



ICLG

The International Comparative Legal Guide to:

Project Finance 2015

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Kazakhstan

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1 Overview

1.1 What are the main trends/significant developments in the project finance market in Kazakhstan?

Project finance in the strict sense of the term (i.e. where the financing structure is based on the performance of the project itself) has not yet been developed or tested so far in Kazakhstan. So-called ‘project finance’ transactions that took place in Kazakhstan, in fact, were either conventional bank loans (mostly from international financial institutions such as the European Bank for Reconstruction and Development and International Finance Corporation) that have somehow benefited from government guarantees, security packages, direct budgetary investments or net private investments.

It is expected, however, that proper project finance deals will finally take off in Kazakhstan in the near future, firstly because proper legislation on project finance and PPPs has been put in place (substantial amendments to the existing legislation were passed in 2014) and, secondly, after decades of neglect, the Government of Kazakhstan has finally declared its readiness to improve the investment climate and to attract private investments through PPPs (including into the housing and utilities sector) and decided to invest at least part of the wealth from commodity exports in long-postponed infrastructure projects (e.g. the Government of Kazakhstan is planning to launch major transport and infrastructure projects stipulated in the address of the President of Kazakhstan to the people of Kazakhstan dated 11 November 2014 (*‘Nurly Zhol’* ('Path to the Future')), as well as the ‘State Program of Industrial-Innovative Development of the Republic of Kazakhstan for 2015–2019’ and the ‘Program for Development of the Public-Private Partnership in the Republic of Kazakhstan for 2011–2015’).

1.2 What are the most significant project financings that have taken place in Kazakhstan in recent years?

Recently China’s state-owned China Development Bank (CDB) provided a \$1.8 billion syndicated secured loan facility to Beineu Shymkent Gas Pipeline LLP (controlled 50:50 by KazTransGas and CNPC) to finance a gas pipeline project in Kazakhstan, as well as two secured loans totalling \$12.2 billion to Asia Gas Pipeline LLP to finance the Central Asia-China Gas Pipeline project.

It is also expected that long-awaited Balkhash Power Plant (debut \$4 billion Independent Power Producer project in Kazakhstan) and the Almaty Ring Road (BAKAD) (the first PPP structured project under the new regulatory framework that took legal effect in 2014) projects finally would be implemented in the near future.

2 Security

2.1 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Kazakh law provides for several methods of securing obligation. Obligations could be secured by penalty, pledge, surety, guarantee, deposit, withholding the debtor's property, guarantee deposit, and other methods stipulated by legislation or agreement. Invalidity of a security agreement does not invalidate the main obligation. In contrast, invalidity of the main obligation would invalidate the obligation under a security agreement, for security is an accessory obligation under Kazakh law.

Under Kazakh law a pledge is a type of security under which the creditor (the pledgee) has the right, in the event of failure by the debtor to perform the obligation secured by the pledge, to receive satisfaction from the value of the pledged property, in a priority procedure before other creditors of the person to whom that property belongs (the pledgor), subject to exceptions stipulated by the Civil Code.

Pledges can be of two types: (1) mortgages; and (2) possessory charges. A mortgage is a type of pledge when the collateral remains in the possession of the pledgor or a third party. A possessory charge is a type of pledge when the collateral is transferred to the possession of the pledgee.

An agreement governing creation of an asset security interest must contain a subject of the collateral, its value, nature, scope and maturity period of the obligation secured by such collateral. The agreement must also clearly identify a party which retains the collateral. The value of the collateral shall be indicated in national currency.

In general, there are no restrictions as to the type of debts that can be secured. Also, it is possible to secure debts not yet existing (future or conditional), debts expressed in foreign currency, and even fluctuating debt.

With limited exceptions, Kazakh law does not limit the types of property that can be pledged. Acquired assets may be pledged, as well as goods in turnover (i.e. equivalent to the floating charge), such as inventories, raw material, semi-finished goods, and finished products.

Possible forms of security for the financing of an infrastructure project in Kazakhstan, generally, include the following: (i) mortgage over real property of the project company; (ii) pledge agreements

over equipment and other movable assets; (iii) assignment of rights under insurances, project contracts and project bonds; (iv) pledges of bank accounts and cash; (v) pledge of shares in the project company; and (vi) limited guarantees by the sponsors.

Such security arrangements generally require a separate agreement in writing in relation to each type of asset to be enforceable under Kazakh law.

2.2 Can security be taken over real property (land), plant, machinery and equipment (e.g. pipeline, whether underground or overground)? Briefly, what is the procedure?

The pledgor can pledge its plant and machinery in favour of creditors, including foreign creditors. If the relevant plant and machinery is deemed to be immovable property (i.e., inseparable from the land or building at which it is installed), pledge must be registered with the Ministry of Justice to be valid. If plant and machinery is not deemed to be immovable property, security interest (pledge) will be created by means of the pledge agreement. However, to ensure priority of creditors' security interest, the pledge should be registered with the registration authorities of the Ministry of Justice as discussed above. Land plots owned or leased for a long-term period may be mortgaged in favour of creditors. As mentioned above, title to a land plot is inseparable from the title to immovable property. Therefore, a mortgage of a building means that the underlying land plot will also become the subject of the same mortgage. A mortgage must be registered with the Ministry of Justice via making application to a Centre of Service for the Population.

