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The International Comparative Legal Guide to:

Project Finance 2012

A practical cross-border insight into project finance

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1 Overview

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

Project finance market in Kyrgyzstan is mostly represented by project financing in the mining sector where large amounts of funding are required to be raised. Given that only one large gold mine is currently fully operated in Kyrgyzstan, numerous other mineral deposits with fairly attractive reserves of precious, rare earth metals, and uranium etc., are frozen at the exploration stage, waiting for funding to proceed to the development stage; therefore, growth of the project finance market, in particular in the mining sector, is expected to take place in the near future.

As the political situation becomes more stable, public & private partnership projects in power engineering, infrastructure, transport and telecommunication may also become the key areas for project financing.

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

One of the largest recent project financings is financing of Kumtor gold mine (the biggest operating mine in the country) provided by EBRD for US\$ 150 mln in 2011. Another project financing of the major gold deposit named Andash for US\$100 mln is currently frozen due to the issues with the local community.

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?

Civil Code and Law on Pledge provide for the following types of security: (i) pledge of movable property; (ii) mortgage of immovable property; and (iii) pledge of rights. The law establishes specific requirements on execution and perfection of the security agreements subject to the collateral; albeit the law does not require to execute separate security agreement for each type of the collateral, in practice, separate security agreements are executed, taking into account the specifics on the execution and perfection subject to type of the collateral (movable, immovable or rights) established by the law and with a view to avoid the additional procedures and requirements, which differ depending on nature of

the collateral. For instance, mortgage agreement requires state registration with the public registration authority and notarisation while agreement on pledge of movable property is not subject to notarisation and is to be registered when amount of the secured obligation exceeds 30,000 KGS (approx. US\$ 650).

Agreement on pledge/mortgage is made in writing and must contain the names and addresses of the parties, a description and value of the secured obligation, identification of the collateral and its value, and the validity period and enforcement procedure (judicial or extrajudicial). It is worth noting that agreement on the extrajudicial enforcement may be incorporated into the body of the agreement on pledge of movable property and has to be executed as a separate document for the mortgage.

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

Civil Code of Kyrgyzstan provides for the following types of property: movable; immovable property; and rights. Movable property includes equipment, machinery, securities, and intangibles such as rights etc. Immovable property is represented by the land, subsoil, building, constructions and other assets firmly attached to the land.

Security can be taken over both movable (pledge) and immovable (mortgage) property. It is a concept of the Kyrgyz law that mortgage is a special type of pledge over immovable property, including the mortgage of enterprise as a property complex. It must be noted that foreign nationals and companies are only entitled to use the land in Kyrgyzstan, but can't own it, therefore, the foreign chargee having acquired the land as a result of the mortgage enforcement, must sell this land within one year after it is so acquired.

The collateral in Kyrgyzstan normally comprises all types of the collateral including equipment, machinery, various rights etc., as movables, and land, buildings etc., as immoveables.

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

Kyrgyz law allows taking security over the receivable on the chargor's bank account, which may be collected by the chargor in case of no default. The security over receivables is created by executing an agreement on pledge of funds on the chargor's bank account between the chargor, chargee and a servicing bank where the terms of such pledge are stipulated. Such pledge is to be

registered in case it secures an obligation with the value exceeding 30,000 KGS or approx. US\$650 to be valid and enforceable.

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

Security can also be taken of the cash deposited in bank accounts under the pledge agreement executed between the chargor, chargee and a servicing bank. The chargee is authorised to enforce such pledge immediately, in case of default. It is worth noting that the chargee may face certain difficulties with enforcement of the pledge where the collateral is cash in domestic currency through a public sale given that cash is a payment tool itself; therefore, it is recommended having security over the cash in foreign currency, which may be sold at a public sale for the local currency.

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

Security over shares in companies incorporated in Kyrgyzstan may be created in form of a pledge agreement. It must be noted that title to the shares (participating interests) in a Limited Liability Company is evidenced by its Foundation Agreement, Articles of Association and Extract from the Unified Register of Legal Entities. Shares of the Joint-Stock Companies are non-documentary and are reflected in an electronic form. Register of a Joint-Stock Company's shareholder is kept either by the in-house or independent registrar.

No notarisation is required for perfection of the security over shares/participating interests, however registration of the pledge of shares/participating interest securing an obligation, which value exceeds 30,000 KGS or approx. US\$650 is necessary for the pledge to be a valid and enforceable document.

