

## Private equity and venture capital in Russia | BY ANTON KLYACHIN

In this article we outline the most recent developments in Russian law and practice that concern private equity and venture capital investors. We also discuss the bills that are now coming through Russian legislature and that will, if passed, be important for investors in Russian assets and companies.

### Shareholders' (participants') agreements

Until recently, Russian law was not familiar with the concept of a shareholders' agreement, which was one of main legal risks for investors willing to invest directly into a Russian company. Court practice in many cases held invalid any agreement between shareholders or participants of a Russian company aimed at governing their shareholder rights. The grounds for that was quite simple: Russian law did not recognise the concept of a shareholders' agreement and therefore the courts decided that all corporate relations between shareholders and the company should be governed by the law and not by an agreement.

This position was much criticised but remained in place for quite some time. In summer 2009, the main Russian laws governing legal entities (the Law on Limited Liability Companies and the Law on Joint-Stock Companies) were amended to introduce the concept of shareholders' (or participants', in case of a limited liability company) agreements. According to the new laws, the parties to such agreements may undertake to vote in a particular manner at general shareholders' (participants') meetings, to agree on voting options with other shareholders (participants), to acquire or dispose of shares (or participatory interests) at a pre-determined price and/or upon the occurrence of certain events, to refrain from share (or participatory interests) transfers subject to certain conditions, and/or to perform other actions related to the management of the company and its activities in a coordinated fashion.

These developments are thought to be very progressive for Russian law. However, practicing lawyers envisage certain problems with their implementation. First of all, new rules remain untested in Russian courts and therefore a lot of questions concerning their construction and interpretation are yet to be cleared by the courts. Second, the laws contain many mandatory provisions. Such provisions prescribe certain ways of doing things and set limits for the parties in agreeing on terms and conditions of shareholders' (participants') agreements that contradict mandatory legal requirements. In practice, Russian courts often act based on the assumption that what is not expressly allowed is prohibited. These factors clearly limit the effectiveness of shareholders' (participants') agreements.

### Convertible loans

The funds often wish to start an investment with granting a convertible loan to a potential target company. This ties the company and its shareholders to the investor and therefore to buys some time for due diligence of the company.

Russian law, however, presents certain obstacles to direct conversion of debt into equity. Those come from the general concept of equity (chartered capital) of a Russian commercial company, which is considered to be a security for all creditors and counterparties of the company. Therefore, Russian law prohibits increasing the equity (chartered capital) to cover losses or discharge a debt to one creditor. However, recent discussions among Russian legal experts, courts and legislature point out the necessity of introducing a concept of convertible loans into the law. The matter is more relevant in these turbulent times and we believe the law should be amended quickly to allow many companies to convert their debt to equity, and by doing so avoid bankruptcy.

### Enforcement of pledges

Investors often seek to secure the loan granted to a potential recipient company with a pledge of its assets. Given that the pledged assets are usually situated in Russia, the pledge would usually be regulated by Russian law. At the beginning of 2009, Russian law on pledges changed to simplify the procedure of enforcement of pledge, which would potentially help the investors to structure security measures more efficiently. The amendments provide for alternative methods of enforcing pledges over assets (other than auction which has been the only option until now) that can be established by a contractual arrangement among companies and/or individual entrepreneurs. For example, it is now possible for them to agree on the sale of a pledged asset to third parties or on direct acquisition of the ownership of pledged property by the pledgee in case of default. Amendments came into force on 11 January 2009. We would, however, note, that the new law describes the new methods quite briefly and many details would depend on the court interpretation of the new rules. Considering the economic situation, we would expect this new law to become extremely popular in the coming months and therefore the court practice would be accessible in the near future.

### Antimonopoly rules

On 22 December 2008, the Russian Government submitted draft laws contemplating changes to the competition regulations to the State Duma. The amendments are aimed at increasing thresholds relevant for clearances of qualified transactions and at simplification of the applicable procedure while proving monopolistic high level prices. At the same time, the amendments will sever the liability for breach of anti-monopoly rules. ■

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