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# CIS AND CENTRAL EUROPE LEGAL NEWSWIRE

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RUSSIA

## Legislative Update: Proposed Amendments to the Limited Liability Company Law Would Eliminate Right of Withdrawal

The Russian Federation ("RF") State Duma is currently preparing for a second reading of a draft law which would amend the RF Law 'On Limited Liability Companies' (the "LLC Law") (the "Draft LLC Amendments"), significantly affecting the legal status and procedures governing LLCs in the RF. The most significant changes proposed are summarized below.

### Establishment

Under the LLC Law, an LLC is liable for the obligations of its founders related to the establishment of the LLC only if the founders' actions are subsequently approved by the general participants' meeting. The Draft LLC Amendments limit the liability of founders to 1/5 of the paid in charter capital of the LLC.

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UKRAINE

## Major Revamp of Securities Law

The end of March saw the Ukrainian parliament pass a new law "On Securities and the Capital Market" (the "Securities Law"), intended to replace the very outdated 1991 Securities Act and meet the growing demands of the burgeoning Ukrainian securities market. The Securities Law came into effect on May 12, 2006, and provides a unifying framework for the securities laws enacted in Ukraine to date. It also seeks to regulate areas ignored by previous legislation, such as the disclosure of information on the securities markets.

The biggest impact of the Securities Law appears to be in the area of protection of rights of

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POLAND

## New Lobbying Law Opens Legislative Process to Lobbyists and Interested Parties

March 2006 saw the entering into force of a law which both regulates professional lobbying and encourages public participation in the lawmaking process in Poland. While lobbying is highly regulated in the US, it has previously not been regulated or treated in a uniform manner in the EU.

The Act of July 7, 2005 "On Lobbying Activity in the Lawmaking Process" (the "Lobbying Law") i) defines professional lobbying, ii) regulates who may engage in professional lobbying and how, and iii) requires the government to make public not only officers' contact with lobbyists,

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The Draft LLC Amendments would extend the list of issues to be approved by the founders of an LLC at the foundation meeting, stipulating that the founders should elect at the meeting, if required, the audit committee (or auditor) and the external auditor. Also, the majority required to elect such auditing committee (or auditor) and the external auditor, as well as the management bodies of the LLC, would be increased from 2/3 to 3/4 of all of the founders' votes.

The Draft LLC Amendments establish that if a founder of the LLC does not make the required contribution to the charter capital within one year after the LLC's establishment, then the unpaid portion of the participatory interest would be transferred to the LLC and sold within six months after such transfer to other participants or, if not prohibited by the LLC's charter, to third parties.

### Constituent Documents

Under current Russian law, an LLC must have two constituent documents, which consist of the foundation agreement and the charter. According to the Draft LLC Amendments, the constituent document of an LLC will comprise only the charter. In addition, the Unified State Register of Legal Entities, rather than the charter, will include information on the size and nominal value of the participants' participatory interest in order to avoid the need to amend the charter each time there is a change in the participatory interests. The Draft LLC Amendments propose to replace the foundation agreement with an "Agreement on the Establishment of a Company" (the "Agreement on Establishment"), similar to the Law on Joint Stock Companies, which would not be considered a constituent document. The Agreement on Establishment would be executed by the founders and determine, *inter alia*, the joint activity of the founders related to the establishment of the LLC, the size of the charter capital, the nominal value of the participatory interests, and the procedure and schedule for the payment of contributions.

### Reorganization

The LLC Law currently permits the reorganization of an LLC into a joint stock company, a different liability company or a manufacturing cooperative. The Draft LLC Amendments would add partnership to the list of permissible entities into which an LLC may be reorganized.

### Elimination of Right of Withdrawal

One of the most significant changes proposed by the Draft LLC Amendments is the deletion of Article 26 from the LLC Law, which would eliminate the right of a participant to withdraw

from the LLC at any time and receive the actual value of its participatory interest in the LLC. If Article 26 were removed, should a participant decide to leave the LLC, its participatory interest must be sold to the other participants, third parties or the LLC, depending on the circumstances, in compliance with the right of first refusal rules. The elimination of this provision will likely encourage investors, particularly in closely held companies, to set up companies in the LLC form, instead of the joint stock company form, as the LLC form provides greater flexibility to shareholders in terms of corporate governance and eliminates the need to comply with securities law requirements. In the past, some investors have avoided the LLC form due to concerns about the possible economic impact of another participant withdrawing from the company and through a put of its participation interest to the company.

### Right of First Refusal

The Draft LLC Amendments would affect the right of first refusal rules. In particular, the Draft LLC Amendments clarify that the charter of an LLC may (i) provide for a disproportionate right of first refusal of the participants and (ii) establish a preliminary price at which the right of first refusal may be exercised by a participant or the LLC (currently, the right of first refusal may only be exercised at the price established for a third party sale). These rules may be provided for in the charter of the LLC at the time of its establishment or in amendments to the charter upon approval by a unanimous decision of the general participants' meeting. The Draft LLC Amendments indicate that if a participant does not exercise its right of first refusal, the other participants may purchase such participatory interests in proportion to their respective participatory interests. Such changes would provide greater flexibility to owners to agree on an exit strategy.

### Interested Party Transactions

The Draft LLC Amendments propose a number of changes to the interested party rules, most of which clarify existing provisions. One of the newly proposed rules would permit the general participants' meeting of the LLC to pre-approve an interested party transaction which may be concluded in the future. In such case, the general participants' meeting must agree on a maximum threshold amount for the transaction, and the decision would be effective until the next general participants' meeting. This again would provide greater flexibility to owners, who are often hampered by the interested party transaction rules which

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create uncertainty about subsequent approval of contemplated agreements with the owners, such as loan agreements or management support agreements.

### General Director Liability

The Draft LLC Amendments would make the general director jointly liable for increases in the charter capital made by increased valuation of the company's property. The general director must sign the application for the registration of the amendments to the charter of the LLC related to such increases in the charter capital. This application would serve as confirmation that the company has fulfilled its obligation related to such increases in the charter capital of the company (i.e., determination of the amount by which the charter capital may be increased through increased value of the company's property). Together with the company, the general director will be jointly liable in the amount of the value of such portion of the property which has not been transferred to increase the charter capital within three years after the registration of the increase of the charter capital.