It is worth noting that in case of enforcement of the security over shares/participating interest in a Closed (Private) Joint-Stock Company and Limited Liability Company, other shareholders enjoy the right of first refusal.

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)?

Security over the immovable property is subject to mandatory notarisation and registration in Kyrgyzstan. Fee for notarisation of a mortgage agreement is 300 KGS (US\$6.50), and registration fee is 586 KGS (US\$12.60).

Security over movable property is subject to mandatory registration in case value of the secured obligation exceeds the amount of 30,000 KGS or approx. US\$650. Fee for notarisation of a pledge agreement is 1,000 KGS (US\$22), and registration fee is 120 KGS (US\$2.50).

No other stamp duties or charge are payable apart from the notarisation and registration fees.

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?

In light of the Kyrgyz law, security is perfected by notarisation, and registration of the security documents, with the competent state registration authorities, as applicable.

The security perfection procedures are not too costly in Kyrgyzstan and do not take a substantial amount of time provided that all documents submitted for notarisation/registration are in order.

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.?

There are mainly no regulatory consents required for creation of security over the movable or immovable private property, other than corporate approval, or consent of the owner, in respect of private property or approvals of the competent state authorities, in relation to the state owned property.

The exceptions are enforcements of the mortgages/pledges where the collateral is a strategic asset and the Government enjoys its right of first refusal. Strategic assets include deposits, airports, and gas pipelines. Another example, is consent of the mining authority required for pledge of the mining rights.

3 Security Trustee

3.1 Regardless of whether Kyrgyzstan recognizes 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?

Kyrgyz law does not recognise the concept of "trust"; only the creditors/lenders can hold security interests in their capacity of pledgees/mortgagee.

There are concepts of pledge manager appointed by the chargee and enjoying all rights of the chargee and enterprise manager in case of enterprise mortgage responsible for the enterprise management and its preparation for sale enjoying rights of the enterprise management bodies once appointed, but these concepts are not similar with a 'trustee concept'.

3.2 If a security trust is not recognised in Kyrgyzstan, 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?

Kyrgyz law does not provide for similar mechanism to eliminate the need to enforce security separately. Each lender holding its security interest is to enforce its security interest on its own, and creation of security does not contemplate transfer of title to the collateral, to the chargee.

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?

Enforcement of security in Kyrgyzstan can be judicial or

extrajudicial subject to agreement of the parties. Judicial enforcement can be time and effort consuming, due to possible appeals from the chargor or other creditors.

Extrajudicial enforcement is more straightforward, but in practice often goes through a public sale to avoid any possible disputes from the chargor or other parties concerned.

As noted earlier, there are restrictions applicable to enforcement of pledges/mortgages where the collateral includes strategic assets triggering the Government's right of first refusal in case of their sale/transfer.

It must be noted that right of a secured creditor are not affected by the bankruptcy proceedings.

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

There are no restrictions, apart from when the collateral is land. Foreign nationals and companies can only use, but not own, the land in Kyrgyzstan, except for the case of mortgage crediting.

Foreign banks and financial & credit institutions can own the agricultural lands within one year in case they are acquired as a result of enforcement.

5 Bankruptcy 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?

Secured lender has a priority right under the bankruptcy proceedings, as compared to other creditors in case the security is valid and enforceable. Collateral of a secured creditor is not included into liquidation estate and is transferred to the charge for enforcement. In case the enforcement proceeds are not sufficient to satisfy the secured creditor's claims, the secured creditor becomes a third tier unsecured creditor and its unsatisfied claims may be satisfied *pro rata* to claims of other third tier creditors.

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?

Kyrgyz law on bankruptcy provides that the collateral is not included into the liquidation estate; therefore, a secured creditor is entitled to satisfy its claims independently from claims of the unsecured creditors and subject to its ranking in case other secured creditors are present.

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

Please see question 5.2.

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 enforcement?

Kyrgyz laws provide for the extrajudicial enforcement as long as the relevant provisions are included in the security agreement or represent a separate agreement on extrajudicial enforcement.

6 Foreign Investment and Ownership Restrictions

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

Laws of Kyrgyzstan do not set forth any restrictions on foreign ownership of a project company, other than those related with the use of land.

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

Many bilateral treaties on protection of investment are in place with many of the European, Asian and former USSR countries.

