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News

Hungary loses an international investment arbitration case at the International Centre for Settlement of Investment Disputes requested by two subsidiaries of Canadian airport operator Airport Development Corp. over the government's alleged unlawful expropriation of investments made by ADC in Terminal 2B of Budapest Ferihegy International Airport. The ICSID Tribunal orders Hungary to pay the ADC units a total of U.S.\$76.2 million plus expenses. (Page 4)

Poland's Finance Ministry proposes transfer pricing rule changes that would extend those rules to permanent establishments of foreign companies, so that foreign parent companies would be required to prepare documentation on transactions with their permanent establishments in the country. (Page 5)

Russia's Federal Tax Service decides to make legal entities' registration details publicly available, which will help potential investors and trading partners seeking official information about Russian companies. (Page 9)

Albania's Stabilization and Association Agreement with the European Union, which eventually will lead to the Balkan nation's accession to the Union, is approved by the European Parliament, clearing the way for an interim trade agreement to enter into force in November 2006. (Page 14)

United States-based Barr Pharmaceuticals pays U.S.\$2.5 billion for Croatia's Pliva d.d. to become the world's third-largest generic drug company. (Page 22)

Special Report

Russian tax officials have become more successful at challenging transfer prices, according to an analysis of court decisions by Maureen O'Donoghue, Maxim Maximov, and Alina Gaynanshina, of Ernst & Young (CIS), Moscow. (Page 16)

Feature Report

Transfer pricing law in Azerbaijan, Kazakhstan, and Ukraine is analyzed by Nuran Kerimov, Anuar Mukanov, and Olga Loboda, of Deloitte, CIS. (Page 18)

Analysis & Perspective

Russia's recent concession law is examined by Jérôme de Montmollin, Marco A. Rizzi, and Dmitri A. Pentsov, of Froriep Renggli. (Page 23)

Romania's new public procurement law is analyzed by Daniel F. Visoiu and Iulia Bugaru, of Britis Goran SCA, Bucharest. (Page 25)

Recent Romanian capital markets reforms are surveyed by Claudia Stoian, of CMS Cameron McKenna, Bucharest. (Page 27)

Ukrainian companies' initial public offerings are discussed by Mykola Steisenko, of Baker & McKenzie, Kyiv. (Page 29)

Ukraine's rules on defending against hostile takeovers are examined by Kirill Andrianov, of Frishberg & Partners, Kyiv. (Page 30)

Contents

Topical Summary	2
Country Reports	4
Multilateral News	15
Special Report	16
Feature Report	18
Markets & Deals	22
Finance	22
Analysis & Perspective	23

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Analysis & Perspective

Russia's Recent Law On Concession Agreements

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On July 21, 2005, President Putin signed Federal Law No. 115-FZ On Concession Agreements ("Concession Law"), which has the aims of attracting investments to the Russian economy, providing effective utilization of property which is in public or municipal ownership on conditions of concession agreements, and increasing the quality of goods, works and services provided to consumers (see *BEEER*, December 2005, page 5).

The importance of the adoption of the Concession Law in today's Russia, where the overwhelming majority of infrastructure facilities (such as railroads, federal motor roads, and pipelines) continues to be state-owned, cannot be overestimated. While many of these facilities are in desperate need of modernization, due to the lack of state resources, the required financing cannot be exclusively provided from the state budget. On the other hand, many of these facilities may be successfully run as profitable businesses, which makes taking charge of their operations an attractive opportunity for private parties. That is why the Concession Law, which sets a legal framework for the construction and subsequent operation of such facilities by private parties, is widely expected to provide a major boost to the modernization of the country's infrastructure.

This article describes selected provisions of the Concession Law. It is intended for general information purposes only, and is not intended to provide legal advice. Readers should obtain legal advice before applying the information contained in this article to specific issues or transactions.

General Overview Of The Concession Law

The Concession Law consists of 37 articles subdivided into three chapters. Chapter 1 "General Provisions" deals with the goals and the subject matter of the law, the meaning of "concession agreement", the parties to such agreements, their rights and obligations, the conditions of the concession agreement, its conclusion, modification and termination, as well as the liability of its parties and the procedure for the adjudication of disputes. Chapter 2 "Guarantees of the Rights and Legitimate Interests of Concessionaires" deals with guarantees to conduct activities stipulated by the concession agreement, guarantees of equality of concessionaires as well as guarantees of the rights of a concessionaire in case of unfavorable changes in the legislation. Finally, Chapter 3 "Procedure of Conclusion of a Concession Agreement" contains provisions dealing with the tender for the right of conclusion of a concession agreement, the procedure for

submission of tender documentation, criteria for selection, selection procedure, consideration and evaluation of proposals, determination of the winner, and the procedure for conclusion of a concession agreement.

Summary Of Selected Provisions Of The Concession Law

Purpose Of The Concession Law¹

The goals of the law are:

- attracting investments to the Russian economy;
- providing effective utilization of the property in public or municipal ownership on conditions of concession agreements; and
- increasing the quality of goods, works and services offered to consumers.