The Draft LLC Amendments are currently being prepared for their second reading in the Russian State Duma, which is expected to occur some time near the end of June. /E.  
*Korotkova, N. Stenina*

### Factoring Licenses May Be Abolished

The RF Duma is considering an amendment to the Civil Code that, if ratified, will resolve an inconsistency in Russian law and open the door for any commercial entity to engage in factoring.

On April 14, 2006, the RF State Duma carried out the first reading of a draft federal law that would abolish the requirement in the RF Civil Code that factoring companies hold licenses (the "Factoring Amendment").

Factoring, which is also referred to as accounts receivable financing, is the selling of a company's accounts receivable at a discount to a factor who then assumes the credit risk of the account debtors and receives cash as the debtors settle their accounts.

Pursuant to the RF Civil Code, a company must hold a factoring license in order to engage in factoring. However, RF Law No. 128-FZ "On Licensing Certain Types of Activities", dated August 8, 2001 (the "Licensing Law"), does not require factoring companies to apply for such license. Thus, no agency exists to

issue factoring licenses. Due to this inconsistency in the law, participation in the factoring market has been limited to banks, which may trade in accounts receivable under the terms of their banking licenses.

If adopted, the Factoring Amendment would eliminate the existing conflict between the relevant provisions of the RF Civil Code and the Licensing Law and, therefore, would likely encourage the entry of new major factoring companies and suppliers into the Russian receivables market. According to Andrey Sharonov, the Head Deputy of the RF Ministry for Economic Development and Trade, the Factoring Amendment could result in an increase in the volume of the factoring market from 0.5% of the RF's GDP in 2005 to 3% of the RF's GDP in 2008<sup>1</sup>. /D. *Gubarev, O. Gorshkolepova*

### Payments to Universal Communications Services Reserve Fund Declared Unconstitutional

The RF Constitutional Court (the "Constitutional Court") recently ruled in favor of public communications network operators in a case initiated by the Koryaksky Autonomous District Duma.

The Constitutional Court declared unconstitutional Articles 59 (2), 59(3) and 60 of RF Law No. 126-FZ "On Communication," dated July 7, 2003 (the "Telecoms Law") for its failure to establish clear procedures to carry out the requirements of such law. The Telecoms Law introduced a new category of "universal communications services," which are services related to (i) public pay phones; and (ii) data transmission and access to the Internet through the use of shared sites. The Telecoms Law provided that any losses incurred by the operators of such services would be recoverable from a special reserve fund which would be funded by all public communications network operators through the payment of mandatory fees<sup>2</sup>. The purpose of the fund is to encourage the development of a telecommunications network in Russia.

The Telecoms Law failed to set out specific procedures for the payment of such fees to the reserve fund, leaving it to the RF

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<sup>1</sup> Please see <http://www.sostav.ru/print/rus/2006/17.04/news/72>.

<sup>2</sup> For a review of the Telecoms Law, please see A. Kelina. "New Telecommunications Law is Finally Adopted." *CIS and Central Europe Legal Newswire*. September 4, 2003.

Government to adopt an appropriate mechanism in the future. In accordance therewith, on April 21, 2005, the RF Government issued Decree No. 243 on "the Procedures for the Creation and Expenditure of Universal Services Reserve Funds," establishing the base, period, rates, and procedures for calculating and paying the mandatory fees to the reserve fund, which the Constitutional Court ruled unconstitutional. This ruling is consistent with prior decisions of the Constitutional Court on similar matters. For example, the Constitutional Court had previously ruled that taxes and fees must be explicitly established by law and that such law must also provide for a mechanism for the payment of such taxes or fees (e.g., Decree No. 9-P, dated April 4, 1996; Decree No. 16-P, dated November 11, 1987).

In order to avoid impacting the federal budget for the year 2006, the Constitutional Court ruled that Articles 59(2), 59(3) and 60 of the Telecoms Law may be enforced until January 1, 2007, at which time the Telecoms Law must comply with the Constitutional Court ruling. If the Telecoms Law is not brought into compliance with the Constitutional Court ruling by such date, public communications network operators would not be required to pay fees to the reserve fund unless the necessary changes to the law are made. /A. Kelina

## The Russian Depository Receipt - Russia May Permit Distribution of Foreign Securities

The RF State Duma is currently preparing for the first reading of amendments to the law "On the Securities Market" which would provide for the introduction of Russian Depository Receipts ("RDR") in Russia (the "Draft RDR Amendments").

Currently, non-Russian or foreign securities may only be publicly circulated or issued on the Russian securities market if a respective prospectus is registered, which, in turn, is only possible where a relevant international treaty with the issuer's country has been entered into. Since no such international treaties have been entered into, foreign securities, in practice, may not be publicly issued or sold in Russia. Thus, the Draft RDR Amendments would permit foreign securities to be circulated on Russian exchanges in RDR form, a long anticipated opportunity for foreign issuers.

The RDR would be very similar to the American Depository Receipt (ADR) and Global Depository Receipt (GDR): an RDR

would certify entitlement to a certain amount of shares or bonds of a non-Russian issuer and confirm the right of the holder to demand a respective amount of shares (bonds) from the issuer. The Draft RDR Amendments set forth requirements for RDR issuers comparable to those for ADR and GDR issuers. An RDR issuer may choose to enter into an agreement with any issuer of securities represented by RDRs or proceed unsponsored, unless otherwise required by foreign law.

However, certain of the provisions of the RDR Amendments would require further input from the Federal Financial Markets Service ("FFMS"), without which the law would not work. In particular, this relates to two areas:

*Foreign Custodian.* The FFMS must approve a list of permissible foreign custodians from whom shares may be issued in RDR form by a Russian custodian.

*Foreign Stock.* Only stock which is traded on foreign exchanges included in the list to be approved by the FFMS may be used to issue RDRs.

In addition, the Draft RDR Amendments set forth the following requirements that local custodians must meet in order to become an RDR issuer:

- (i) local custodians must be established under the laws of the Russian Federation and be licensed to operate in Russia;
- (ii) custodians must hold an account with an "admitted foreign custodian" (i.e., one included in the list to be approved by the FFMS), and all rights of a custodian as an RDR issuer with respect to the represented shares must be properly reflected on such account;
- (iii) a custodian must have been operating in Russia for three years.

