privatisation of federal property.

List of Eligible Arrangers

The first step is for the Government to compile a list of legal entities eligible for appointment as arrangers of the privatisation process and/or sellers of the property to be privatised (the "**Eligibility List**"). The Amendments do not

Key Issues

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Privatisation via IPO

Going Forward

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¹ Federal Law No. 106-FZ dated 31 May 2010 "On Introducing Amendments to the Federal Law "On Privatisation of State and Municipal Property"".

² Federal Law No. 178-FZ dated 21 December 2001 "On the Privatisation of State and Municipal Property".

³ The Federal Agency for the Management of Federal Property (*Rosimushchestvo*).

specify either the procedure or the criteria for selecting entities to go into the Eligibility List. However, we understand that in early July the Ministry for Economic Development invited a number of investment banks to apply for inclusion into the Eligibility List, and that the Ministry has now submitted to the Government a draft list containing the names of 20 investment banks (both Russian and foreign). The Government is expected to approve the initial list by the end of August, but it is possible that other names may subsequently be added.

Engagement of Eligible Arrangers

Although the Amendments are not entirely clear on this point, the mere inclusion of a bank into the Eligibility List should not by itself create any commitment of that bank to participate in a given privatisation, and the subsequent engagement of a bank or banks from the Eligibility List for the privatisation of a particular asset should be subject to a separate mandate process. The mandate will be confirmed by a decision of the Government, which will also specify the property to be privatised, and the responsibilities and fees of the mandated bank(s).

As the law stands, this mandate process is subject to the Procurement Law⁴, which requires that the selection of financial organisations to render services to state or municipal authorities be carried out on a tender basis. However, there are rumours that the Procurement Law may shortly be amended to exclude its application to the mandating of banks for the purposes of the Privatisation Law (although it seems that such amendments have not yet made it onto the agenda of the State Duma).

Clearly, before committing to a mandate banks will want to consider carefully both the scope of their obligations, and any potential liability they might face as a result of their role in the privatisation process (as well as the ability to obtain meaningful indemnities for or otherwise to mitigate such liability).

PRIVATISATION VIA IPO

A second key change under the Amendments is the removal of provisions that had effectively prevented a share privatisation being structured as an IPO.⁵

The previous version of the Privatisation Law generally permitted the privatisation of shares in Russian open joint stock companies by way of sale outside of Russia, including through a foreign stock exchange. However, this method of privatisation was available only with respect to companies with fixed assets⁶ in excess of 5 million times the minimum wage (approximately RUB 500 million). Moreover, the privatisation of shares through a stock exchange was regarded as an exception, to be used only where other methods such as an auction or tender had failed.

In addition, there were previously significant practical difficulties due to the Russian securities law provisions that an offering of shares in a Russian company for sale outside Russia is subject to (among other things) receipt of permission from the Federal Service for the Financial Markets, and an obligation to first offer the shares for sale within Russia, either on a private basis (via a licensed broker) or through a stock exchange. Such provisions did not sit easily with those of the previous Privatisation Law, which did not provide for sales via a broker, and which permitted sales through a stock exchange only in the case of relatively small companies (those having non-current assets of less than 5 million times the minimum wage).

With the introduction of the Amendments, these restrictions have been removed, and it is now possible to structure the privatisation of shares as a public offering, whether as a domestic offering through one of the Russian stock exchanges, or as an offering outside Russia (with shares first being offered within Russia to comply with Russian securities legislation), or as a combination of both.

GOING FORWARD

While this latest privatisation process is still in its early stages and much remains to be done - many provisions of the Amendments are broadly drafted and require the subsequent adoption by the Government of supplementary regulations - things seem to be moving forward fairly rapidly, and no doubt both investment banks and their lawyers will be watching this space closely over the coming months.

⁴ Federal Law No. 94-FZ dated 21 July 2005 "On the Placement of Orders to Supply Goods, Carry out Works and Render Services for Meeting State and Municipal Needs".

⁵ Clifford Chance was involved in submissions on this point prior to adoption of the Amendments.

⁶ Based on balance sheet value as at the most recent financial reporting date

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