As a matter of Kazakh law, construction in progress constitutes movable property (not real estate) until construction is finished, commissioned by the state and registered by the registration authorities of the Ministry of Justice as a unit of immovable property. Thus, construction in progress can be pledged as movable property, but not as immovable property. Pledge over construction in progress does not automatically convert into pledge over immovable property after completion and registration of construction. Accordingly, after the plant is commissioned, it will be necessary for the pledgor to execute a new pledge agreement in respect of the plant, replacing the earlier agreement in respect of construction in progress.

Please also note that, taking into consideration that some time is required for registration of the immovable property after its construction, there is a time period between the date of completion of construction and the date when the immovable property is mortgaged. During this period, the loan agreement will not be properly secured by an immovable property mortgage (other than by the land plot) because at that time the construction in progress will no longer exist and the immovable property will not yet be registered. This risk is mitigated to a certain extent by the fact that the creditor will in any case keep hold of a mortgage over the land, and according to Kazakhstani Land Code the title to a land plot is inseparable from the title to immovable property located on such land plot. However, even so, it may be argued that until a new mortgage agreement is entered into, the creditor has security only in respect of the land plot. This circumstance has been highly criticised in Kazakhstan, however, it remains the position and is a matter of certain risk to a creditor. We normally recommend that a creditor adds an additional clause to a loan agreement obliging the pledgor to promptly grant a new mortgage in relation to the immovable property (on substantially the same terms as the terms of the mortgage agreement) once it is accepted and registered.

2.3 Can security be taken over receivables where the chargor is free to collect the receivables in the absence of a default and the debtors are not notified of the security? Briefly, what is the procedure?

It is possible for a company to pledge its monetary claims under a contract (e.g. insurance agreement or off take agreements) provided that such claims are assignable. Where rights to receivables are pledged, the enforcement will be carried out by way of assignment of the relevant rights to the pledgee (i.e. without the public auction as it is with most other types of collateral). The debtor must be notified for the pledge of receivables to be enforceable and the chargor cannot collect the receivables in the absence of a default.

2.4 Can security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Under Kazakh law, strictly speaking, the pledge of a bank account is not possible. However, the law allows pledging money on a bank account of a Kazakh pledgor. It is important to note that the pledge of money on a bank account is recommended to be executed among three parties: the pledgee; the pledgor; and the local account bank, which maintains the pledgor's accounts. Such structure allows the parties to incorporate into the pledge agreement specific wording on direct debiting, allowing the pledgee to debit the pledgor's accounts without its consent and making the local account bank acknowledge such pledgee's right upon the serving of a notice of default. On a contractual basis the parties may agree that a certain amount shall not to be withdrawn by the pledgor. There are certain risks related to the money pledged in a bank account. Under Kazakh law, if an entity has debts on taxes or customs payments, tax and customs authorities may suspend transfer of funds from such bank accounts. Moreover, tax and customs authorities may withdraw money from such entity's bank accounts without such entity's consent, prior to any other creditors (except for cases of liquidation and bankruptcy when debts are repaid in accordance with a legislatively established priority).

2.5 Can security be taken over shares in companies incorporated in Kazakhstan? Are the shares in certificated form? Briefly, what is the procedure?

Holders of shares of a Kazakh joint-stock company (hereinafter the 'JSC') and participatory interests of a Kazakh limited liability partnership (hereinafter the 'LLP') have the right to pledge all or part of such shares or participatory interests respectively in favour of creditors (including foreign creditors). The major shortcoming of such a pledge is that the creditors would not be entitled to take possession of the shares but must instead seek to sell the shares through a public auction, as discussed below.

A pledge over shares of the JSC must be registered with the Unified Registrar, which will make an entry regarding the pledge in the system of registers of security holders. Such pledge is only valid upon its registration.

Another form of commercial legal entity under Kazakh law is an LLP which has participatory interests as opposed to shares. A pledge over participatory interests of the LLP, generally, can be registered with the relevant department of the Ministry of Justice, unless a Unified Registrar is provided under the corporate documents of the LLP and, in this case, pledge over participatory interests must be registered with the Unified Registrar.

There are no restrictions on the creditors' right to enforce pledge over shares, subject to their compliance with local procedural rules for such enforcement.

It should be noted that a purchaser of more than 25 per cent of shares in a Kazakh company may be required to obtain approval of such purchase from the Competition Agency. If the purchase is subject to antimonopoly approval (this will depend on the combined asset value or annual turnover of the purchaser and the Kazakh entity), then the purchaser will be required to apply for approval within 30 days after the public auction at which it acquired the shares. If the pledge provides for a transfer of voting rights in the event of default over more than 25 per cent of shares, such transfer may be a subject of separate approval of the Competition Agency.

2.6 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets (in particular, shares, real estate, receivables and chattels)?

Registration of a pledge over most types of movable assets is not required for the pledge to be effective. In contrast, security over immovable assets and certain registered movable assets (e.g. vehicles, aircraft and registered securities) must be registered in order to be effective. A pledge of other movable property is subject to mandatory registration only if the further pledge of such movable property is prohibited by the pledge agreement.

