

# Legal Newsletter – „Financial and Capital Market Developments in Russia“

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## 1. Insurance and Pension Funds

### Clarification of the Functions of the Ministry of Health and Social Development and the Federal Financial Markets Service (“FFMS”) in the Sphere of State Control over the Activity of Non-state Pension Funds

The Government of the Russian Federation has clarified<sup>1</sup> the functions of the Ministry of Health and Social Development of the Russian Federation and the FFMS in the sphere of state regulation and control over the activity of non-state pension funds and the non-state provision of pensions, obligatory pension insurance and professional pension insurance.

Thus, the Ministry of Health and Social Development shall exercise, *inter alia*, the following functions:

- approval with the FFMS’s consent of model agreements on obligatory pension insurance, model insurance rules over non-state pension funds, requirements for the non-state provision of pension schemes;
- approval of application forms of insured persons, model agreements on mutual certification of signatures with a non-state pension fund, etc.;
- submission of requests to the FFMS and non-state pension funds for the provision of information;
- consideration within its competence of claims and petitions of individuals and legal entities in relation to breaches of legislation on non-state pension funds, etc.

The functions of the FFMS are more extensive, which, along with the adoption of certain regulatory acts, include, *inter alia*, the issue and revocation of licenses, registration of rules of

<sup>1</sup> Government Regulation No. 9 of January 19, 2010, entered into force on February 2, 2010

non-state pension funds, carrying out inspections, etc.

**Changes in Requirements on Pension Reserves Structures** The Government of the Russian Federation introduced certain amendments<sup>2</sup> to the Rules on Pension Reserves Placements, which update the requirements on the structure of the pension reserves of non-state pension funds. It is now stipulated that the share of securities of one issuer, save for the state securities of the Russian Federation, state securities of constituent entities of the Russian Federation and shares of stock unit investment funds may not exceed 15% of the pension reserves (previously – not more than 10 %).

## 2. Capital Markets and Securitization

### Clarification of the Requirements for the Activities on the Securities Market

FFMS Order of January 26, 2010 No. 10-3/pz-n clarifies the license requirements for carrying out of professional activities on the securities market and the licensing procedure as well as increases the terms for trading. New amendments came into effect on March 28, 2010. In particular, the amendments concern, *inter alia*:

- procedure for reviewing applications provided by the self-regulating organizations and passing decisions on the issuance of licenses within reduced terms has been cancelled;
- requirement to the sole executive body of licensees has been changed. In particular, the period of work experience has been increased twofold as well as the list of companies in which the sole executive body has to have worked has been clarified. In particular, to the list is now added organizations that exercise professional functions in the specialized depository of investment funds, unit investment funds and non-state pension funds;
- notification procedure of the license body of the appointment of temporary or new sole executive bodies in the event of a suspension (early termina-

<sup>2</sup> Government Regulation No. 119 of March 04, 2010

tion) of the powers of the existing sole executive has been established;

- term of trading within a single trading session has been increased from 18.00 to 19.00 Moscow time and the term for providing the registration of deals to each participant of the trading session have been increased.

Terms for the passing of decisions on the revocation of licenses of professional participants in credit organizations in the event of the revocation or cancellation of their licenses have been established.

**Clarification of the Procedure for Securities Issuance** FFMS Order No. 10-15/pz-n of March 4, 2010 clarifies the procedure for securities issuance, in particular, via the clarification of the content of the documents to be submitted to the FFMS containing information about the assets of stock companies. The mentioned Order came into force on April 16, 2010.

**New Procedure for the Provision of Reports by Professional Participants in the Securities Market** FFMS Order No. 09-49/pz-n of November 19, 2009 provides a new procedure for the provision of reports by professional participants in the securities market. The last procedure has been terminated under the mutual Order of the FFMS and the Ministry of Finance of November 16, 2009 No. 09-37/pz-n/118n.

The new procedure establishes the liability of sole executive bodies and controllers for the authenticity, completeness and terms for the provision of reports.

The new procedure also provides, in particular, reporting dates and dates for the submission of reports as well as the way (hard copy/electronic form) to provide the reports.

The new procedure came into effect on February 6, 2010.