The RDR issuance procedures would include the following 3 steps:

- (1) adoption of the decision on RDR issuance, which would include procedures for exercising voting rights of the RDRs;
- (2) state registration of the RDR issuance; and
- (3) placement of the RDRs.

The RDR placement procedures would contain some unusual features in comparison with other securities. For instance, in contrast to the requirements for the placement of other Russian securities, where an issuer is required to complete a placement within a one-year term and register a placement

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report afterwards, an RDR would not be held to such one-year term. The RDR issuer would only be required to first state the maximum amount of RDRs that it will place, and then quarterly register a placement report for the quarters in which it decides to place the RDRs. Such report must contain information on the quantity of RDRs placed in a certain reporting period, the outstanding amount of RDRs to meet the maximum quantity stated by the issuer, and the quantity of securities represented by RDRs.

The Draft RDR Amendments are still in the first stages of development, but are expected to be adopted by the end of 2006. /T. Sharipov, K. Konstantinov

## Currency Restrictions Lifted Ahead of Schedule

The RF Central Bank (the "CBR") recently has announced that the requirement to hold special transaction accounts and non-interest reserves for certain transactions will be lifted on July 1, 2006, as opposed to the original deadline of January 1, 2007.

The restrictions were introduced by the CBR in accordance with RF Law No. 173-FZ "On Currency Regulation and Currency Control", dated December 10, 2003 (the "Currency Control Law")<sup>1</sup>, which regulates convertible currency transactions between residents and non-residents. In accordance with the restrictions, borrowers must use a "special account" for, e.g., loans with a pay-back period of three years or less, and are required to deposit 1% of the amount of such loans in an interest-free account with a Russian bank before the loan can be disbursed.

The announcement came on May 30, 2006, just less than three weeks after RF President Vladimir Putin proposed the initiative in his annual address before the Federal Assembly. This is yet another positive step forward in encouraging financing in the RF and moving towards full convertibility of the Russian ruble. It also follows the decision by the CBR on March 29, 2006, which became effective in May, to eliminate the mandatory conversion of hard currency proceeds into rubles. Previously, companies were required to convert 10% of their export proceeds into rubles. Over the last few years, the requirement had dropped from 50% of such proceeds. /D. Gubarev

<sup>1</sup> For more on the RF Currency Control Law, please see E. Abrossimova, K. Konstantinov and O. Titenko. "New Currency Control Law Liberalizes Currency Transactions." *CIS and Central Europe Legal Newswire*. February 12, 2004; and A. Kelina. "Liability for Currency Law Violations Toughened." *CIS & Central Europe Legal Newswire*. December 7, 2004.

## UKRAINE

### Major Revamp of Securities Law

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shareholders, and particularly minority shareholders. The Securities Law has significantly expanded the obligation of an issuer to disclose information about itself, its main shareholders and matters affecting its securities. Also, before the Securities Law was passed, Ukraine had no legally defined concept of insider information, nor was there a requirement not to use such information to the detriment of other share holders. As a result, foreign and Ukrainian investors should be better able to make informed investment decisions on Ukrainian securities. Investors have also been provided with legal remedies to protect against fraudulent practices in the securities market. An indirect effect of the Securities Law should thus be increased investment flows into Ukrainian securities from abroad. Below is a summary of the major changes introduced by the law.

#### Classification of Securities

The Securities Law distinguishes between issuance and non-issuance securities. Issuance securities are issued pursuant to a statutory procedure and confer equal rights on their owners. They include shares, bonds, mortgage certificates, mortgage bonds, real estate operation funds certificates, investment certificates and treasury notes of Ukraine. Non-issuance securities are created individually, and include certificates of deposit, mortgage notes, promissory notes and drafts.

The Securities Law further recognizes share securities (company shares and investment certificates), bond securities (company bonds, municipal bonds, state bonds, treasury notes, deposit certificates, promissory notes/drafts), mortgage securities (mortgage bonds, mortgage certificates, mortgage notes, real estate operation funds certificates), privatization securities, derivative securities, and title securities (warehouse receipts, etc.). The Securities Law further classifies securities by form of issuance (in documentary and non-documentary form) and method of transfer (bearer, registered and order securities).

#### Shares and Bonds

The Securities Law introduces the concept of a securities prospectus for disclosing information about the securities,

provides for the registration of each issue of share securities or bonds and the prospectus and sets out the steps and procedures to be followed in issuing shares/bonds.

The Securities Law distinguishes between public and private placements and imposes different obligations on issuers depending on whether an issuance is private or public.

Shares are issued by joint stock companies, and only in registered form. A share must be assigned a nominal value set in Ukrainian currency. Shares may be common or preferred. Common shares accord their owners equal rights, such that no different classes of common shares can be instituted, and cannot be converted into preferred shares or other securities of the issuer. Preferred shares may be of different classes and may be convertible into common shares or preferred shares of other classes. Preferred shares cannot exceed 25% of the share capital of a company.

The Securities Law provides for several categories of bonds, including company bonds, municipal bonds and the state bonds of Ukraine. The Securities Law further permits interest bonds, discount bonds and special purpose bonds (that entitle holders to specific goods or services from the issuer). From 2008, companies will be able to issue bonds for an amount equaling either (i) three times the company's share capital or (ii) an amount guaranteed by a third party, whichever is greater. Until 2008, there (unusually) does not seem to be any limitation on the amount of the bonds issue: the new Securities Law repealed both the old Securities Law limit of 25% of the share capital of the company, and the Civil Code limitation of 100% of the share capital of the company.

Shares and bonds (except for state bonds) come into existence only after the registration of their issue by the Ukrainian Securities Commission. Prior to registration, transactions with shares and bonds are prohibited.

### Disclosure of Information

The Securities Law provides for the disclosure of information about the issuer of publicly placed shares and material events potentially affecting the price of shares and holders of large blocks of shares (from 10%).

Regular information concerning the finances and business of an issuer must be filed with the Ukrainian Securities Commission annually and quarterly. Annual information includes, in particular, the name and location of an issuer, its management, business and financial operations, issued securities, annual financial reports and an auditor's report. Essentially the same information is filed on a quarterly basis,

except quarterly financial reports and information on participation of an issuer in other companies also must be filed.

