

FOREIGN IPOs BY RUSSIAN ISSUERS — NEW RULES

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To Our Clients and Friends:

The Federal Service for Financial Markets of the Russian Federation (“FSFM”) has published new “Regulations on the Approval by the Federal Service for Financial Markets of Offerings and/or Trading of Securities of Russian Issuers Outside the Russian Federation” (“New Regulations”), which introduce significant changes to the existing rules for foreign securities offerings by Russian issuers. The FSFM Order approving the New Regulations was registered by the Ministry of Justice on October 2, 2009, and is expected to come into effect, together with the New Regulations, on January 1, 2010.

The key point of the New Regulations that has generated such lively discussion among industry participants provides for a reduction in the number of shares of Russian issuers admissible to trading outside Russia in the form of depositary receipts. The maximum limit on the number of shares traded abroad – no more than 5% of the total number of shares – applies to Russian private issuers making initial public offerings. Below we discuss this and other changes in more detail.

RESTRICTIONS ON THE NUMBER OF SHARES OFFERED OUTSIDE RUSSIA IN THE FORM OF DEPOSITARY RECEIPTS

Under the existing rules governing foreign offerings of the shares of Russian issuers,¹ the number of shares of a Russian issuer offered and traded abroad in the form of depositary receipts may not exceed 30% of the total number of shares of such issuer. Issuers with strategic importance for national defense and national security² (“Strategic Companies”) are subject to additional restrictions: no more than 25% of the shares of a Strategic Company may be traded abroad, and, furthermore, if the Strategic Company performs geological studies of subsoil resources and/or exploration and production of mineral resources at

¹ *Regulations on the Approval by the Federal Service for Financial Markets of Offerings and/or Trading of Securities of Russian Issuers Outside the Russian Federation, approved by Order No. 06-5/pz-n of FSFM Russia, dated January 12, 2006 (“Existing Regulations”).*

² *See Federal Law No. 57-FZ dated January 29, 2008 on Foreign Investment in Commercial Entities of Strategic Importance for National Defense and National Security (“Law 57-FZ”).*

subsoil sites of federal importance (“Strategic Subsoil User”), this number is reduced to a maximum of 5% of shares.

The New Regulations introduce additional restrictions and propose a variable approach to establishing the maximum number of shares traded abroad depending, primarily, on the level of the listing of the issuer’s shares on Russian stock exchanges:

	Maximum number of shares that may be offered and traded abroad in form of depositary receipts as a % of total shares	
	Existing Regulations	New Regulations (from January 1, 2010)
Shares listed on quotation list “A” on Russian stock exchange	30% (for Strategic Companies 25%)	25%
Shares listed on quotation list “B” on Russian stock exchange		15%
Shares listed on quotation lists “V” or “I” on Russian stock exchange		5%
Shares listed on any quotation list on Russian stock exchange, if a depositary issuing depositary receipts in respect of such shares is registered in a country whose regulator has entered into a cooperation agreement with the FSFM		25%
Shares of Strategic Subsoil Users	5%	5% (for transactions relating to offerings and trading approved under Law 57-FZ – in the approved number, but not more than 25%)

Clearly, the companies for whom the new restrictions could create the most problems are private companies going public, since these are the companies whose shares would be listed on the “V” and “I” quotation lists. It is fairly likely that, as a result, these quotation lists could largely lose their appeal for companies launching IPOs. Moreover, even issuers with “B”-listed shares could find difficulty attracting foreign investors on foreign exchanges, because 15% of the total number of shares will not always be sufficient to create the necessary liquidity abroad.

The number of shares traded abroad may be increased to 25% if the issuer of depositary receipts is a depositary registered in a country whose regulator has entered into a cooperation agreement with the FSFM. At present, all of the major depositary banks

operating in Russia are U.S. entities; however, the U.S. securities regulators have not signed a cooperation agreement with the FSFM.³

In addition to restricting the overall number of shares traded abroad, the New Regulations state that not more than 50% of the total number of shares offered for sale in the Russian Federation may be placed outside the Russian Federation (this number is 70% under the Existing Regulations). The requirement that shares underlying depositary receipts issued abroad must be offered in Russia in effect has prevented Russian issuers from establishing depositary receipt programs without an offering (or other sale of shares), even if the shares of such issuer are traded and listed on Russian exchanges. In recent interviews, the head of the FSFM has said that the possibility of amending the New Regulations is being considered with a view to allowing for depositary receipt programs to be established in respect of the shares of Russian issuers without the need to offer shares.

OTHER CHANGES

Amendment of Deposit Agreement

The New Regulations set forth that in the event of any amendments to the deposit agreement governing the issuance of depositary receipts evidencing the shares of a Russian issuer, the Russian issuer or, if such Russian issuer is not a party to such agreement, the issuer of the foreign securities must notify the FSFM of such changes, and append a copy of the new version of the deposit agreement. No new FSFM approval is required if the depositary is replaced. These provisions in effect consolidate existing practice.

Reorganization of the Russian Issuer

The New Regulations provide for the possibility that a company created as a result of the reorganization of another company whose shares are traded abroad pursuant to previously obtained FSFM approval can obtain FSFM approval to establish a depositary receipt program. This matter was not mentioned in the Existing Regulations and had continued to be a cause for concern.

Notification of the Results of Foreign Share Offerings

Contrary to the Existing Regulations, the New Regulations provide for the obligation to notify the FSFM of the results of share offerings not later than 30 days from the expiration of the share offering in Russia and abroad. Such notification is made by the Russian issuer or shareholder whose shares were offered or, upon their instruction, by a Russian stock exchange or broker through whom the offer was made.

³ *A list of countries whose securities regulators have signed a Memorandum of Understanding and Exchange of Information with the FSFM may be found on the FSFM website: www.fscm.ru/catalog.asp?ob_no=182101.*

Termination of FSFM Approval

The Existing Regulations do not envisage the possible termination or revocation of FSFM approval. The New Regulations set forth three cases in which the FSFM may cancel FSFM approval:

- if the offering or trading in the securities has not commenced within one year from the date of issue of the FSFM approval;
- if notification of the results of a share offering is not made within the prescribed time; or
- if the securities of the Russian issuer in respect of which FSFM approval was issued are redeemed (canceled).

We would be happy to answer any questions you may have on these or any other aspects of Russian securities law.

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