**Clarification of the Procedure for the Disclosure of Information on the Calculation of Equity Funds on the Internet** The professional participants on the securities market as well as companies managing the investment funds, unit investment funds and non-state pension funds are obliged to calculate their equity funds as of the last calendar day of each month in accordance with the FFMS acts. FFMS Order No. 10-7/pz-n of February 11, 2010 provides that information on the calculation of such

firms' equity funds is to be disclosed on the Internet within one month after the month within which these funds have been calculated. This provision differs insignificantly from the former one. The mentioned Order also provides for technical requirements of the information disclosure. The Order comes into force on May 22, 2010.

**Clarification of the Conditions of Placement of Russian Issuers' Securities outside the Russian Territory** Under FFMS Order No. 09-46/pz-n of November 12, 2009, shares of Russian issuers included in the quotation list "A" (first and second echelons) can be placed outside the territory of Russia, provided that the requirement of placing not less than 50% of the Russian issuers' shares of a respective issuance initially within the territory of Russia can be not observed under certain conditions. In particular, these conditions are: the application to obtain the FFMS' permission to circulate Russian issuers' securities outside the territory of Russia to be signed by the Russian depository that complies with certain requirements of experience, amount of its equity funds, market value of the securities under its depository management, quality of its services as well as an obligation of the issuer of the foreign securities (by the issuance of foreign securities it arranges of the circulation of Russian issuers' securities) to utilize the services of a depository that comply with the above-mentioned requirements and to provide, on a regular basis, to the Russian issuer a list of the real and nominal owners of the above-motioned securities. The clarified conditions of the placement of Russian issuers' securities outside the territory of Russia came into force on March 13, 2010.

**Clarification of the Legislation with respect to the Placement and Circulation of Foreign Securities in Russia** The amendments to the legislation with respect to the placement and circulation of foreign securities in Russia concern the following:

- list of foreign companies that may be engaged in placing foreign securities for circulation in Russia has been approved<sup>3</sup>. The list includes 63 foreign companies (banks, clearing houses and depository companies), in which the

<sup>3</sup> FFMS Order No. 10-6/pz-n of February 09, 2010

Russian depositories may open accounts in favor of persons acting in the interests of other persons for the purposes of the recording of the rights of foreign securities permitted for public placement and circulation in Russia;

- conditions of access of foreign securities to be placed and circulated in Russia have been clarified<sup>4</sup>. In particular, the composition and procedure for the calculation of indexes that show the liquidity level and investment risk level of the securities have been determined;
- requirements of equity funds and experience of the broker that signs foreign issuers securities prospectuses have been provided<sup>5</sup>. Requirements of the depository that holds the rights to securities of foreign issuers to be permitted to public placement and(or) circulation have been stipulated<sup>6</sup>;
- procedure for the FFMS's passing of a decision on the permission of foreign securities to public placement and (or) circulation in Russia, as well as the procedure for the registration of foreign securities prospectus, including a list of the documents to be submitted to the FFMS for registration of foreign securities prospectuses, have been provided<sup>7</sup>. The procedure does not apply to foreign securities that can be submitted for circulation in Russia under a decision of the Russian stock exchange.

**Clarification of the Conditions with respect to the Inclusion of Foreign Securities in the Composition of Pension Reserves of Non-State Pension Fund** FFMS Order No. 10-8/pz-n of February 11, 2010 adds 9 European, American and Asian stock exchanges to the list of foreign stock exchanges on which foreign securities must be listed in order to be included in the composition of pension reserves of non-state pension funds. The mentioned Order came into force on April 16, 2010.

**Clarification of the Requirements to Mortgage Securities in which Pension Savings can**

**be Invested** Under Government Regulation No. 73 of February 20, 2010, the investment of pension savings into mortgage-backed securities is allowed, provided that the fulfillment of the obligations towards the bonds holders is secured by a guaranty of a legal entity which has been assigned a rating of long-term creditworthiness in Russian rubles or in foreign currency by one of the international rating agencies or a national rating agency accredited in accordance with the Russian legislation.

Pension savings may also be invested into Eurasian Development Bank securities under certain conditions.

The new requirements came into force on March 09, 2010.

**Clarification of the Composition of the Assets of Stock Investment and Unit Investment Funds** FFMS Order No. 09-64/pz-n as of December 29, 2009 clarifies the definition of illiquid securities. In addition to that, it increases the maximum share of the securities of the assets of the investment funds for qualified investors. The amendments came into force on March 13, 2010.

**Derivatives** FFMS Order No. 10-13/pz-n of March 04, 2010 determines types of derivatives. They are option contracts, future contracts, forward contracts, over-the-counter forward contracts and swaps. The underlying assets of such contracts are determined. The amendments came into force on May 4, 2010.