Special information is information about events affecting an issuer that may result in a material change in value of its shares. Such events particularly include placement by an issuer of securities in excess of 25% of its share capital, redemption by an issuer of its shares, listing or delisting of shares of an issuer on a stock exchange, an issuer obtaining loans in excess of 25% of its assets, a change in the officers of an issuer, a change of shareholders owning 10% or more of the shares, and the reduction in the share capital of an issuer.

### Insider Information

The Securities Law defines insider information as any information not publicly disclosed about an issuer or its securities or transactions with its securities, the disclosure of which may materially affect the securities' value. Under the Securities Law, insiders include persons in possession of insider information due to the fact that they are owners of voting shares of an issuer, officers of an issuer, or persons with access to insider information in connection with their employment or contractual relations (e.g., lawyers, accountants, consultants, etc).

The Securities Law makes it illegal for an individual to use insider information to (i) enter into contracts on his or her behalf or on behalf of other persons involving the acquisition or transfer of shares subject to insider information and (ii) disclose insider information to third parties, or make recommendations on the acquisition or transfer of shares before public disclosure of such information. Securities traders and other members of the securities markets are required to report to the Securities Commission transactions suspected to be based on insider information. The Securities Law introduces criminal liability for the unauthorized disclosure of insider information. */V. Fedichin*

### Elections Update

On March 26, 2006 parliamentary and local elections were held in Ukraine based, for the first time in Ukrainian history, on the proportional representation system. The proportional representation system, a single nation-wide electoral district with votes allocated to political parties or election blocs

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rather than to individual candidates, was implemented by recent constitutional reform<sup>1</sup>.

Forty-five political parties and blocs endeavored to win the 3% of votes necessary to receive representation in the parliament, but only five of them managed to do so. According to the official results announced by the Central Election Commission on April 10th, the Pro-Russian Party of Regions won 32.14% of the vote; the three more western oriented parties - the Yulia Tymoshenko Bloc, the Our Ukraine Bloc and the Socialist Party of Ukraine - won, respectively, 22.29%, 13.95% and 5.69% of the vote; and the Communist Party of Ukraine won 3.66%.

In general, the elections were called "the most democratic" in Ukrainian history, conducted in a free, open and transparent manner.

However, a number of political parties and blocs that did not cross the 3% threshold needed for parliamentary representation brought suit against the Central Elections Commission (CEC), contesting the election results in court. On April 25, 2006 Ukraine's Higher Administrative Court ruled in favor of the CEC, and, on April 27, 2006 the results of the election were finally validated and were published in official Ukrainian publications.

With effect from April 27, 2006, the parliament has one month to assemble, two months to form a majority, and three months to nominate members to the Cabinet of Ministers. The first step towards formation of the future coalition was taken on April 13, when the Socialist Party of Ukraine, the Yulia Tymoshenko Bloc and the Our Ukraine Bloc signed the Protocol on the Coalition of the Democratic Forces. These three parties have agreed on the structure of the coalition agreement, comprising three sections: the program/agenda of the coalition, the coalition regulations and the division of responsibility among the participants of the coalition.

However, as of May 23, 2006, the coalition has yet to be formed. The political forces are still negotiating on the major issues of the future coalition, including the future policies and priorities of Ukraine, and on the person to occupy the position of Prime Minister. While these negotiations continue, many analysts believe that the Our Ukraine Bloc is also holding alternative negotiations with the pro-Russia Regions' Party (although the Our Ukraine Bloc has denied that

any such discussions are taking place).

The latest date that a parliamentary coalition can be formed is June 27, 2006, and most politicians expect that the democratic parliamentary coalition will be formed by early June. If no coalition is formed by June 27, 2006, the reformed constitutional provisions require that new elections are announced and held.

If the parliamentary coalition of the three pro-Western parties (the Socialist Party of Ukraine, the Yulia Tymoshenko Bloc and the Our Ukraine Bloc) is formed by the end of June, a new government will, most likely, consist of representatives from these three parties. Not only would this be a major step towards strengthening these forces on the Ukrainian political scene, but any such coalition would also affect the state's policies in the business arena. While in some jurisdictions the existence of a parliamentary coalition can slow down the decision-making process, in Ukraine, analysts predict that the existence of an effective coalition between the Socialists, the Yulia Tymoshenko Bloc and the Our Ukraine Bloc (i.e. a coalition which agrees its program/agenda in advance) would result in faster implementation of democratic and economic reforms in Ukraine. /O. Burlyuk, D. Fedoruk

## Enforcement of Decisions of the European Court for Human Rights

On March 20, 2006, the President of Ukraine signed into law Law No. 3477-IV "On the Procedure for Enforcement of Decisions of the European Court for Human Rights." This law is a further step in the process of bringing Ukraine's enforcement system in line with international standards.

Because Ukraine is a party to the Convention for the Protection of Human Rights and Fundamental Freedoms, dated November 4, 1950 (also known as the European Convention on Human Rights), any natural person or legal entity which has reason to believe that his or her or its rights have been violated under the Convention by the State of Ukraine may take a case to the European Court of Human Rights (the "ECHR"). Technically, natural persons and legal entities are allowed to apply to the ECHR only in cases where all national means of defense against an allegedly incorrect decision have been exhausted.

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<sup>1</sup> For more on the constitutional reforms, please see A. Putintseva. "Ukraine's Constitutional Amendments Take Effect on January 1, 2006." *CIS & Central Europe Legal Newswire*. March 21, 2006.

The number of applications to the ECHR seeking the reversal of decisions of Ukrainian national courts has been increasing tremendously in recent years. In 2005, Ukrainian citizens submitted 2,457 applications to the ECHR.

Both Ukrainian and foreign legal entities may also apply to the ECHR to reverse the decisions of Ukrainian national courts, and have been doing so quite successfully. Probably the most well-known case is *Sovtransavto Holding vs. Ukraine* in which the ECHR ordered the State of Ukraine to pay Sovtransavto, a Russian company, EUR 625,000 in damages.