While it is not obligatory to register pledges in relation to most movable assets, such registration grants the creditor priority right in the collateral. If two or more creditors obtain security interests in the same collateral (whether movable or immovable), law gives priority to security interests in the order in which they are registered and registered pledges generally have priority over unregistered ones regardless of the time of creation. Unregistered pledges generally have priority in the order in which they are created. Generally, it is possible to check registered pledges – for this purpose, the extract from the relevant register shall be requested.

Accordingly, it will be necessary for the lenders to procure that the pledge/mortgage is registered with the relevant registration authorities to ensure that they have first priority security interest in the collateral. No further steps for perfection of security interest will be necessary. Any subsequent registered or unregistered pledge (or any prior unregistered pledge) by any third party pledgee over the same collateral will rank lower than the lenders' perfected security interest in the collateral. Registration of a pledge does not need to be renewed (unless either secured obligation or composition of collateral is amended).

Registration authorities at the Ministry of Justice register pledge over most movable and all immovable assets. Depending on the type of pledged property, some authorities also register security (e.g. traffic police register pledges over vehicles, the Ministry of Agriculture registers pledges over tractors and certain other agricultural machinery, and the Unified Registrar registers pledges over registered securities).

In general, no governmental or regulatory consents are required for granting security (except for pledges over subsurface use rights, strategic objects and certain other specific classes of assets).

2.7 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Under the Kazakh law, registration of a movables pledge should take no more than two working days from the moment required documents are submitted to the registration authority. In relation to a pledge of immovable property, the registration authority has to register security within five working days.

Registration fees for the registration of pledges over movable and immovable property are payable by the pledgor who normally is the party responsible for the registration of the relevant pledge agreement.

The fee for registration of a pledge over shares is a percentage of the value of the shares being pledged, whereas registration of other types of the movable property pledge (including such movable property as equipment, goods, money in a bank account and participatory interests in a company) requires one so-called 'monthly calculation index' from physical persons (approx. \$10) and five monthly calculation indexes from legal entities (approx. \$50).

Registration fees on the immovable pledge property vary depending on the kind of the immovable property.

Application for registration of the immovable property pledge, generally, shall be submitted by both parties of the immovable property pledge agreement unless such agreement is notarised.

2.8 Are any regulatory or similar consents required with respect to the creation of security over real property (land), plant, machinery and equipment (e.g. pipeline, whether underground or overground), etc.?

No, as prior consent from the respective authorised state body is only required for a pledge over, among others: (i) subsurface use rights; and (ii) so-called 'strategic objects', being assets that are deemed to be strategic objects (such as oil and gas pipelines, national electricity grids, oil refineries, international air and sea ports, etc.) and equity interests in entities holding such assets or in the entities that directly or indirectly define or influence decisions of the entity holding such assets.

3 Security Trustee

3.1 Regardless of whether Kazakhstan recognises the concept of a "trust", will it recognise the role of a security trustee or agent and allow the security trustee or agent (rather than each lender acting separately) to enforce the security and to apply the proceeds from the security to the claims of all the lenders?

Kazakhstan does not recognise trusts and, accordingly, security must be granted to the actual creditor, i.e. the creditor which advances the loan. Accordingly, as a matter of Kazakhstan law, a security trustee (who is not the actual creditor) cannot hold security and act as a pledgee on behalf of the creditors. Thus, if loan participation is transferred, any pledge or mortgage for that loan

must be re-registered in the name of the new creditor. Accordingly, it is uncertain whether any security arrangement whereby a security trustee acts as a holder of security on behalf of the creditors would be enforceable in Kazakhstan.

3.2 If a security trust is not recognised in Kazakhstan, is an alternative mechanism available (such as a parallel debt or joint and several creditor status) to achieve the effect referred to above which would allow one party (either the security trustee or the facility agent) to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

Parallel debt structure seems to address the above issue and shall be enforceable under Kazakh law. It shall be noted, however, that it has not been tested in the Kazakh courts and there is a theoretical risk that parallel debt structure may be challenged as sham transaction for the purposes of Kazakh law.

4 Enforcement of Security

4.1 Are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction or the availability of court blocking procedures to other creditors/the company (or its trustee in bankruptcy/liquidator), or (b) (in respect of regulated assets) regulatory consents?

A secured creditor cannot simply take possession of the collateral (except for cash and receivables). The creditor must seek to sell the collateral through a public auction and recover the debt from the sale proceeds. The sale proceeds will be used first to cover expenses incurred in connection with the enforcement and sale (including any fines imposed on the debtor by a court marshal during the enforcement). After that the proceeds will be used to repay the debts. The remainder, if any, will be returned to the debtor. Enforcement may take up to six months from the moment of default to the sale of the pledged property. It may take longer if the pledgor contests the underlying default. The enforcement costs should be in a range of several thousand U.S. dollars (without taking into account the court fee). The law, however, provides that expenses incurred by the pledgee are recoverable from the sale proceeds, and the court fees are to be reimbursed by the pledgor.

A pledge agreement may be enforced either through a court-supervised judicial procedure or through an out-of-court procedure. The relevant pledge agreement must specify the mode of enforcement (i.e. through the courts or without court involvement).