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

The key laws regulating nationalisation or expropriation of project companies and assets are the Constitution, Civil Code and Law on Investments, as well as international bilateral and multilateral treaties on mutual protection of foreign investments.

The Law on Investments states that the Government is entitled to provide various benefits in the priority areas of economy by executing the investment agreements and in case such agreements contain tax, customs or other exemptions/benefits, they are subject to ratification by the Parliament.

7 Government Approvals/Restrictions

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

The Government and its relevant ministries and agencies are responsible for overall coordination of strategic project sectors, such as mining, power generation transportation etc., within their competence.

The Parliament ratifies the investment agreements containing various exemptions and benefits.

By way of example:

1. State Property Fund under the Government is responsible for privatisation of the state owned assets;
2. State Inspectorate on Environmental and Technical Safety – for monitoring and compliance with the environmental and technical requirements;
3. Ministry of Economy and Antimonopoly Policy - for the antitrust clearance;
4. State Agency on Geology and Mineral Resources under the Government – licensing and control of the mining sector;
5. National Bank is the regulatory and licensing authority in the banking and financial sector; and
6. State Communication Agency under the Government is the licensor and coordinator within the telecom sector.

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?

All the financing or project documents must be duly executed and translated into either Russian or the Kyrgyz language if they were originally prepared and negotiated in another language (e.g. English). It is not strictly required that this translation be certified, except where such documents are filed with relevant authorities.

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)?

Ownership of assets alone would not typically trigger licensing requirement under the Kyrgyz law. Meanwhile, operation of certain assets, e.g. natural resources, pipeline, telecommunications equipment etc., is subject to licensing. A foreign entity operating through its Kyrgyz subsidiary or by virtue of shareholding in a company, registered in Kyrgyzstan, shall be allowed to obtain such a licence.

Operations in key business areas including, but not limited to, mining, subsoil use, extraction and processing of minerals, telecommunications, pharmaceuticals, wholesale trade, etc., are subject to licensing.

The exhaustive list of licensable activities in Kyrgyzstan is approved and regulated by the Law on Licensing.

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

Bonuses and royalties are the main specific mining taxes payable by a resident company in Kyrgyzstan. Bonus is a one time payment payable for obtaining a mineral right. Amount of the bonus depends on the quantity of reserves to be used under a mining right granted and type of natural resource.

Royalties are payable under the Kyrgyz tax law for the extraction of natural resources in Kyrgyzstan. Rate of royalty is subject to the type of a natural resource and amount of reserves extracted.

Income of non-residents received from extraction of the natural resources, is subject to 10% withholding tax.

Resident companies engaged in the mining sector operating in Kyrgyzstan also pay other applicable taxes.

The export VAT rate is 0%.

Please note that the competent state authority can exercise its right of refusal to purchase precious metal or their concentrates to be exported.

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

There are no such restrictions, apart from the anti-money laundering requirements in Kyrgyzstan.

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?

There are no restrictions preventing a foreign shareholder from receiving and repatriating dividends. Income of non-resident

without a permanent establishment in Kyrgyzstan is subject to 10% withholding tax.

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

Project companies are entitled to open and maintain onshore foreign currency accounts. Offshore accounts may be opened by the Kyrgyz resident companies, but these accounts are to be registered with 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 Kyrgyzstan or abroad?

There are no such restrictions in Kyrgyzstan; dividends paid abroad are subject to the withholding tax of 10%.

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?

Kyrgyz companies are required to comply with numerous environmental, health and safety requirements. Compliance with these requirements is monitored by the state regulators in various sectors. Normally, it is a requirement of the lender(s) that the project company complies with all applicable regulations in order to finance the project.

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

Public procurement is subject to specific regulatory framework in Kyrgyzstan. Procurement by project companies, where procurement involves financing arranged by private funds, or through foreign lending institutions, and not guaranteed by the Government, is subject to general commercial regulations and procurement practices. In this case, a “freedom of contract” principle shall govern procurement mechanics under relevant contractual arrangements.

Legal entities having state as their shareholder are subject to the public procurement procedures.

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?

Only insurance companies licensed in Kyrgyzstan are allowed to insure risks in Kyrgyzstan. Once insured with a Kyrgyz insurance company, these risks may be reinsured by a foreign insurance company. Reinsurance is normally required by foreign investors under major project finance projects.