Despite the success of applicants to the ECHR, the enforcement of decisions in Ukraine has proved to be very time consuming and unpredictable. The new law emphasizes Ukraine's obligation to diligently enforce the decisions of the ECHR and would generally appear to be an important step towards harmonization of Ukrainian law with international norms and principles in the area of human rights. /O. *Burlyuk*, D. *Fedoruk*

## Foreign Employee Requirements Clarified

The Ukrainian authority charged with the issuance of work permits has recently clarified the law relating to the employment of foreigners in Ukraine (Letter of the State Employment Center dated March 24, 2006, No. DTs-12-1556/o/6-06 "Concerning the Use by Employers of Foreign Nationals and Persons without Nationality as Hired Labor").

The State Employment Center has confirmed that foreigners who come to Ukraine to work can do so only subject to a work permit. However, no work permit is required for employees of representative offices of foreign firms registered by the Ministry of Economy of Ukraine (i.e., in the normal manner applicable to the registration of foreign representative offices). The State Employment Center also clarified that work permits are not required for foreigners working in Ukraine as 'independent contractors'. This is an important point, since there had been uncertainty as to the legal treatment of independent contractors, and particularly the extent of risk of re-characterization of independent contractors as employees by the labor authorities. It follows from the clarification, however, that where foreigners operate in Ukraine as truly independent contractors, they should not require work permits and should not face the risk

of reclassification as employees.

This development should be seen as a positive move for businesses wishing to engage foreign nationals. Not only has the process of obtaining a work permit always been a time-consuming process in Ukraine, it is also never guaranteed, as an employer must show that there are no Ukrainian nationals able to perform the work for which a work permit is sought. /V. *Fedichin*

## Graduation of Ukraine from the Jackson-Vanik Amendment

On March 23, 2006, U.S. President George W. Bush signed into law House of Representatives Bill No. 1053, graduating Ukraine from the Jackson-Vanik Amendment, thus granting normal trade status to Ukraine.

The Jackson-Vanik Amendment was enacted into U.S. law in 1974 to put pressure on communist countries who were restricting emigration. The Jackson-Vanik Amendment still applies to Russia, Kazakhstan and Belarus.

The purpose of the Jackson-Vanik Amendment was to treat Ukraine and other such countries at the time as non-market economies for the purposes of U.S. trade law, which had a number of negative consequences on trade for Ukraine. It denied "normal trade relations" status on a permanent basis, and limited the amount of credit available to U.S. exporters from a number of government agencies, especially the U.S. Export-Import Bank. The imposition of trade restrictions and increased taxes and tariffs on Ukrainian exports caused particular problems to companies operating in the light industry and metallurgical sectors in Ukraine.

As a result of the removal of Ukraine from Jackson-Vanik status, Ukrainian imports to the U.S. will now be treated more favorably, which should give a boost to Ukrainian exports.

The graduation from the Jackson-Vanik Amendment complements the U.S. move on February 17, 2006 to grant Ukraine market economy status, and the WTO bilateral protocol signed on March 6, 2006, between the U.S. and Ukraine. /E. *Cook*

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## Ukraine Enacts a New Law on Holding Companies

A new law has been introduced governing the creation, operation and liquidation of holding companies in Ukraine, but foreign investors and Ukrainian companies alike will be disappointed that the new law raises more questions than it answers. Not only does the new law restrict the ability of private companies to qualify as a holding company, it also fails to provide the legal mechanisms for preferential tax treatment or other advantages which holding companies in other jurisdictions enjoy. Significant further amendments are required for a holding company to be considered a beneficial corporate structure in Ukraine in terms of strategic tax planning and management.

The Law "On Holding Companies in Ukraine" (the "Holding Companies Law") came into effect on April 18, 2006. All holding companies and their subsidiaries established in Ukraine before this date must bring their foundation documents into compliance with the requirements of the Holding Companies Law within 3 years<sup>1</sup>. The Holding Companies Law contains a significant number of regulations specifying the rules governing the formation, decision-making process, liability and liquidation of holding companies. The following points are of particular note:

### New Criteria

The Holding Companies Law restricts the ability of a company to qualify as a holding company in that it requires the company to meet each of the following three criteria in order to qualify: (a) it must be an open joint stock company; (b) it must own corporate rights in two or more other companies; and (c) it must *either* control more than 50% of the shares in at least two other companies *or* must ensure decisive influence on the economic activity of at least two other companies.

These new criteria therefore preclude limited liability companies and closed joint stock companies from becoming holding companies as defined under the law, even if they have full control or ownership over several other companies. Similarly, a company owning or otherwise controlling only one subsidiary company cannot be a holding company, as it

<sup>1</sup> Previous legislation did not govern the creation of private holding companies (only those holding companies established in the process of privatization and corporatization), and the Holding Companies Law contains a recommendation that the President cancel this earlier legislation.

must own 50% + 1 share in each of two or more companies. Since private companies are more frequently established in the form of limited liability or closed joint stock companies, the Holding Companies Law significantly restricts the ability of private companies to establish holdings (compared to state companies, which are generally organized in the form of open joint stock companies). A limited liability company or joint stock company that would otherwise meet the holding company requirements, will thus be required to re-organize into an open company and then register as a holding company.

The name "holding company" may only be used by those companies whose founding documents and activity are in line with the Holding Companies Law. A legal entity cannot call itself a "holding company" unless it is registered in the form of a holding company.

### Holding Company Creation

Article 3 of the Holding Companies Law stipulates that holding companies may be established by: (a) the bodies authorized to manage state property; (b) state privatization bodies; (c) state privatization bodies together with other founders; and (d) other entities on contractual terms. In certain circumstances, the founders of a holding company must obtain the preliminary approval of the Antimonopoly Committee (the "AMC") prior to filing its foundation documents with the relevant registration authorities.

### Mandatory Disclosures

Under the Holding Companies Law, holding companies are required to disclose specific information in the official printed media of the State Commission on the Securities and Stock Market and must publicize their own and their subsidiaries' consolidated financial reports at least once a year. Failure to file, late filing or filing false information can result in fines being levied on the holding company (of up to 1,000 times the non-taxable minimum income (UAH 17,000, or US \$3,370)) and the company's chief executive (of up to 50-100 times the non-taxable minimum income (UAH 850 - 1,700, or US \$168-337)).

