

New Listing Rules of the Moscow Exchange come into force

On 9 June 2014, a new version of the listing rules (the "**New Listing Rules**") of the Moscow Exchange (formerly known as MICEX) will enter into force¹. They introduce a number of significant changes, including with respect to corporate governance of the issuers. We discuss some of the most important amendments below.

The New Listing Rules were adopted² further to the revision by the then securities regulator, the Federal Service for Financial Markets, of the regulatory framework for admission of securities to organised trading in July 2013 (the "**FSFM Regulation**")³.

The New Listing Rules are expected to bring listing at the Moscow Exchange in line with the revised regulatory framework as well as the best practices of the major internationally recognised stock exchanges.

To soften the effect of the new rules on the day to day operation of the issuers, the New Listing Rules provide for a two year transition period (please see '*Transition period*' below).

Key changes

Reduction of trading lists number

To simplify the structure of trading activities, the number of trading lists will be reduced from six to three where:

- the Level 1 List will include securities that are currently traded in the Class "A" list (both A1 and A2 sub-levels);
- the Level 2 List will include securities that are currently traded in the Class "B", Class "V" or Class "I" lists⁴; and
- the Level 3 List will include any remaining securities (comprising securities traded without listing and securities that were admitted to trading for the purposes of initial placement and as such have not been relocated to other sections yet).

To effect the change, the Moscow Exchange will introduce a new combined list of securities admitted to trading. It will be launched on 9 June 2014 when the New Listing Rules come into force. With certain exemptions relating to bonds and investment units in unit investment funds, allocation of securities to particular lists will take place on the basis of their current listing and the issuers will not be checked for compliance with the requirements of the New Listing Rules for the particular list level on an individual basis. Please refer to '*Transition period*' below for further details.

Key issues

- Number of trading lists down to 3
- Higher corporate governance requirements for top lists
- Mandatory use of IFRS
- Monitoring of disclosure obligations
- Two year transition period

¹ Here and further, the date of entry into force of the New Listing Rules is provided as at the date of this client briefing. Shortly before this, this date was slightly postponed and additional changes may not be excluded.

² The New Listing Rules were adopted by the board of directors of the Moscow Exchange on 31 December 2013 and registered by the Financial Markets Service of the Central Bank of Russia on 7 February 2014.

³ Decree of the Federal Service for Financial Markets No. 13-62/пз-н dated 30 July 2013.

⁴ In Russian, classes "Б", "В" and "И", respectively.

Instead of automatic qualification for the Level 1 or Level 2 Lists, the issuers currently trading in the corresponding higher level lists may prior to 9 June 2014 (when the new combined trading list is due to become effective) choose to request that their securities are included in the list of a lower level (Level 2 and/or Level 3, respectively).

Listing at placement

Securities that are being placed (sold to their first holders) through the Moscow Exchange no longer have to wait until they have sufficient trading history before they can be put on one of the top two list levels. In addition, the three month minimum liquidity requirement has been abolished as well. On this basis, it will be possible to include newly issued securities into the top lists from the beginning of their trading history (assuming they meet all other applicable criteria).

Corporate governance

Changes to the corporate governance requirements are quite substantial and are arguably the main amendment introduced by the New Listing Rules. The New Listing Rules introduce a range of new requirements as well as abolishing some of the former criteria.

New criteria for independent directors

The New Listing Rules establish higher standards of independence in comparison with the current requirements. It is also important that these changes do not affect the definition of "independent directors" for the purposes of approval of interested party transactions.

Under the New Listing Rules, an "independent director" is one who is not related with any of the following persons:

- (i) the issuer;
- (ii) the issuer's material shareholders (i.e. someone who directly or indirectly, on a stand-alone basis or acting together with other third parties on the basis of, for example, a shareholders agreement, controls 5% or more voting shares of the issuer);
- (iii) material counterparties (i.e. parties that have contractual arrangements with the issuer which envisage obligations in the amount of 2% and more of (a) the consolidated assets value of the issuer or such party or (b) the consolidated annual revenue (income) of the issuer or such party);
- (iv) competitors of the issuer; and

(v) the Russian Federation, its constituents and municipal authorities.