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

It is standard practice in Kyrgyzstan that foreign (secured) creditors are appointed as loss payees under insurance policies over project assets.

9 Foreign Employee Restrictions

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

Any foreign workers (without distinction between different categories) seeking employment in Kyrgyzstan must obtain work permits prior to starting their work. Resident employer is also to obtain a permit for use of foreign workforce in addition to the work permit obtained by each foreign employee. Ministry of Youth, Labor and Employment issues a work permit for the maximum period of one year, which may then be renewed based on application.

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?

There are standard customs and security rules that apply to imports of equipment to Kyrgyzstan. In certain cases, where special-purpose equipment or products enter Kyrgyzstan, a permit of the relevant governmental agency may be required.

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

The following duties are paid in case of import of equipment, spare parts, components and raw materials to Kyrgyzstan:

- customs tariffs (5-15%, Kyrgyzstan as a WTO member grants favourable customs regime the list of WTO countries, Russia, Georgia and PRC);
- excise tax (rate is subject to the type of excisable products, basic rate is set forth in the fixed Som equivalent based on a calculation unit);
- import VAT (at the rate of 12%); and
- customs clearance fee (at the rate of 0.15%).

11 Force Majeure

11.1 Are force majeure exclusions available and enforceable?

Force Majeure exclusions are enforceable under the Kyrgyz laws.

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?

The Anti-Corruption Law of the Kyrgyz Republic defines

“corruption” as, profit-motivated actions of the officials, performing certain responsibilities in public sector, intended to gain illegal benefits that subsequently lead to the breach of their duties imposed on them by the status of a state official.

Corruption embraces bribery, larceny, negligence, and appropriation of public and private property by the state officials, as well as the malpractice.

Corruption is punished by imprisonment for up to 20 years; nevertheless, the level of corruption in Kyrgyzstan remains high.

13 Applicable Law

13.1 What law typically governs project agreements?

Although the application of Kyrgyz law is mandatory in certain types of transactions (e.g. transactions between Kyrgyz legal entities), the choice of foreign law by a Kyrgyz legal entity in other contracts with a foreign counterparty should be recognised, and given effect to, by the Kyrgyz courts, unless the consequences of the application of foreign law contravene Kyrgyz public order. Therefore, there is no particular need for a project agreement to be governed by local law in order for such agreement to be valid and enforceable in light of the of Kyrgyz laws.

When foreign law is the choice of governing law, the mandatory provisions under Kyrgyz law, in respect of methods, and procedure involving performance of the agreement, shall still apply. Hence for a project agreement to be enforceable by a Kyrgyz court, it must be valid under the Kyrgyz law, even though the governing law is foreign law. The foreign law shall be used by the Kyrgyz court to interpret provisions of the project agreement with regard to the rights and obligations of the parties, as well as to the consequences of non-performance or undue performance of the obligations. However, the enforcement procedures shall be performed in accordance with the Kyrgyz law, should the agreement be enforced locally.

13.2 What law typically governs financing agreements?

English law is typically a choice of foreign law in cross border transactions. This choice of foreign law for financing agreements is acceptable under the Kyrgyz law (except for security transactions involving Kyrgyz based real estate). However, the mandatory rules, bankruptcy rules etc. and Kyrgyzstan’s public policy, remain applicable.

13.3 What matters are typically governed by domestic law?

The security documents in respect of the property registered in Kyrgyzstan are required to be governed by the laws of Kyrgyzstan.

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?

Kyrgyzstan is not party to any multilateral or bilateral treaties with any western jurisdiction or the United States for the mutual enforcement of court judgments. Consequently, should a judgment be obtained from a court in any western jurisdiction or the United States, it is highly unlikely to be given direct effect by the Kyrgyz courts.

Article 168 of the Kyrgyz Civil Code specifies that the state (represented by the government) takes part in relationships regulated by civil legislation, on an equal basis with other participants and is liable for its undertakings with its own property excluding the cases provided by law.

15 International Arbitration

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

Kyrgyzstan is a party to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Accordingly, a foreign arbitral award obtained in a state which is party to that convention should be recognised and enforced by a Kyrgyz court, subject to the qualifications in the UN Convention and compliance with the Kyrgyz civil procedure and the procedures established by the Kyrgyz laws on commercial arbitration for the enforcement of arbitration decisions. We note, however, that in practice, reliance upon international treaties may require that relevant Kyrgyz officials be supplied with more information as to the effect and procedures under the treaty, which may not be entirely consistent with the legislation relating to procedure or with court rules. This could delay enforcement procedures in Kyrgyzstan.