If the lender enforces the pledge through a court-supervised procedure, it will be necessary for the lender to pay a court fee in the amount of 3 per cent of the value of the collateral. If the lender is successful in its court action seeking pledge enforcement, the court will order the customer to reimburse the lenders for the court fees paid by the lender in commencing the court action.

In case of enforcement through judicial action, the court marshal is obliged under the law to conduct the auction and sell the collateral within four months after he received the relevant court order. This term may be extended in certain circumstances.

4.2 Do restrictions apply to foreign investors or creditors in the event of foreclosure on the project and related companies?

Existing legislation of Kazakhstan provides for certain forms of restrictions on foreign ownership of certain assets (e.g. land for commercial agriculture and forest cultivation) and the volume of foreign investments in specific sectors of the economy (e.g. mass media, telecommunications, banking, insurance, etc.). Also, as discussed above, investment by a foreign or local investor into certain types of entities or assets requires governmental approval. The above restrictions also apply in the event of foreclosure on the relevant company.

5 Bankruptcy and Restructuring Proceedings

5.1 How does a bankruptcy proceeding in respect of the project company affect the ability of a project lender to enforce its rights as a secured party over the security?

Final liquidation of a Kazakh legal entity upon bankruptcy, generally, involves a disposal of the debtor's assets and distribution of the proceeds to creditors in the payment order established in the Law on Rehabilitation and Bankruptcy. A pledge would effectively be terminated in the event of bankruptcy of the pledgor. Creditors secured by a pledge become creditors of the 'second priority' (i.e. claims secured by the pledge are satisfied after claims for alimony payments and compensation for wrongful damage to one's health or life; and claims for payment under employment contracts, related social security and mandatory pension payments, and under copyright agreements) and unsecured creditors become creditors of the forth and/or fifth (last) priority and their claims are satisfied only after settlement of all other claims in a lengthy and not transparent liquidation process. Note that creditors having security other than a pledge would be considered unsecured creditors in bankruptcy proceedings.

5.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g. tax debts, employees' claims) with respect to the security?

The Kazakhstani legislation provides for a three-year hardening period when transactions of an insolvent company may be invalidated on certain grounds as specified in the Law on Rehabilitation and Bankruptcy (e.g. a transaction made within three years prior to initiation of bankruptcy involving the transfer of property free of charge, below market price or without sufficient grounds to the detriment of the creditors' interests).

5.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

So-called state enterprises and state institutions are excluded from bankruptcy proceedings. There is no insolvency procedure in the local law for these types of entities.

5.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of the project company in an enforcement?

No, there are not in case of bankruptcy proceedings. Otherwise out-of-court enforcement is available as stated in the answer to question 4.1.

5.5 Are there any processes other than formal insolvency proceedings that are available to a project company to achieve a restructuring of its debts and/or cramdown of dissenting creditors?

It is possible to apply for a rehabilitation procedure instead of bankruptcy. Rehabilitation is a special insolvency regime to rescue a debtor that a respective Kazakh court may impose (generally, for not more than five years) at the request of a debtor, subject to certain conditions (e.g. there should be a real possibility for recovery of the financial stability of a debtor).

5.6 Please briefly describe the liabilities of directors (if any) for continuing to trade whilst a company is in financial difficulties in Kazakhstan.

Officers of a company may be required to bear subsidiary liability before the creditors of the company for, among others, premediated bankruptcy of the company and failing to fulfil their statutory duties (e.g. officials of a company are required to file a petition for bankruptcy of the company within six months from the date the company learned or should have learned about its financial insolvency).

6 Foreign Investment and Ownership Restrictions

6.1 Are there any restrictions, controls, fees and/or taxes on foreign ownership of a project company?

Apart from certain foreign ownership restrictions discussed above, there are no specific restrictions relating to the permitted ownership of a project company. It is worth mentioning, however, that voting shares/participatory interests in companies which own or manage so-called ‘strategic objects’ for the Republic of Kazakhstan may not be pledged or alienated without the approval of the Government of Kazakhstan. In addition, the government enjoys a pre-emptive right over other participants or shareholders of such companies to purchase the voting shares/participatory interests.

In addition, the Government of Kazakhstan enjoys a pre-emptive right over other participants and third parties to purchase the shares/participatory interests of Kazakh subsurface user companies.

Also, it is worth mentioning that notification of the respective state agency is required for any acquisition by third parties of a stake in a company that is so-called ‘subject of a natural monopoly’ giving them more than 10 per cent of the votes on the shares of such a natural monopoly.

Finally, acquisition of a stake in a Kazakh company in certain cases may be considered as a so-called ‘direct investment’ that require registration with the National Bank of Kazakhstan.

No specific taxes are imposed by Kazakhstan legislation on foreign ownership of a project company.

6.2 Are there any bilateral investment treaties (or other international treaties) that would provide protection from such restrictions?

Kazakhstan has concluded bilateral treaties on the encouragement and mutual protection of investments with 42 countries. Kazakhstan is also a party to a number of multilateral treaties concerning foreign investments (for example, the Energy Charter). Investment treaties provide for a number of guarantees to nationals of member countries, including most-favoured-nation treatment, protection against discrimination, requisition and nationalisation and the right to resolution of investment disputes by international arbitration in the absence of an arbitration agreement.