**Requirements for the Use of Derivative Instruments (Option and Futures Contracts) in the Assets of Investment Funds and Non-State Pension Funds** FFMS Order No. 09-45/pz-n of November 10, 2009 provides the requirements of the use of derivatives instruments in the assets of investment funds and non-state pension funds ("**Assets**"). The Order came into force on March 19, 2010.

The requirements concern, in particular, the following:

- it provides a definition of option and futures contracts, the rights of which may be included in the Assets;
- it describes the conditions under which option and futures contracts can be included among Assets;
- it provides the requirements for the acquisition of derivative instruments un-

<sup>4</sup> FFMS Order No. 10-5/pz-n of February 09, 2010

<sup>5</sup> FFMS Order No. 10-12/pz-n of February 25, 2010

<sup>6</sup> FFMS Order No. 10-19/pz-n of March 23, 2010

<sup>7</sup> FFMS Order No. 10-20/pz-n of March 23, 2010

der option contracts on Assets, in particular, it determines the value of the derivatives instruments within the Assets structure;

- it sets forth the requirements related to risk management in the case of concluding option contracts; and
- it provides the requirements for executing repo-transactions on Assets.

### 3. Banking Law

#### New in the Regulation of Banking Activity

**Banks have Become Obligated to Notify State Funds on the Accounts of Clients** Starting on January 1, 2010, when Federal Law No. 212-FZ “On Insurance Contributions in Pension Funds, Social Insurance Funds, Federal Compulsory Medical Insurance Funds and Territorial Funds of Compulsory Medical Insurance in the Russian Federation” came into force, all the banks became obliged to notify, within 5 days, respective insurance control authorities when opening (closing, making requisite changes) bank accounts of legal entities or individual entrepreneurs. The order of such notification must be approved by the Central Bank of the Russian Federation (“**CB RF**”) upon agreement with the Pension Fund of the Russian Federation and Social Insurance Fund of the Russian Federation (“**SIF**”). The SIF has already prepared drafts<sup>8</sup> of such notifications and directed them to the CB RF for the preparation of the order of the notification of clients’ accounts to be made by banks.

**Bank are not Allowed to Change the Conditions of Credit Facility Agreements Unilaterally or Charge for the Opening of Loan Accounts** Within a short period of time, the Russian legislation was amended in respect of credit organizations’ activity related to the provision of credit. For instance, the Federal Law “On Banks and Banking Activity”<sup>9</sup> has been amended<sup>10</sup> in respect of credit organizations’

rights provided in credit facility agreements concluded with individuals and legal entities (individual entrepreneurs). In cases of credit facility agreements concluded with individuals, a credit organization does not have the unilateral right to reduce the term of an agreement, increase the credit facility rate and (or) change its revision procedure, increase or fix the operations’ commission - save for the cases provided by the law. Additionally, the Supreme Arbitration Court of the Russian Federation (“**VAS RF**”) has concluded<sup>11</sup> that the unilateral right of a credit organization to change the interest rate specified in a credit facility agreement derogates individuals’ rights. As to clients, legal entities and individual entrepreneurs, a credit organization is entitled to unilaterally change credit facility rates or (and) change their revision procedure, deposits rates, commissions and terms of such agreements if such rights are clearly provided in the agreement as well as in other cases set-out in Russian legislation. The above-mentioned amendments came into force on March 20, 2010 and must be applied to legal relationships arising from agreements concluded after this date.

In addition, the VAS RF has appraised<sup>12</sup> charging for loan accounts which are opened and maintained to debtors-individuals. The court instance concluded that loan accounts (i) are not bank accounts, (ii) used by banks only for the indication of the debt on balance, (iii) are not an independent bank service and (iv) imposing a condition demanding payment for the opening of an account is not based on law and violates consumer rights.

