
June 2009 www.ssd.com

## Amendments to Russian Law Permit Shareholders' Agreements

On 9 June 2009 Federal Law No. 115-FZ, "On Introduction of Amendments to the Federal Law On Joint Stock Companies and Article 30 of the Federal Law On Securities Market" (the Revisions), was officially published in Russia and went into force.

The Revisions implement, among other things, amendments to the Federal Law "On Joint Stock Companies" and expressly provide that shareholders of Russia-based joint stock companies may enter into shareholders' agreements. Previously shareholders' agreements were neither directly prohibited nor permitted, but such agreements had been held to be void by some Russian courts for violating fundamental norms of Russian law.

The Revisions follow recent amendments to the Federal Law "On Limited Liability Companies," which was also revised to permit the execution of members' agreements and goes into effect on 1 July 2009. The Revisions, however, provide more guidance as to the form and substance of permissible shareholders' agreements.

### Russian Shareholders' Agreements

According to the new provisions introduced in the Revisions, a shareholders' agreement is "an agreement on realization of the rights provided by shares" and is binding only among the parties thereto. The joint stock company itself may not be a party to the shareholders' agreement. The Revisions do not define expressly whether shareholders' agreements are permitted if not all shareholders participate, but certain provisions of the Revisions may be interpreted to permit such a result. The parties to such an agreement may agree on the following:

Founded in 1890, Squire, Sanders & Dempsey L.L.P. has lawyers in 32 offices and 15 countries around the world. With one of the strongest integrated global platforms and our longstanding one-firm philosophy, Squire Sanders provides seamless legal counsel worldwide.

### Contacts:

David M. Wack
+7.495.258.5280

Christopher A. Rose
+7.495.258.5250

Ivan A. Trifonov
+7.495.258.5250

Patrick J. Brooks
+7.495.258.5250

Squire Sanders publishes on a number of other topics. To see a list of options and to sign up for a mailing, visit our subscription page.

- To vote a certain way at the general shareholders meeting;
- To agree with other shareholders to vote in a certain way (e.g., pooling votes to appoint a favored director nominee);
- To acquire or dispose of their shares at a predetermined price and/or under certain circumstances, thus permitting put and call options (although it remains unclear if tag-along and drag-along rights would be upheld on the basis of the Revisions);
- To refrain from disposing of the shares until the occurrence of certain circumstances (permitting temporal and circumstantial lock-up rights); and
- To act in an agreed-upon manner in relation to the management of the company, its operations, reorganization and liquidation.

The Revisions also provide for new regulations in relation to deadlock situations in which the board of directors fails to appoint a CEO during two consecutive meetings or within two months after the previous CEO's dismissal.

As a matter of form, shareholders' agreements should be executed as one document signed by all the parties thereto, rather than as counterparts.

Although there is no requirement to disclose the terms of a shareholders' agreement, the Federal Financial Markets Service and the company should be notified of the execution of a shareholders' agreement if (i) a share prospectus was registered with the Federal Financial Markets Service (e.g., if the company's shares are publicly traded) and (ii) the shareholders' agreement provides the parties and their affiliates the right to exercise shareholder votes exceeding any of the following thresholds: 5, 10, 15, 20, 25, 30, 50 or 75 percent. If a notification is required, the parties to the shareholders' agreement must submit such notification within five days after acquisition of the respective right (the effective date of the shareholders' agreement). The notification should include the name of the company, the name of the parties to the shareholders' agreement, the execution date and effective date of the agreement, the date of amendment to the agreement and effective date of such amendments (if applicable), the term of the agreement, the number of shares owned by the parties to the agreement on its date of execution, and the number of shares the notifying party can control at any general meeting of the company. Failure to notify the company of the existence of such a shareholders' agreement may give rise to future challenges by

interested parties of decisions taken in accordance with the agreement.

Lastly, the Revisions provide that no management decisions may be challenged due to violation of the provisions of the shareholders' agreement. This indicates that if board approval for a certain action required by the shareholders' agreement is not obtained, a shareholder will not be able to reverse the transaction based on the shareholders' agreement alone. Thus, it will be critical to incorporate relevant governance provisions into the company's charter.

**Limitations of the Revisions**

While the Revisions are a positive step forward, they do not go far enough in certain key respects, go too far in others and raise many questions that will only be sorted out with time, litigation and further legislative clarifications.

For example, the Revisions specify that a shareholders' agreement may provide for payment of compensatory damages and penalties and punitive damages (either in the set monetary amount or calculated based on a formula) if a party violates the agreement. It remains unclear how the concept of punitive damages can be squared with contract law and how it will be applied. Moreover, many violations cannot be compensated for monetarily, and how such compensation will be determined remains to be seen.

Moreover, the standard for challenging actions that violate a shareholders' agreement is muddied by the provision that any contract executed by a party to the shareholders' agreement in violation of its provisions may be challenged in court only if the other party to the agreement knew or should have been aware of the restrictions set by the agreement.

Further, the drafting of the deadlock provision may lead to narrow interpretations of the permissible scope of deadlock provisions and limit this as an effective tool despite the broad approval of puts and calls.

Finally and most fundamentally, it still remains unclear whether the courts will hold that the Revisions themselves violate various fundamental norms of Russian law, such as the prohibition on waiver of rights.

**Conclusion**

Despite the limitations, the Revisions provide new tools to empower shareholders to strengthen their rights and protections under Russian law, which is a positive step forward. Indeed, the ability to regulate shareholder relations in a more direct manner may present certain advantages to more commonly used investment structures that make use of offshore holding companies. However, until the Revisions have been

tested in the courts, it would be prudent to continue with offshore structures together with the new tools provided by the Revisions to provide maximum rights and protection.

The Moscow office of Squire Sanders has considerable experience in advising on shareholders' agreements and would be pleased to assist in reassessing your arrangements. For more detailed consultation on shareholders' agreements, contact your principal Squire Sanders lawyer or one of the individuals listed in this alert.

---