6.3 What laws exist regarding the nationalisation or expropriation of project companies and assets? Are any forms of investment specially protected?

Under the current investment legislation, seizure of an investor’s property is effected either through nationalisation or requisitioning, both possible only in ‘exceptional cases’ and subject to ‘state needs’. Should the investment be nationalised, the investor is entitled to full indemnification for damages caused by nationalisation, while, in the case of requisitioning, only payment of the market value of the requisitioned property is provided.

7 Government Approvals/Restrictions

7.1 What are the relevant government agencies or departments with authority over projects in the typical project sectors?

The Ministry of Energy is responsible, among others, for the oil and gas sector, petrochemical industry, transportation of hydrocarbons, state regulation of the production of oil products, gas and gas supply, trunk pipeline, electric-power industry, coal, nuclear energy, environment, natural resources, protection, control and supervision for management of natural resources, municipal solid waste management, renewable energy, and control over the national development policy ‘green economy’.

The Ministry of Investment and Development is responsible, among others, for the mining sector, engineering, chemical, pharmaceutical and medical industry, light industry, woodworking and furniture industry, building industry and manufacture of building materials, and the state control of resource exploitation of the underground water and therapeutic mud, solid minerals, except coal, and uranium.

Local authorities (*Akimats*) are responsible for granting land use rights, for control and supervision over the use and protection of land, water and the environment, and for monitoring compliance with local content obligations.

7.2 Must any of the financing or project documents be registered or filed with any government authority or otherwise comply with legal formalities to be valid or enforceable?

As discussed above, there are different government bodies’ approvals/licences and fees that may be applicable to an infrastructure project in Kazakhstan depending, *inter alia*, on the economy sector.

Kazakh law does not impose any material restrictions on a project company borrowing funds from foreign lenders and in foreign

currency. Residents of Kazakhstan may use any currency in their transactions with non-residents. However, in borrowing from foreign lenders, the project company will be required to comply with certain registration requirements. In particular, the Currency Control Law requires that any loan from a non-resident lender to a Kazakh borrower which is both (i) in excess of \$500,000, and (ii) for a term exceeding 180 days, be registered with the National Bank of Kazakhstan.

7.3 Does ownership of land, natural resources or a pipeline, or undertaking the business of ownership or operation of such assets, require a licence (and if so, can such a licence be held by a foreign entity)?

There are various government approvals required for companies operating in certain sectors of the Kazakh economy. For instance, a company may be required to obtain a licence from the relevant state authority in order to be able to carry out a particular type of activity (e.g. exploitation of the main gas pipeline). Such licences, generally, cannot be held by a foreign entity. Other approvals may be required, including, *inter alia*, approvals for construction, etc.

7.4 Are there any royalties, restrictions, fees and/or taxes payable on the extraction or export of natural resources?

Severance tax is payable in respect of extraction of mineral resources in Kazakhstan. The basis for this charge is the volume of extracted mineral resources. The rule for determining of the basis calculation of the severance tax for each type of the mineral resources is specifically stipulated separately (see Chapter 45 of the Tax Code).

There are also the following main taxes that shall apply to subsurface use operations: (i) signature bonus (this bonus is a fixed payment for the right to conduct subsurface use operations in the contract area); and (ii) commercial discovery bonus (this bonus is payable for each commercial discovery and is based on the actual volume of discovered mineral deposits approved by the authorised state agency).

As for general tax regulation, in accordance with the Tax Code these are principal taxes applicable to a Kazakh legal entity:

- The corporate tax rate is 20 per cent.
- The current rate for VAT is 12 per cent on taxable turnover and taxable import.
- The current rate for individual income tax is 10 per cent, withheld by employers from payments to employees.
- The current rate of social tax is 11 per cent, withheld by employers from payments to employees.
- The general rate of property tax is 1.5 per cent on the average book value of the property classified, immovable property, or investments in immovable property.
- Land tax rates depend on the land category.
- Tax rates for vehicles depend on the type of the vehicle and its engine volume.
- Export rent tax (this tax applies to exported crude oil, gas condensate and coal).

7.5 Are there any restrictions, controls, fees and/or taxes on foreign currency exchange?

Generally, foreign currency exchange transactions are carried out without restrictions. Certain types of currency transactions are

subject to either a registration regime (e.g. a loan from foreign lender in excess of \$500,000 and with a tenor of more than 180 days needs to be registered with the National Bank) or a notification regime.

No specific tax is imposed by Kazakhstan legislation on foreign currency exchange operations.

7.6 Are there any restrictions, controls, fees and/or taxes on the remittance and repatriation of investment returns or loan payments to parties in other jurisdictions?

Generally, any revenue received by a Kazakh company from the export of goods or services must be deposited in its Kazakh bank account within the relevant period of time of repatriation. A Kazakh company must also repatriate to its Kazakh bank account foreign and national currency transferred by it to a non-resident under a contract for the import of goods, works or services if the non-resident fails to perform its obligations under the contract.

Repayments of principal amount of a loan by a Kazakh borrower to a non-resident are not taxable in Kazakhstan. Payments relating to interest on a loan by a Kazakh-resident to a non-resident are normally subject to withholding tax in Kazakhstan at a general rate of 15 per cent, unless reduced or exempt by an applicable treaty on avoidance of double taxation.