### Notable Absences

The Holding Companies Law fails to address a number of significant issues, including the administration of a holding company. Nor does it regulate the interaction of a parent company with its subsidiaries, or the exercise of control by a

holding company over its subsidiaries. The Holding Companies Law also fails to provide any regulation of the rights of subsidiary enterprises, so that subsidiaries could fully realize their rights as independent economic entities.

Furthermore, the Holding Companies Law does not include any provisions for preferential tax treatment of holding companies, which will not provide any incentive to investors to use Ukrainian holding companies in their tax planning, a practice common in more developed countries. For example, if a Ukrainian holding company carries out no operations but owns shares in two or more subsidiaries, each of the subsidiaries will be required to pay an advance corporate tax (the "ACT") of 25% on any dividends it pays to its holding company. Each subsidiary is then permitted to deduct the ACT from its future profit tax obligations. However, when the holding company pays out dividends to its own shareholders, it also must pay a 25% ACT - but since the holding company has no taxable earnings of its own (dividends do not qualify as taxable income), it is unable to set off the ACT against future profit tax payments. So, while the holding company keeps building up its 25% ACT credit, it is unable to utilize that credit. The result is that an additional 25% is effectively lost to tax in such a structure unless the holding company engages in other activities that generate taxable income, against which the 25% ACT on dividends can later be offset. */A. Putinsteva*

POLAND

## New Lobbying Law Opens Legislative Process to Lobbyists and Interested Parties

*(Continued from page 1)*

but also upcoming legislation.

Professional lobbying is defined as lobbying conducted for the benefit of third parties in order to have their interests taken into consideration by public authorities in the lawmaking process.

In order to engage in lobbying activity, a lobbyist must register in the professional lobbyists' register, which is maintained by the Minister of Internal Affairs and Administration in accordance with the Lobbying Law. Data contained in the register is publicly available and published in the official Public Information Bulletin

(the "PIB") on the Internet. In the two months since the Lobbying Law become effective, almost 50 entries have been made in the register.

Registered lobbyists are entitled to engage in lobbying on the premises of the public authorities and the Parliament and to contact government officials. The officials must register such contacts, and information on the lobbyists' activities is also published in the PIB.

In order to make the lawmaking process more transparent and to allow interested parties to take part in the process, the Lobbying Law requires that the Council of Ministers prepare, at least every six-months, a legislative schedule concerning the acts directed to the Parliament. The schedule must contain information explaining the reasons for the new draft legislation, outline the essence of projected solutions to be implemented, as well as indicate the authority in charge of preparatory works on the act. Similarly, the Council of Ministers and the ministers prepare an executive act (ordinance) schedule.

All of this information, along with drafts and other documents relating to the legislation, is published in the PIB. A party interested in participating in review of a proposed regulation (not limited to professional lobbyists) may file a notice to the relevant authority indicating the interests such party will support, and the suggested solutions.

The Lobbying Law also introduces the institution of public hearings on proposed regulations, in which those notified interested parties are entitled to participate. Protocols from public hearings are published in the PIB. */L. Oldakowski*

KYRGYZ REPUBLIC

## New Rules Restrict Alcohol, Tobacco and Gambling Advertising

On February 6, 2006, the Parliament of the Kyrgyz Republic (Kyrgyzstan) adopted a series of amendments that significantly limit the advertisement of alcohol, tobacco and gambling and provide for greater penalties for the violation of such provisions. New amendments to the Law "On Advertisement" prohibit the advertisement of alcohol and tobacco products through radio, television, and through outdoor advertisement. The display of advertisements for alcohol and tobacco immediately prior, during or after movies in theaters and similar institutions, unless the audience is limited to adults, is also now prohibited.

Also prohibited is the widespread distribution of free samples of alcohol and tobacco products, as well as the public sponsorship of events primarily geared toward minors and the sale of goods unrelated to alcohol and tobacco product consumption (e.g., T-shirts, headwear, umbrellas, bags) with illustration of names and/or images of alcohol or tobacco products visibly displayed (exceptions include ash-trays, lighters, matches, trays and others goods used in bars, restaurants, hotels and similar establishments).

Additionally, Kyrgyz legislators have supplemented the Criminal Code of the Kyrgyz Republic with a new article that introduces penalties for violating the provisions on advertising alcohol, tobacco and gambling activities, in particular, imposing a fine in the amount equal to 20 to 30 specified rates<sup>1</sup> or incarceration for up to six months. The same offences committed by government officials or editors of mass media shall be subject to imprisonment for up to three years.

The Amendments were introduced by the Law of the Kyrgyz Republic "On the Amendments to the Law of the Kyrgyz Republic 'On Advertisement', the Code of Administrative Responsibility of the Kyrgyz Republic and Criminal Code of the Kyrgyz Republic and Criminal Procedural Code of the Kyrgyz Republic" dated February 6, 2006, No. 35 (effective date February 14, 2006). /*Kalikova & Associates*

*Bishkek, Kyrgyz Republic. www.k-a.kg*

<sup>1</sup> "Specified rates" is a new term recently introduced by the Law of the Kyrgyz Republic dated January 26, 2006, No. 16 to replace the term "minimum monthly wage", which was previously used for the calculation of fines, etc.

BELARUS

## New Law on Companies

On August 2, 2006, a new edition of the Law on Joint Stock Companies, Limited Liability Companies and Additional Liability Companies, will come into effect, renamed as the Law on Economic Companies. The Law on Economic Companies, adopted on January 10, 2006, introduces many novelties into the legal regulation of companies created by two or more founders, i.e., open and closed joint stock companies (JSCs), limited liability companies (LLCs)<sup>1</sup> and additional liability companies (ALCs). Some of the significant changes are as follows:

### Number of Shareholders

- the maximum number of shareholders in closed JSCs, LLCs and ALCs is now limited to 50 shareholders (participants)
- a company exceeding the limit must reorganize within one year into an open JSC, for which such limits are not fixed

### Charter Capital Formation

- the formation of capital from only proprietary rights is no longer allowed
- the volume of investment in the form of rights must not exceed 50% of the minimum size of authorized capital (e.g., if the minimum capital of an LLC is EUR 1600, even if the actual capital is 5000 EUR, the maximum volume of investment of proprietary rights may not be more than 800 EUR)

### Share Transfers

- if the participant of an LLC or ALC fails to pay for all of its interest within the term set by the statutory documents and the law, its share is transferred to the LLC or ALC accordingly

### Subsidiaries

- a subsidiary company is now defined as a company in which a parent company holds 20% or more of the authorized capital
- subsidiaries are prohibited from making investments into the parent company

*(Continued on page 12)*

<sup>1</sup> LLC is the most popular form of company in Belarus.