The New Listing Rules further explain in which cases a person shall be deemed to be 'related' to each of the above categories. It is important that the New Listing Rules do not provide an exhaustive list of criteria for each category.

For example, a person will qualify as *related to the issuer*, among other things, if any of the following is true in respect of such person and/or its related persons:

- presently or at any time during the past three years he/she has held a position (and not just positions in the management bodies) at the issuer, an entity that the issuer controls or its management company;
- in any of the past three years he/she received substantial remuneration or other benefits from the issuer or an entity that the issuer controls in an amount exceeding half of the basic remuneration of a member of the board of directors ("BoD") of the issuer;
- he/she holds or is a beneficiary with respect to more than 1% of the issuer's share capital;
- he/she is a member of the executive management bodies and/or otherwise an employee of the issuer if the remuneration of such person is subject to approval by the remuneration committee of such issuer and such persons sits in this remuneration committee;
- he/she provides advisory services to the issuer, an entity controlled by the issuer or controlling the issuer or it is a member of the management bodies of organisations that provide such services or an employee of such organisations that is directly involved in the provision of services described above;
- he/she:
 - (i) provides or has at any time during the past three years provided valuation services, tax advisory, accounting or bookkeeping services to the issuer, an entity controlled by the issuer or controlling the issuer;
 - (ii) has been a member of executive management bodies of organisations that provided services referred to in item (i) or a rating agency used by the issuer, in each case during such three year period; or
 - (iii) was employed by any organisation referred to in item (ii) during such three year period if he/she was directly involved in the provision of respective services to the issuer; and
- he/she has been a member of the BoD of the issuer for more than seven years in aggregate.

Also, a person shall qualify as being *related to a material shareholder* of the issuer (as defined above) if, among other things, such person and/or persons related to such person:

- is employed by, or sits on the executive management bodies of, such material shareholder or entities controlling it;
- at any time during the preceding three years, has received any remuneration and/or other benefits from such material shareholder, entities controlling it or controlled by it in the amount exceeding a half of the base (fixed) annual remuneration of a member of the BoD of the issuer.

Level 1 List - shares

The following corporate governance requirements apply:

- the issuer must have a board of directors;
- not less than three independent directors comprising not less than 1/5th of the BoD headcount;
- a corporate secretary and internal auditor division and respective internal policies;
- committees of the BoD (audit, nomination and remuneration (the latter two may be combined));
- a dividend policy and internal audit policy, in each case approved by the BoD;
- a provision in the charter of the issuer requiring to disclose convening of the shareholders meeting not later than 30 days prior to its date (this requirement existed before); and
- a requirement to disclose the record date (for the purposes of participation in general shareholders meetings) not later than five days prior to such date (which should also be envisaged in the charter or other internal documents of the issuer).

Level 1 List - bonds

A new requirement for bonds to be eligible for the Level 1 List is to have an internal audit division and an internal audit policy approved by the BoD (or another authorised management body if the issuer is not a commercial entity⁵ under Russian law). Other eligibility criteria remain in force.

Level 2 List

The following corporate governance requirements apply:

- the issuer must have a board of directors;
- not less than two independent directors (used to be not less than one);
- an audit committee;
- an internal audit division and a policy on internal audit approved by the BoD;
- a provision in the charter of the issuer requiring to disclose convening of the shareholders meeting not later than 30 days prior to its date (this requirement existed before); and
- a requirement to disclose the record date (for the purposes of participation in general shareholders meetings) not later than five days prior to such date (which should also be envisaged in the charter or other internal documents of the issuer).

IFRS financials

In line with the requirements of other top global exchanges, to qualify for the Level 1 List issuers will be required to produce financials under IFRS or other internationally recognised accounting standards for three full financials years. Likewise, issuers targeting the Level 2 List will be required to provide such financials for one full financial year. In each case, financials need to be disclosed together with an auditor opinion.

Free float requirements

The free float requirement is replacing the former limitation on the amount of shares that can be held by one shareholder or a group of affiliates as an eligibility criterion for the top two list levels.

For inclusion of ordinary shares into the Level 1 List, issuers should have not less than RUB 3 billion worth of shares (by market value) in free float which:

- for issuers with a market capitalisation over RUB 60 billion, shall constitute not less than 10% of their issued outstanding ordinary shares; and
- for issuers with market capitalisation of RUB 60 billion and less, should not be less than the result of the following formula: $(0.25789 - 0.00263 * \text{market capitalisation (in RUB billion)}) * 100\%$.