7.7 Can project companies establish and maintain onshore foreign currency accounts and/or offshore accounts in other jurisdictions?

Yes, subject to subsequent notification of the National Bank.

7.8 Is there any restriction (under corporate law, exchange control, other law or binding governmental practice or binding contract) on the payment of dividends from a project company to its parent company where the parent is incorporated in Kazakhstan or abroad?

No restrictions are applicable and no authorisation is generally required for repatriation of funds from the Republic of Kazakhstan. Profit repatriation is normally effected through dividend mechanics. A resident distributing dividends has to withhold tax at source on payment of dividends, at a rate of 15 per cent, unless the rate is reduced by an applicable double-taxation treaty.

7.9 Are there any material environmental, health and safety laws or regulations that would impact upon a project financing and which governmental authorities administer those laws or regulations?

Environmental matters are primarily regulated by the Environmental Code and the Law on Specially Protected Nature Areas. These laws are administered by the Ministry of Energy and the Ministry of Agriculture.

Health-related matters are primarily regulated by the Code on People's Health and the Healthcare System and the Sanitary Regulations. These laws and regulations are administered by the Ministry of Health and Social Development.

Safety-related matters are primarily regulated by the Law on Civil Defense and the Fire Safety Regulations. These laws and regulations are administered by the Ministry of Internal Affairs.

7.10 Is there any specific legal/statutory framework for procurement by project companies?

Only certain state-owned companies and companies directly or indirectly owned by the Sovereign Wealth Fund «*Samruk-Kazyna*» are subject to the stringent requirements of the Law ‘On State Procurement’ and the procurement rules of the *Samruk-Kazyna*, respectively.

8 Foreign Insurance

8.1 Are there any restrictions, controls, fees and/or taxes on insurance policies over project assets provided or guaranteed by foreign insurance companies?

Any property interests located on the territory of Kazakhstan and belonging to a legal entity or a natural person resident of Kazakhstan may be insured by a Kazakh insurer only. Subject to prudential norms, local insurance companies may reinsure their risks with foreign insurance companies.

Mandatory insurance with local insurance companies is required for certain types of assets and risks (e.g. ecological risks). In respect of the mandatory types of insurance, the loss payee is determined by law and cannot be changed on contractual basis.

Fees payable for insurance policies are commonly treated as a taxable income for the tax purposes in Kazakhstan.

8.2 Are insurance policies over project assets payable to foreign (secured) creditors?

A policy holder or a beneficiary under an insurance policy must have insurable interest in the insured property. Accordingly, where the lender has insurable interest in the insured property, the lender may be named as the beneficiary in the relevant insurance policy.

Kazakh legislation provides a pledgee with a priority right to receive insurance proceeds under an insurance contract relating to the pledged property. The pledgor will be entitled to the insurance proceeds only if the pledgee waives his priority rights to such proceeds. However, where the lender does not have such an interest, he may not be named as the beneficiary.

Kazakh legislation provides a pledgee with a priority right to receive insurance proceeds under an insurance contract relating to the pledged property. The pledgor will be entitled to the insurance proceeds only if the pledgee waives his priority rights to such proceeds. Thus, where the insured property is pledged in favour of the lenders, the lenders will have the priority right to the insurance proceeds in respect of such property.

9 Foreign Employee Restrictions

9.1 Are there any restrictions on foreign workers, technicians, engineers or executives being employed by a project company?

When hiring foreign citizens or stateless persons, a Kazakh employer (i.e. project company) has to obtain a work permit for each foreign specialist, including the top management of Kazakhstan incorporated companies.

There are a number of exemptions from the general requirement to obtain a work permit. Foreigners holding a residence permit,

foreign citizens and stateless persons holding the position of head of a branch or a representative office of a foreign company or those travelling to Kazakhstan for business purposes for an aggregate period not exceeding 120 calendar days per year do not need a work permit.

10 Equipment Import Restrictions

10.1 Are there any restrictions, controls, fees and/or taxes on importing project equipment or equipment used by construction contractors?

The importation of project equipment is generally subject to the requirements of the customs legislation (e.g. payment of applicable customs duties and taxes, etc.). However, certain benefits are established by the legislation with respect to imports of specific equipment and machinery, depending on specifics of imported goods.

The project company may need to obtain a number of licences depending on the kinds of activity the project company will be involved in, including for import of certain goods (e.g. explosives) according to the list approved by the Government of Kazakhstan.

It also shall be noted that in order to protect domestic producers of goods and national economy in whole, the Government of Kazakhstan may enact export or import bans, import or export quotas and safeguard measures against imports. Import quotas are enforced by means of licensing.

10.2 If so, what import duties are payable and are exceptions available?

Customs duties may vary depending on the applicable customs procedure(s) and specifics of the imported goods in question.

11 Force Majeure

11.1 Are force majeure exclusions available and enforceable?

Kazakh law provides for such released matter as circumstances of insuperable force, i.e. circumstances extraordinary and unpreventable under existing conditions (acts of God, military operations, etc.).

12 Corrupt Practices

12.1 Are there any rules prohibiting corrupt business practices and bribery (particularly any rules targeting the projects sector)? What are the applicable civil or criminal penalties?