Parties To A Concession Agreement²

Grantor: the Russian Federation (acting through the Government of the Russian Federation), or a duly authorized Federal body of the executive power, or a constituent territory of the Russian Federation (acting through the competent state power of such constituent territory), or a municipal unit (acting through a competent body of local self-governance).

Concessionaire: an individual entrepreneur, Russian or foreign legal entity, or two or more such legal entities acting under a simple partnership agreement ("contract on joint activity") without establishing a separate legal entity.

Meaning And Main Elements Of A Concession Agreement³

The Concession Law sets out what a concession agreement ("Concession Agreement") is by listing the main obligations of the parties to such an agreement.

Accordingly, the Concessionaire undertakes, in its name:

- to construct or to reconstruct an immovable property, indicated in the agreement ("Concession Object"); and
- to operate the Concession Object (*i.e.*, to carry out activities associated with the exploitation/operation of such object).

On the other hand, the Grantor undertakes to transfer to the Concessionaire for a period determined by, and on terms stipulated in, the Concession Agreement:

- the right of possession of the Concession Object; and
- the rights of operation/exploitation (as described/stipulated in the Concession Agreement) of the Concession Object.

Possible Concession Objects

The Concession Law indicates that Concession Objects can be immovable property which is part of a wide list of categories,

including any kind of (sea, air and land) transport infrastructure/facilities, pipelines and related infrastructure/facilities, energy production and distribution infrastructure/facilities, waste management and water treatment infrastructure/facilities as well as health, education, culture and sports infrastructure/facilities.

Ownership In The Concession Object⁴

The right of ownership in the Concession Object either is/remains with the Grantor (presumably in case of the reconstruction of an existing Concession Object) or shall subsequently be acquired by the Grantor (presumably in case of the construction of a new Concession Object by the Concessionaire).

Model Forms Of Concession Agreements⁵

The Concession Law states that Concession Agreements shall be concluded in accordance with approved model forms ("Model Agreements"). Draft Model Agreements are currently being prepared and are under review by the Government of the Russian Federation, which shall approve the Model Agreements.

According to the Concession Law, the Concession Agreement shall contain, in particular, the following provisions:

- description of the Concession Object (including technical and economic indicators);
- terms and conditions for the construction or reconstruction of the Concession Object by the Concessionaire;
- terms and conditions for the operation/exploitation of the Concession Object by the Concessionaire (the "Concession Activity");
- duration of the Concession Agreement;
- procedure for the granting of land parcels to the Concessionaire in connection with the Concession Activity, as well as (where relevant) the time limit for the conclusion of lease or sublease contracts with respect to such land parcels; and
- purpose/scope and period of Concession Activity.

Procedure For The Granting Of A Concession And For The Conclusion Of A Concession Agreement

As a general rule, Concession Agreements shall be concluded following a (public or private) tender⁶. A conclusion without prior tender is possible, in particular, if fewer than two proposals have been submitted to a tender commission or if fewer than two proposals satisfy the tender criteria⁷.

The tender procedure is described in detail in Chapter 3 of the Concession Law (Articles 21-36).

Pricing For The Operation Of The Concession Object

The Concession Law contemplates two possibilities for the determination of the prices/fees to be charged by the Concessionaire in the operation/exploitation of the Concession Object:

- application of a pricing mechanism freely agreed by the parties to the Concession Agreement⁸; or
- application of state-regulated prices ("Tariffs") and/or of a pricing mechanism based upon such Tariffs⁹.

Amendment And Termination Of A Concession Agreement

A Concession Agreement may basically be modified by mutual agreement of the parties. However, the terms and conditions of a Concession Agreement which have been determined on the

basis of a tender proposal may be changed only in case of unfavorable changes in the legislation¹⁰ and/or of changes in Tariffs¹¹.

Apart from that, a Concession Agreement may be modified by a competent court upon a unilateral request of one of the parties on the general grounds for modification of agreements, provided for by the Civil Code of the Russian Federation¹².

A Concession Agreement shall be terminated:

- upon the expiration of the period of its validity;
- by mutual consent of its parties; or
- by a court decision¹³ (as described further below).

Protection Of The Rights Of A Concessionaire

The Concession Agreement shall be subject to the laws of the Russian Federation. Thus, in the operation/exploitation of the Concession Object, the rights and — as the Concession Law puts it — "legitimate interests" of a Concessionaire shall be protected in accordance with the Constitution of the Russian Federation, international treaties ratified by the Russian Federation, the Concession Law itself and other federal laws as well as legal acts of the Russian Federation¹⁴.