Also, the VAS RF has defined that stipulating a condition that resolving disputes arising from credit facility agreements concluded between a bank and individual shall take place at a court relative to the bank’s location (territorial jurisdiction of the court in relation to the bank) violates consumer rights. However, this conclusion contradicts the opinion of the Supreme Court of the Russian Federation which recently declared<sup>13</sup> that credit facility agreements con-

<sup>8</sup> Letter of the SIF No. 02-10/05-13656 of December 28, 2009

<sup>9</sup> Federal Law No. 395-1, dated December 02, 1990

<sup>10</sup> Federal Law No. 11-FZ, dated February 15, 2010

<sup>11</sup> Resolution of the Presidium of the Supreme Arbitration Court of the Russian Federation No. 7171/09, dated March 02, 2010

<sup>12</sup> Resolution of the Presidium of the Supreme Arbitration Court of the Russian Federation No. 8274/09, dated November, 17 2009

<sup>13</sup> Letter of the Supreme Court of the Russian Federation No. 8/obsh-1936, dated July 20, 2009

cluded between credit organizations and individuals may contain a provision that all disputes arising between the parties may be resolved with a court at the place of the bank's location.

**New Procedure on State Registration of Credit Organizations and the Issuance of Licenses to Conduct Banking Activities has been Adopted** On May 11, 2010, the Instruction of the CB RF No.135-I "On the Procedure of Decision Making by the Bank of Russia on the State Registration of Credit Organizations and Issuance of Licenses to Conduct Bank Activities" dated April 02, 2010 came into force. This instruction has substituted the already voided Instruction of the CB RF No. 109-I dated January 14, 2004. Generally, the new document repeats the provisions of the previous instruction.

In accordance with the Instruction, credit organizations must be established as a business entity (stock company, limited liability company or additional liability company). Legal entities as well as individuals may be the founders of a credit organization save for the cases provided by the legislation in force. Herewith the founders are not entitled to withdraw from the bank within the first three years from the state registration of the bank.

The Instruction regulates the procedure of decision-making on the state registration of credit organizations, opening and closing of subdivisions of credit organizations within the territory of Russia, state registration of amendments to the charter of a credit organization, its reorganization, etc.

The new Instruction does not provide a possibility to open currency exchange points (as an internal subdivision) as it was possible in accordance with the previous instruction. In addition, the CB RF has prohibited the opening of new currency exchange points starting from May 11, 2010. All of the existing exchange points must be transformed into the other types of internal subdivisions or closed by October 1, 2010. Moreover, a credit organization is not entitled to delegate to an internal subdivision buying and selling of cash foreign currency function only. Such division must provide other services that are delegated by the credit organization.

**Explanations in respect of Deposit Interest Rates** The Department of Banking Regulation

and Supervision of the CB RF has given certain explanations in respect of the limitation of deposit interest rates. In Letter No. 15-6-1-1/465 of February 05, 2010, it states that exceeding the average deposit interest rate by 1,5% will ensure acceptable level of competition along with the medium interest rate risk accepted by banks.

**New Financial Reporting Preparation Procedure has been Adopted** The CB RF in its Letter No. 24-T of February 17, 2010 has adopted new methodic recommendations for the preparation and provision of the financial reporting of credit organizations. The document contains requirements on the structure and content of the forms, preparation, audit, publishing, provision and use of the financial reporting. It also contains other information required for the due preparation of the reporting of credit organizations.

**Recommendations of the CB RF in respect of the Financial Market Participants** The FFMS publishes on its web-site<sup>14</sup> information about those financial market participants that are prohibited or limited in performing their operations. The CB RF recommends<sup>15</sup> that credit organizations pay attention to such information, particularly during the establishment of relations with financial market participants, performing of operations with such participants or carrying out the operations of financial market participants by using its accounts.

#### 4. Anti-money Laundering Legislation

**New Rosfinmonitoring's Notification Order** The Federal Financial Monitoring Service ("Rosfinmonitoring") has adopted an Instruction<sup>16</sup> regulating the obligation of organizations performing operations with monetary funds or other property as well as attorneys, notaries and persons performing business activity connected with the rendering of legal or accounting services to provide the Rosfinmonitoring with the information stipulated in the Federal Law "On Countering Legalization of Income (Money

<sup>14</sup> [http://www.fcsm.ru/catalog.asp?ob\\_no=232639](http://www.fcsm.ru/catalog.asp?ob_no=232639)

<sup>15</sup> Letter of the CB RF No. 29-T of March 1, 2010

<sup>16</sup> Order of the Rosfinmonitoring No. 245 of October 5, 2009

Laundering) Derived from Criminal Activity and Financing of Terrorism”<sup>17</sup>. In accordance with the Instruction, said information must be provided in electronic form while a hard copy form notification must be submitted upon the prior consent of the authority. In the course of the preparation and delivery of electronic messages, the above-mentioned persons shall use the software system with cryptographic facilities provided by the Rosfinmonitoring. Also, the document contains an order of notification (rules, terms, etc.) as well as additional information required for due notification of the state authority.