There are general rules prohibiting corrupt business practices and bribery established by the Law ‘On Fighting with Corruption’ dated 2 July 1998 whereunder ‘corruption’ is referred to in relation to persons carrying out state functions. Corrupt practice in the public sector may be subject to a fine of up to 80-fold amount of the bribe, deprivation of freedom for up to 15 years with confiscation of property, life term deprivation of right to hold specific positions or carry out certain activities. Corrupt practice in the private sector may be subject to a fine of up to 4,000 monthly calculated indices (KZT 7,928,000; approx. \$43,000) or correctional labour of

13 Applicable Law

13.1 What law typically governs project agreements?

Generally, parties may choose foreign law as the governing law of the agreement if at least one party or its object is foreign. There are limited exceptions to this rule, e.g. contracts relating to shares in Kazakh entities or to real estate located in Kazakhstan must be governed by Kazakh law. However, such exceptions do not apply to a typical loan agreement, which may be governed by a foreign law. The same general rule applies to project agreements: contracts between local parties must be governed by Kazakh law, unless there is another foreign element involved.

13.2 What law typically governs financing agreements?

In most cases, loan agreements between foreign lenders and Kazakh borrowers are governed by English law, or, in some cases, by New York law or the laws of the People's Republic of China or Japan.

13.3 What matters are typically governed by domestic law?

It is strongly recommended that security agreements are governed by Kazakh law to be enforceable.

14 Jurisdiction and Waiver of Immunity

14.1 Is a party's submission to a foreign jurisdiction and waiver of immunity legally binding and enforceable?

The concept of waiver of rights is, generally, not recognised by Kazakhstani legislation, however, if a party enters, for instance, into an agreement governed by English law that provides for waiver immunity, such a contractual arrangement shall be legal and enforceable from the Kazakhstani legislation perspective.

15 International Arbitration

15.1 Are contractual provisions requiring submission of disputes to international arbitration and arbitral awards recognised by local courts?

Yes, they are. Kazakhstan is a member of the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards and, if a foreign arbitral award is obtained in another member country, such award should generally be enforced by Kazakhstani courts without a review of the merits, subject to compliance with qualifications set out in the Convention and certain procedural rules of Kazakhstani law. However, in practice the enforcement of foreign arbitral awards in Kazakhstan can be difficult.

15.2 Is Kazakhstan a contracting state to the New York Convention or other prominent dispute resolution conventions?

Yes, Kazakhstan is a contracting state to the New York Convention.

15.3 Are any types of disputes not arbitrable under local law?

Disputes concerning interests of minors, persons recognised incapable or partially capable; disputes arising out of personal non-property relations related to the life and health, private life privacy, personal and family privacy, right of name are not arbitrable. In addition, some cases are subject to exclusive Kazakh court's jurisdiction (including disputes concerning rights over immovables in Kazakhstan, carriers and some others).

15.4 Are any types of disputes subject to mandatory domestic arbitration proceedings?

No, they are not.

16 Change of Law / Political Risk

16.1 Has there been any call for political risk protections such as direct agreements with central government or political risk guarantees?

Yes, and a concept of 'direct agreement' has recently been introduced into legislation in Kazakhstan.

17 Tax

17.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Generally, interest (remuneration) payable to domestic or foreign lender by a resident borrower on a loan is subject to withholding tax at source and value added tax.

Interest (remuneration) payable to specific types of financial organisations established in Kazakhstan, such as special finance companies under Kazakhstani project finance legislation, banks, organisations performing certain kinds of banking operations, credit partnerships and microfinance organisations, etc., is subject to corporate income tax on a self-assessment basis.

Interest payments to a foreign lender and specific types of domestic financial organisations having a qualified lender status (such as banks, including Islamic banks, credit partnerships, etc.) are exempt from value added tax. In relation to the proceeds of a claim under a guarantee or the proceeds of enforcing security, we note that Kazakhstan tax legislation is not clear how to treat such proceeds for tax purposes. The commonly practised approach in Kazakhstan is to view any proceeds under a guaranty or other security in the same manner as the underlying obligation. Under such approach, if a borrower defaults on a payment of interest or principal, proceeds to be receivable by a lender under or in connection with the security to the extent relating to principal, would unlikely be subject to any tax in Kazakhstan.

However, proceeds relating to interest would be characterised as income subject to all applicable taxes as discussed above.

17.2 What tax incentives or other incentives are provided preferentially to foreign investors or creditors? What taxes apply to foreign investments, loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

The Law on Investments, that applies to both local and foreign investments, creates a system of benefits and preferences supporting direct investments in priority types of activity, the full list of which is approved by the government (examples include certain types of production of equipment, agriculture and construction). Local companies engaged in a designated priority activity as provided by the Law on Investments may be eligible for benefits and preferential treatment and may receive, depending on the circumstances:

- an exemption from customs duties on imported equipment required for investment projects; and/or
- state grants in-kind (land plots, buildings, equipment, machinery, etc.).

So-called investment priority projects in addition may benefit from:

- investment subsidies; and
- investment tax preferences.

Additional support may be provided for specific sectors of economy or locations (e.g. there are certain privileges for projects in the agriculture sector, special economic zones, etc.).