According to the Concession Law, this protection shall include:

- compensation of damages caused to the Concessionaire as a result of illegal acts (or omissions or failure to act) of Federal bodies, bodies of local self-government or officials of these bodies, in accordance with the Civil Code of the Russian Federation¹⁵;
- guarantee of equal rights (also to foreign legal entities) as provided by the legislation of the Russian Federation. This would include protection from measures of a discriminatory nature and other measures precluding a Concessionaire from freely disposing of its investments as well as proceeds and profits resulting from the Concession Activity as stipulated in the Concession Agreement¹⁶; and
- protection against adverse changes in legislation. If, during the period of operation of the Concession Agreement, new legislation introduces provisions or standards which negatively affect the position of a Concessionaire to such a degree that he is to a significant extent deprived of the economic benefits that he was entitled to expect at the moment of conclusion of the Concession Agreement, the Concession Agreement shall be modified so that such expectations are re-established¹⁷.

Potential Issues In Connection With The Concession Law

It is anticipated that, from the point of view of a foreign Concessionaire or financier, a number of provisions of the Concession Law or their interpretation may be problematic.

For example:

- Under the Concession Law, the Concessionaire does not have the right to encumber a Concession Object with a mortgage¹⁸. Since the wording of the Concession Law does not make any distinction, this would seem to be the case also where the Concessionaire initially has ownership in the Concession Object;
- The substitution of parties to the Concession Agreement by means of assignment of rights or a transfer of the debt is

allowed only with the consent of the Grantor after the entry into operation of a Concession Object¹⁹. However, it is not clear whether the Grantor may give his (general) consent to such assignment or transfer before the entry into operation of the Concession Object (*i.e.*, in the Concession Agreement);

- A Concessionaire may not pledge his rights under the Concession Agreement²⁰. It is not clear to what extent this prohibition is absolute (for example, if it also includes pledging of future proceeds of the Concession Activity);
- The Concession Agreement may be terminated by a court decision at the unilateral request of a party to the Concession Agreement in case of 1) a substantial breach of the contractual obligations by the other party, 2) substantial change of the circumstances upon which the parties have been relying at the moment of the conclusion of the Concession Agreement, and 3) for other reasons stated in the Concession Law, in other Federal laws or in the Concession Agreement itself²¹;
- The Concession Law does not contain a clear and specific reference to the possibility of adjudication of disputes by international arbitration; and
- Although, as indicated above, the Concession Law appears to offer a certain degree of protection to the Concessionaire, it is difficult to assess how far this protection goes and how effective it is.

Comment

One of the aims of the Concession Law is to attract foreign know-how and financing in the modernization of the transport infrastructure of the Russian Federation. This aim can certainly be reached if potential foreign Concessionaires and financiers are

convinced that the Concession Law grants effective protection of their rights and economic interests. Whether this is always the case, however, is to some extent open to doubt. Possibly, the legislator and the executive power of the Russian Federation will provide answers which shall dissipate any doubt.

In any event, a proper assessment of the legal environment, as well as a careful redaction of the Concession Agreement, will be crucial for any foreign Concessionaire or financier.

NOTES

- 1 Article 1
- 2 Article 5(1)
- 3 Article 3(1)
- 4 Article 3(1)
- 5 Articles 10(4) and 13(2)
- 6 Article 13(1)
- 7 Article 37
- 8 Article 10(2)(2)
- 9 Article 10(2)(6)
- 10 Article 13 in connection with Article 20(1)
- 11 Article 13 in connection with Article 20(3)
- 12 Article 13(4)
- 13 Article 13(5), items 1-3
- 14 Article 18(1)
- 15 Article 18(2)
- 16 Article 19
- 17 Articles 20(1) and 20(3)
- 18 Article 3(6)
- 19 Article 5(2)
- 20 Article 5(2)
- 21 Article 15(1)

Romania's New Public Procurement Law Makes Significant Improvements, But Leaves Key Problems Unresolved

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While the Romanian State should be congratulated for making great strides in terms of the new public procurement legislation intended to transpose European Union Directives 17/2004 and 18/2004 (Law 337/2006; the "Law"), which also now indirectly deals with public-private partnerships, there is still room for improvement. For example, less than a month after the new legislation came into effect on June 30, 2006, there was already a public controversy regarding Fondul Proprietatea (Property Fund) — an investment fund to be set up as part of a program to provide compensation for property taken abusively — and specifically whether or not this institution would be a "contracting authority" and thus subject to the new public procurement legislation.

This article sets forth a brief analysis of the existing Romanian legislation, as well as the current E.U. rules and European Court of Justice jurisprudence. This article does not address other related legislation, such as the recently enacted Government Emergency Ordinance 30/2006 on the Verification of Procedural Aspects relating to the Awarding of Public Procurement Contracts (which also came into force on June 30, 2006).

Two Major Problems To Date

Regarding the Fondul Proprietatea matter, the main issue involved what constitutes a "contracting authority". Article 1(9) of E.U. Directive 18/2006 used more general language in defining "contracting authority", meaning that there would be little doubt under this directive regarding that Fondul Proprietatea is in fact a "contracting authority" (based on the main objective for the setting up of this fund, based on the