

New Competition Law Focuses Attention on 'Group of Persons'



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It may be too early to judge whether Russia's new competition law, which came into force less than five months ago, will live up to its promise to modernize and streamline the antimonopoly review of mergers, acquisitions, and similar equity transactions. But without doubt, the new law (Federal Law No. 135-FZ "On the Protection of Competition") has in some circumstances eliminated altogether the need to obtain prior regulatory clearance of such transactions, and has at least lowered the hurdles to clearance in others. The law also has introduced a significant degree of ambiguity by elevating the importance of the "group of persons" (*gruppа lits*) of each party to an equity transaction, as it fails to clarify exactly which persons belong to such a group.

THE REVISED CONSENT AND DISCLOSURE REGIME

The new law does not fundamentally alter the structure of the old law; companies entering into a substantial equity transaction are still required to obtain the prior consent of the Federal Anti-Monopoly Service, or FAS, or to notify it of the transaction after the fact. However, previously, where regulatory clearance was required both for any initial equity transaction exceeding a 20 percent stake and for any subsequent acquisition, the new law requires clearance only upon obtaining a blocking share (25 percent or 33 percent depending on corporate form), a controlling share (50 percent), and a supermajority share (66 percent or 75 percent).

Assuming no party has been officially identified as a potential monopolist, FAS consent to an equity transaction is required if the total assets of the parties exceed 3 billion rubles (or total revenue exceeds 6 billion rubles), and post-transaction notification is required if total assets

exceed 200 million rubles. Importantly, asset or revenue valuation is determined by reference to also the purchaser's group of persons and, unlike the prior law, the seller's group of persons as well.

The new law also provides that equity transactions within a single group of persons that would otherwise require FAS consent now require only subsequent notification, provided that the group of persons has been disclosed to the FAS and has posted on its web site at least one month prior to the transaction (and without any subsequent changes to the group). Thus, proper identification of a group of persons is necessary both to determine whether consent must be obtained in the first place, and, in the event of an intra-group transaction such as a restructuring or reorganization, whether the consent requirement can be avoided by prior disclosure of the group.

DETERMINING THE 'GROUP OF PERSONS'

Article 9.1 of the new competition law sets forth 14 short paragraphs identifying members of a group of persons, who may be thought of as falling into four categories. The first 13 set forth three categories of members of a group of persons of a given company:

- any person or entity who exercises control over the company, whether by holding a majority of voting equity, nominating or serving as general director, nominating a majority of the board of directors or other executive body, or otherwise having the ability to give binding instructions;
- entities related to such company by sharing any of the foregoing traits, by having more than half their boards of directors in common, or by being members of the same "financial-industrial group";

- spouses, parents, children and siblings.

These three categories differ from the previous law in only two important respects: the concept of majority control under the prior law explicitly provided for indirect majority control while the new law does not, and the category of close relatives no longer requires them to be connected to a natural person serving in an executive capacity or having control authority.

The fourth category, set forth in paragraph 14, represents the most significant change, introducing for the first time the following to the definition of a group of persons: "Persons, each of whom is, based on any of the grounds set forth in [paragraphs] 1-13 above, a part of a group with one and the same person, as well as other persons, who are a part of a group with each of such persons based on any of the grounds set forth in [paragraphs] 1-13 above."

This sentence, which may set a new low for clarity of legislative drafting, is no more comprehensible in the original Russian. Consequently, a debate has raged as to how many steps or "generations" away from the target company one must go in defining a group of persons.

Some companies have preferred to take a conservative approach, noting that paragraph 14 replaces the standard under the prior law by which even indirect control explicitly justified inclusion in a group of persons. In keeping with this view, these companies have interpreted paragraph 14 to apply repeatedly, so that after first identifying the core group of persons according to the criteria in paragraphs 1 to 13, one would then not only apply paragraph 14 to reach any person related on any of the enumerated grounds to any of the group (such as grandparent and granddaughter

companies), but also do so again and again (thus reaching third- and fourth-generation parents or subsidiaries, for example).

Other companies choose to read paragraph 14 more restrictively and apply it only once (and thus would not reach beyond the grandparent and granddaughter companies in the above example). Adherents of this approach note that if paragraph 14 were construed to cycle endlessly, one would reach not only the spouse of the general director, but the spouse's sibling, and the spouse's sibling's child, ad nauseum, to ultimately ludicrous effect. In their view, when it comes to making disclosures to the government, less is more, and what the law was intended to say is less important than what it actually says or could plausibly be said to mean.

A review of the nearly 20 group structures revealed to date on the FAS' web site (at <http://www.fas.gov.ru/merger/groups/index.shtml>) demonstrates that both approaches have gained currency but neither has prevailed. The FAS itself appears to give the law an expansive reading, as the model form of disclosure posted on its web site shows a group of persons five generations removed from the company at the center, but its formal written interpretation of paragraph 14 is not expected until later this year.

In any event, a regulatory agency cannot demand more than what the law requires. At least until the FAS propounds a formal interpretation, and potentially until one interpretation prevails in court or the law is redrafted, a company's determination of its group of persons may well depend on the role it is playing in a given transaction, its own institutional and cultural prejudices, and its relative assessments of insufficient and excessive disclosure.

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