18 Other Matters

18.1 Are there any other material considerations which should be taken into account by either equity investors or lenders when participating in project financings in Kazakhstan?

The concept of a ‘project finance’ was introduced in 2012 into the legislation of Kazakhstan (see the Law ‘On Project Finance and Securitisation’) so we can say that, generally speaking, there is now a solid basis for the structuring of transactions on the principles of project finance in Kazakhstan (i.e. it seems the law cannot be used for cross-border project finance deals). Nevertheless, although gaps will only truly become apparent in practice, we can already note the following significant weakness of the law: Article 6-7 of the Law ‘On Project Finance and Securitisation’ says that the *‘title to the property created under the base agreement by the state order belongs to the state’*. This limits the ability to structure projects involving the state only as BTO (‘Build – Transfer – Operate’) projects, if the project would be implemented under the Law ‘On Project Finance and Securitisation’ framework.

Concept of a PPP is provided in the Law on Concession that provides the possibility of one or more of the following forms of government support for the proposed PPP project:

- 1) government guarantees on infrastructure bonds within concession agreements;
- 2) government guarantees on loans raised to finance concession projects;
- 3) transfer of exclusive rights to a government-owned IP object to a concessionaire;
- 4) in-kind grants in accordance with the Kazakhstani law;
- 5) co-financing of concession projects; and
- 6) guarantees of government consumption of a certain volume

of goods (works, services), when a principal consumer of goods produced by a concessionaire is the state.

A preliminary analysis of the Concession Law, however, has demonstrated that certain problematic aspects of PPP regulation in Kazakhstan remain, in particular:

- 1) The Concession Law still only provides the possibility to obtain ‘availability payment’ under the concession projects that have been classified as ‘socially important’, such as kindergartens, but not, for instance, petrochemical plant.
- 2) The Concession Law has recently introduced the concept of the ‘direct agreement’, however, relevant provisions remain rather unclear and not tested.

It should also be noted that draft Law ‘On Public-Private Partnership’ is now under the consideration of the Parliament of Kazakhstan. Our preliminary analysis of the draft law dated 31 December 2014 suggests that in its current form it is very superficial and in fact redundant.

18.2 Are there any legal impositions to project companies issuing bonds or similar capital market instruments? Please briefly describe the local legal and regulatory requirements for the issuance of capital market instruments.

Section 22-1 of the Law ‘On Securities Market’ contains certain requirements for the issuance and placement of emission securities by a Kazakhstan resident in the territory of a foreign state, including the requirement to receive the permission from the financial regulator for issuance and placement of such issuance securities in the territory of a foreign state.

19 Islamic Finance

19.1 Explain how *Istina'a*, *Ijarah*, *Wakala* and *Murabaha* instruments might be used in the structuring of an Islamic project financing in Kazakhstan.

Kazakhstani legislation does not specifically provide for these instruments, however, their close equivalents are stipulated under the Law ‘On Banks and Banking Activities’ and, moreover, general concept of freedom of contract allows the parties to enter into, generally, any contract even if it is not specifically provided for by legislation.

19.2 In what circumstances may *Shari'ah* law become the governing law of a contract or a dispute? Have there been any recent notable cases on jurisdictional issues, the applicability of *Shari'ah* or the conflict of *Shari'ah* and local law relevant to the finance sector?

As discussed above, save for certain exceptions, the parties to a contract are free to choose any foreign law, including *Shari'ah* law, as the governing law of the contract if one of the parties is a non-resident. We are not aware of any recent notable cases on jurisdictional issues and the applicability of *Shari'ah* or the conflict of *Shari'ah* and local law relevant to the finance sector.

19.3 Could the inclusion of an interest payment obligation in a loan agreement affect its validity and/or enforceability in Kazakhstan? If so, what steps could be taken to mitigate this risk?

If the loan agreement is with a foreign lender, no, it could not.

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- Listed, IFLR 1000 Central & Eastern Europe: Leading Lawyer (2013, 2014).
- Listed, Chambers Asia-Pacific: Asia-Pacific's Leading Lawyers for Business (2013, 2014, 2015).
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GRATA Law Firm was founded on 22 April 1992. It is one of the leading Eurasian law firms with more than 100 lawyers and a network of branches in Kazakhstan (Almaty, Astana, Aktau, Atyrau, Aktobe), Russia (Moscow), Azerbaijan (Baku), Kyrgyzstan (Bishkek), Tajikistan (Dushanbe), Uzbekistan (Tashkent), a country desk in Mongolia (Ulaanbaatar), as well as representatives in Canada (Vancouver), China (Beijing), the Netherlands (Amsterdam), UAE (Dubai), the United Kingdom (London) and USA (New York).

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- Corporate Tax
- Data Protection
- Employment & Labour Law
- Environment & Climate Change Law
- Franchise
- Gambling
- Insurance & Reinsurance
- International Arbitration
- Lending & Secured Finance
- Litigation & Dispute Resolution
- Merger Control
- Mergers & Acquisitions
- Mining Law
- Oil & Gas Regulation
- Patents
- Pharmaceutical Advertising
- Private Client
- Private Equity
- Product Liability
- Public Procurement
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