**Establishment of the Anti-Money Laundering Coordination Council** In accordance with the Rosfinmonitoring’s Regulation No. 336 of December 8, 2009, which came into force on February 28, 2010, the Anti-money Laundering Multiagency Commission has been established in the Russian Federation. In accordance with the document, the Commission’s activity is aimed at the preparation and consideration of draft laws and other regulatory acts, cooperation of state authorities and the CB RF, general line elaboration with respect to international cooperation and proposals in respect of the improvement of the national anti-money laundering system. The Commission was formed with representatives of the state executive authorities of Russia and the CB RF with the participation of other interested persons. The above-stated document regulates the Commission’s order of activity and decisions making. All of the decisions adopted by the Commission within its competence shall be obligatory for all of the state authorities represented in the Commission.

**Clarification of the Identification of Individuals** In addition to Letter No. 117-T of September 25, 2009, which was reviewed in our previous bulletin<sup>18</sup>, the CB RF has issued Letter No. 12-1-5/273 of February 19, 2010. This letter clarifies Letter No. 117-T as well as contains additional information with regard to the identification of individuals. For instance, the CB RF notes that credit organizations are prohibited to open accounts (deposits) for individuals without

their or their representative’s physical presence. Also, it is described that the Regulation of CB RF No. 266-P of December 24, 2004 “On Emission of Bank Cards and Performing of Operations Using Payment Cards” does not contain any restrictions related to the place of the issuance (hand over) of bank cards to a client.

## 5. Other Significant Issues

**Changes to the Laws on Bankruptcy and Laws to Insurance Companies** Federal Law No. 65-FZ “On Changes to the Law On Organization of the Insurance in Russian Federation and Separate Acts of the Russian Federation” of April 22, 2010 made significant amendments to the laws on bankruptcy and laws on insurance companies. These amendments come into force on July, 27, 2010, with the exception of the provisions on minimum charter capital of the insurance companies that come into force on January 01, 2012. In particular, the amendments concern the following:

- The procedure for invoking the bankruptcy of financial organizations, including non-state pension funds, has been clarified. For example, the Russian Ministry of Healthcare and Social Development is now obliged to file a lawsuit with the court seeking that a non-state pension fund be recognized as bankrupt in the case of its having an insufficiency of funds to satisfy its contributors and(or) participants as well as other creditors. The authorized body is obliged to file a lawsuit with the court within 10 days starting from the moment when it knew or should have known about the mentioned circumstances. Previously, the fund itself had to file a lawsuit with the court;
- A list of financial organizations (*in particular, insurance companies, professional participants of securities market, non-state pension funds, managing companies of investment funds, unit investment funds and non-state pension funds*) to which the measures to prevent their bankruptcy should be applied (*for example, providing financial assistance, increasing charter capital, changing the assets and liabilities composition, reorganization*) is provided.

<sup>17</sup> Federal Law No. 115-FZ of August 7, 2001

<sup>18</sup> Please see Legal Newsletter – „Financial and Capital Market Developments in Russia“, Bulletin, January, 2010

The grounds for applying these measures are specified. In particular, they are: repeated refusal within 1 month to pay; non-fulfillment of the obligation to make obligatory payments for more than 10 working days, starting from the exercise date; insufficiency of monetary funds for the proper fulfillment of money liabilities and(or) mandatory payments in the case of the maturity;

- A new special temporary body for the management of financial organizations – temporary administration - has been established. The tasks of the temporary administration are the reestablishing of the solvency of the financial organization and (or) assets safekeeping. The status of the temporary administration, its constitution and its functions are specified;
- The minimum charter capital of an insurance company, with the exception of insurance companies that execute voluntary as well as mandatory medical insurance, has been significantly increased;
- The procedure for the licensing of insurance companies has been clarified. The term for passing a decision on the issuance of a license has been increased twofold and constitutes 120 days, with the exception of cases involving the passing of decisions on the providence of licenses for voluntary as well as mandatory medical insurance.

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This BBH Bulletin is to serve as a general piece of information in respect of certain important news and events taking place in the area of the financial, capital and banking markets. The contents hereof do not, and shall not, serve as legal advice of any kind.

In the case of your interest, please feel free to contact us and request individual information, advice and/or consultation.

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