### Voting in Open and Closed JSCs

- previously, voting was held on the basis of one share-one vote whereby shareholders do not vote; now, one voting share has one vote, except for in cumulative voting (wherein the number of votes of each shareholder is multiplied by the number of candidates)
- also, in certain cases, preferred shares can vote

### Affiliated Persons

- affiliated persons were previously undefined; now, affiliated persons are defined as persons (including legal entities) who can determine or influence the company's decision-making
- the company will need to account for these persons
- there is now a special procedure for carrying out some types of transactions between the company and affiliated persons

### Preemptive Share Purchases in LLCs & ALCs

- previously, preemptive rights were observed only for shareholders; now, if shareholders refuse to buy the shares on the terms set by the seller, the company itself can buy the shares
- if neither shareholders nor the company itself are interested in the purchase, the share can be sold to third persons if not prohibited by the statutory documents of the company

The Law on Economic Companies also affects, among other things, the order of the companies' foundation, the order of reorganization, activity of the company corporate bodies, large transactions, use of preferred shares, and exclusion of a shareholder from an LLC, and also introduces a range of additional requirements to the statutory documents of companies.

After the Law on Economic Companies comes into force, all JSCs, LLCs and ALCs must amend their charters and statutory agreements in accordance with the requirements of the new law and register the amendments within one year (i.e., by August 2, 2007). /A. *Vashkevich*

*Borovtsov & Salei Legal Services*

## RECENT DEVELOPMENTS

### FORMER US EX-IM BANK LAWYER JOINS CIS PRACTICE, EXPANDING ST. PETERSBURG OFFICE

Paul Tumminia, formerly the Director for Russia, the CIS and Turkey at the U.S. Export-Import Bank, joined Chadbourne's St. Petersburg Office as counsel in April.

Mr. Tumminia has over a decade of hands-on experience working on major projects in the banking, energy, and manufacturing sectors in Russia and the CIS. He has also served as chief liaison officer to senior government leaders in the region and to U.S. government agencies with respect to new products and programs he helped to design and develop. Among other things, Mr. Tumminia led the Ex-Im Bank team charged with conducting due diligence (legal and financial) on the Russian banking sector, and monitored compliance and progress of projects for major borrowers at Ex-Im Bank. Mr. Tumminia also served as Country Director in Tallinn, Estonia for the Baltic-American Enterprise Fund, providing support for small- and medium-sized enterprises in the Baltics.

Mr. Tumminia holds a B.A. from Haverford College, an M.A. from Yale University and a J.D. from the University of California, Los Angeles.

While based in St. Petersburg, Mr. Tumminia will work throughout the CIS on financing and corporate matters.

### KEN MACK, MANAGING PARTNER OF ALMATY OFFICE, ELECTED PRESIDENT OF AMERICAN CHAMBER OF COMMERCE IN KAZAKHSTAN

Kenneth Mack, Managing Partner of Chadbourne's Almaty office, was recently elected President of the American Chamber of Commerce ("Amcham") of Kazakhstan. Mr. Mack feels honored to take on this role during a time of intense growth in foreign investment in Kazakhstan. Kazakhstan has attracted billions of dollars of investment from many of the major oil companies in the world, as well

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as from leading international banks and infrastructure companies. The Amcham in Kazakhstan is currently hosting various discussions on initiatives to support the interests of American and other foreign companies, as well as to promote progressive economic and regulatory policies of the Republic of Kazakhstan that would further its development and in the process, create a thriving investment climate. Mr. Mack's goal as President of Amcham is to support Central and South Asian regional integration and to advance substantial commercial, investment and policy objectives.

Mr. Mack was also published recently in the *International Energy Law & Taxation Review*. For a copy of his article entitled "Protection of the Oil and Gas Investor's Rights in Kazakhstan," please refer to the Chadbourne website or contact Iverson Long (ilong@chadbourne.com).

## KYIV OFFICE CLOSES ANOTHER MAJOR BANK ACQUISITION

Chadbourne represented Crédit Agricole S.A. Group in the acquisition of at least 98% of the share capital of JSC Index Bank of Ukraine. Leading the Chadbourne team on the deal were London partner David Levin and Kyiv partner Jaroslawa Johnson.

The deal, signed March 24, includes a stock sale agreement with Index Bank shareholders under which Crédit Agricole agreed to pay US\$260 million for existing and new shares of Index Bank. Index Bank, with assets of US\$460.4 million, was created in 1993 and now ranks among Ukraine's leading banks with 186 offices including 25 branches throughout the country. Index Bank's operations, along with those of Calyon Bank Ukraine, one of the country's major foreign corporate and investment banks, will enable Crédit Agricole to expand its position in the growing Ukraine market. Completion of the deal is subject to obtaining approval from the National Bank of Ukraine (Ukraine's central bank) and the Ukrainian Anti-Monopoly Committee.

## CHADBOURNE ADVISES POLAND'S STATE OIL & GAS COMPANY IN FEASIBILITY STUDY OF PROPOSED LNG PROJECT

Chadbourne has been appointed legal counsel to Polskie Gornictwo Naftowe i Gazownictwo SA (PGNiG), Poland's state-run gas company, to advise in the preparation of a

feasibility study on the development of a liquefied natural gas terminal as part of the State's plan to reduce its dependence on current gas supplies (the "Project"). Representing Chadbourne on the Project are Warsaw partners Igor Muszyński and Kazimierz Jeleński. Other members of the team include Dave Schumacher from Chadbourne's Houston office and Noam Ayali from Chadbourne's Washington DC office.

Chadbourne is part of a select consortium of advisors representing PGNiG on the Project, conferring with PricewaterhouseCoopers LLP and engineering consultant ILF Beratende Ingenieure GmbH to evaluate the plans to build the first LNG terminal on Poland's Baltic Sea coast.