For inclusion of ordinary shares into the Level 2 List, issuers should have not less than RUB 1 billion worth of shares (by market value) in free float and not less than 10% of the issued outstanding ordinary shares in free float.

⁵ In Russian, "хозяйственное общество".

Separate thresholds are provided for preferred stock. The mechanics for calculation of free float are approved by the Moscow Exchange separately.

Monitoring of statutory disclosure

The New Listing Rules require the Moscow Exchange to monitor compliance by the issuers with their statutory disclosure obligations, including disclosure of financials. The Moscow Exchange will start monitoring whether disclosure contains incorrect or incomplete information on the basis of tips provided to it by third parties and/or its own findings.

The Moscow Exchange will be entitled to disclose non-compliance of particular issuers with the disclosure obligations on its website if its listing department concludes that such non-compliance is material. In parallel, the Moscow Exchange shall notify the issuer of its findings and determines a cut-off date by which the non-compliance should be rectified. If the non-compliance is not rectified within the specified term, the Moscow Exchange may (based on the opinion of its listing department and taking into account the materiality and frequency of violations of the issuer) decide either to exclude securities of the relevant issuer from the list of the relevant level or leave them on the list. In either case, it is required to disclose its decision together with the grounds for such decision.

The New Listing Rules expressly provide that exclusion from the trading list may be applied to securities of all levels, including the top level lists.

In addition, the Moscow Exchange may also notify the Central Bank of any material violations that were not rectified within the given time period. Based on this information, the Central Bank may initiate further investigations which may result in additional administrative sanctions for the issuer.

New grounds for exclusion from the list

Securities need to be excluded from the Level 1 and Level 2 Lists if:

- under Russian law they are not eligible for circulation and purchase by an unlimited range of persons (e.g. are designated for qualified institutional buyers only);
- they are issued by microfinance organisations; and
- the issuer has applied for their delisting or transfer to a lower list level.

Further grounds applicable to bonds include default by the issuer under any issues of bonds included in the trading list

and the absence of an appropriate credit rating of the issuer, the bonds issue or the surety (including a downgrade resulting in such absence).

Transition period

The transition period for the New Listing Rules is two years from their entry into force, i.e. until 9 June 2016. The transition period will apply to shares of Russian and foreign issuers, investment units (including units of foreign investment funds), depositary receipts and mortgage participation certificates.

Issuers are required to bring their corporate governance or other criteria in compliance with the New Listing Rules before the transition period expires. If they fail to do so, securities from the Level 1 List are to be transferred to the Level 2 List (provided that they comply with the eligibility criteria for the Level 2 List) or the Level 3 List.

After the New Trading Rules enter into force the Moscow Exchange will be able to accept new securities whose issuer does not comply with applicable corporate governance requirements only if:

- the issuer and the securities meet all other criteria for the relevant level of the trading list; and
- the issuer has provided the Moscow Exchange with a step plan for meeting the outstanding eligibility criteria approved by a shareholder holding not less than 50% of the voting stock and the BoD of the issuer (provided that all such criteria should be met prior to expiration of the two year transition period of the New Listing Rules).

Conclusion

The amendments envisaged by the New Listing Rules follow the best practices accumulated by other major stock exchanges and are expected to aid the further development of organised trading of securities in Russia. To help the issuers and other market participants make the transition as swiftly as possible, the Moscow Exchange has been very active in promoting the New Listing Rules as well as obtaining clarifications from the Central Bank of Russia which is also working on revision of its regulation to reflect changes introduced by the New Trading Rules.

Although technical difficulties at the early stage of operation of the New Listing Rules cannot be ruled out, the market has received the changes quite positively.

Authors



Arthur Iliev

Partner

T: +7 495 258 5021

E: arthur.iliev

@cliffordchance.com



Elizaveta Turbina

Senior Associate

T: +7 495660 8028

E: elizaveta.turbina

@cliffordchance.com

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www.cliffordchance.com

Clifford Chance, Ul. Gasheka 6, 125047 Moscow, Russia

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