By the year 2011, PGNiG expects the Project to import 3 billion to 5 billion cubic meters of gas per year. Poland consumes more than 13 billion cubic meters of gas per year, about two-thirds of which is imported, either from Russia or from other former Soviet countries via pipelines through Russia.

## AT THE PODIUM

### Recent Presentations by CIS and Central Europe Practice Attorneys:

#### Projects International 2006

(Paris, March 14-17). Peter Fitzgerald, Senior Partner in the London office, moderated a panel discussion entitled "Practical & Effective Strategies for Working with ECA & Multilaterals." Laura Brank, Head of the Russia and CIS Practice, spoke about "Effective Development Strategies For Infrastructure Projects in Russia & the CIS." The conference provides strategies for effectively financing, allocating risk and creating value for money in projects globally.

#### Kazakhstan Investment Summit

(London, March 15-17). Chadbourne sponsored this first of its kind Adam Smith Summit, which presented detailed, cross-section coverage of the economic development, investment climate and commercial opportunities in Kazakhstan. Kenneth Mack, Managing Partner of the Almaty office, moderated a panel on investors' views of economic developments in Kazakhstan, i.e. the strategy to diversify, pitfalls and what could be done to solve potential problems, and the pros and cons of investing in Kazakhstan.

Mr. Mack opened the session by delivering a presentation on the general investment climate in Kazakhstan.

## Trade & Project Finance in Russia

(Moscow, March 28-30). Laura Brank, Head of the Russia and CIS Practice, spoke at the second annual conference on trade and project finance, delivering a presentation entitled "Trade and Project Finance in Russia: Structuring within the Russian Legal Framework to Mitigate Risks and Maximize Value."

## Russo-British Chamber of Commerce St. Petersburg International Investment Forum "Live-link" with the London Stock Exchange

(St. Petersburg, April 18-19). Konstantin Osipov, Counsel in the St. Petersburg office, discussed Russian legal issues related to listings on the London Stock Exchange.

## IBC North Asian LNG and Pipelines

(Tokyo, April 19-20). Christopher Owen, Partner in the Moscow office, spoke at and chaired day two of the conference on "Aspects of LNG Project Financings in Russia". The conference focused on issues pertaining to LNG supply for Sakhalin, Sakhalin projects status, and updates and potential contracting problems and challenges.

## Ukraine International Energy Roundtable, "Strengthening Ukraine's Energy Diversity"

(Houston, May 1-3). Attending this conference, which included a number of high profile political figures from Ukraine and the U.S., were Kyiv Managing Partner Jaroslawa Johnson, Houston-based oil and gas partner David Schumacher and Washington-based oil and gas partner Noam Ayali. Chadbourne was a corporate sponsor of the event.

## Offshore Technology Conference

(Houston, May 1-4). Moscow-based partner Shane DeBeer delivered a presentation on the top ten legal issues to be considered by oilfield service companies operating or planning to operate in Russia. This year's conference was the largest ever, with the number of attendees at 59,236 from over 30 countries.

## World Russian Forum 2006

(Washington DC, May 16-18). Laura Brank, Head of the Russia and CIS Practice, delivered a presentation entitled "The

Current State of the Rule of Law in Russia from the Perspective of Foreign Investment" on a panel on "Building a Strong Economic Base for US-Russian Cooperation". The Forum included senior representatives from major corporates, oil and gas companies, organizations and political figures including His Excellency Yuri Ushakov, Russian Ambassador to Washington, and Congressman Curt Weldon.

## 2006 CIS Oil & Gas Summit

(Paris, May 31-June 2). Moscow-based partner Shane DeBeer delivered a presentation on key legal issues in investment in upstream and transportation projects in the CIS. The 2006 CIS Oil & Gas Summit looked in detail at the opportunities and developments that lie ahead for the oil and gas sectors in Russia and the CIS. Dedicated discussions included updates on key projects such as Shtokman, Sakhalin 1 & 2, and Kashagan, together with major export developments, financing and policy debates.

*If you would like a copy of Chadbourne papers and presentations delivered at these conferences, please contact Iverson Long (ilong@chadbourne.com).*

### UPCOMING

## Financing the Growth of Russian and CIS Companies on the London Stock Exchange

(June 22-23, London). Chadbourne's Russia and CIS Practice is sponsoring a FinLab (Financial Laboratory at the London Stock Exchange) annual conference on opportunities for Russian and CIS companies to raise capital in London. The conference is aimed at both mid-cap and larger Russian and CIS companies considering listing in London and other capital markets, and will answer some practical questions concerning the so called "Russian & CIS IPO boom" and sustainability of demand for Russian and CIS assets. Day one provides a platform on the future developments of the CIS IPO market, and day two deals with the practical aspects of preparation for listing and steps companies should take to ensure a successful IPO in London.

Chadbourne Attorneys Christopher Owen, Ken Mack, Adam Mycyk, and Konstantin Konstantinov will all be presenting.

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Some of the “hot” issues to be addressed at the conference:

- Will the optimistic forecasts be substantiated by the real listings and when?
- Who are these Russian/CIS companies and can they meet investors’ expectations?
- Will the demand for Russian and CIS IPOs continue to rise?
- What is the next “hot” thing coming from the CIS. Will it be Real Estate, hi-tech, or...?
- Are the Russian/CIS mid-caps ready for London listing?
- IPO – at what price and where? How does a London IPO rate against local listings?

The conference will take place at The Dorchester, London, and the London Stock Exchange.

**Note:** Recipients of this newswire are eligible for a 15% discount on the attendance fee.

*Please contact Faye Lynam in London (+44 (0)20 7337 8027, flynam@chadbourne.com) or Iverson Long in Moscow (+7 (495) 974-2424, ilyong@chadbourne.com) for more information.*

## KIOGE 2006 14th Kazakhstan International Oil & Gas Exhibition & Conference

(October 3-6, Almaty). Kenneth Mack, Managing partner of the Almaty office, and others will attend this Chadbourne sponsored annual exhibition and conference. Mr. Mack will participate in the session with the special focus on "Socially Responsible Oil and Gas Field Development".

## CIS AND CENTRAL EUROPE LEGAL NEWSWIRE

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