Arbitration clause is to be included into body of the agreement or is to be made as a separate agreement with a set of the required provisions in order to submit dispute to the international arbitration.

It must be noted that the scope of grounds for refusal to recognise and enforce an arbitral award is wider under the Kyrgyz Civil Procedure as compared with the same grounds of the UN Convention.

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

Please refer to question 15.1.

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

Disputes on administrative, family and employment matters and matters in respect of real estate are resolved only by the courts of Kyrgyzstan. Contractual disputes shall not be subject to arbitration, unless otherwise provided by a specific arbitration clause in the agreement.

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

There are no such types of disputes that are subject to mandatory domestic arbitration proceedings.

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?

To the best of our knowledge, there have been no calls for political risk protections; however, there are provisions on protection of investments from the expropriation, nationalisation etc., in the investment agreements between the Government and investors.

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?

There is a withholding tax at the rate of 10% from an interest payable on loans made to domestic or foreign lenders deducted at source of payment. The withholding tax is applicable unless otherwise is specified in a bilateral double tax treaty with the foreign lenders' country of residence. The proceeds of a claim under a guarantee or the proceeds of enforcing security shall apply to the extent they involve any amounts of interest.

There are no general tax incentives applicable to foreign investors or creditors.

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?

There are no general tax incentives applicable to foreign investors or creditors.

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 Kyrgyzstan?

We do not anticipate any other material considerations at this point of time.

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Mongolia

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1 Overview

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

Mongolia is currently experiencing an economic boom and a rapidly developing industry. The more recent discoveries of mineral deposits have led to a huge rush of their extracting by some of the world's leading mining companies. As a result, mining is now a key industry accounting for 85 percent of the country's exports in 2011. Mongolia's extensive mineral deposits have attracted foreign investors, and the country is undergoing an economic transformation through its mining boom. Mongolia possesses copper, gold, coal, molybdenum, fluorspar, uranium, tin, and tungsten deposits, among others, which account for a large part of foreign direct investments and government revenues. Thus, the country's situation demands infrastructure development. The Law on concessions, adopted in 2010, sets out legal framework for private sector participation in the development of infrastructure projects in Mongolia. The Mongolian Government has approved a list of 121 projects, inviting private sector investments. Furthermore, the Law on national development of banking, adopted in 2011, sets out a legal framework for the Government to collect investments for big projects.

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

Mongolia is rich in minerals, in particular, coal, copper, iron ore and precious metals. The mineral sector, as well as related processing industries, has been for years the main area for project finance in Mongolia. This trend is likely to persist in future.

The world's leading copper and gold mine, Oyu Tolgoi, project was financed with a USD 3.5 billion investment at the end of 2011.

Korea proposed a USD 260 billion investment for the world's leading coal project of Tavan Tolgoi just 2 days before the National Development Bank successfully issued a USD 580 million bond for foreign investors.

Further, the Government plans to collect investments of USD 6.2 billion for 100,000 household apartments, USD 7 billion for railway development, and USD 10-14 billion for the establishment of the Sainshand Industrial Park.

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?

The Civil Code of Mongolia, dated 10 January 2002, as amended (the "Civil Code") and the Law of Mongolia on Mortgage, dated 9 July 2009, as amended (the "Law on Mortgage") basically governs the creation and application of different types of security. Under the Mongolian Civil Code, there are generally three types of proprietary security interests: mortgages; pledges; and rights. The general requirement for all three types of security is that the security agreement shall be made in a written form. A security agreement on immovable property must be notarised and registered with the state agency of property registration.

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

Security can be taken over real property (land), plant, machinery and equipment (e.g. pipelines, whether underground or overground). The Civil Code makes a distinction between moveable and immoveable property. Land parcels, subsoil rights, water rights and everything firmly connected to the land (i.e. other objects which cannot be removed without causing a disproportionate harm to their use, such as forests, perennial plantings, buildings and structures, pipelines, aircrafts, etc.) are categorised as immoveable property. Items classified as moveable property are equipment, machinery, money, commercial paper, securities and other intangibles (such as contract rights and/or other rights).

Security over land can be taken only by Mongolian citizens and Mongolian legal entities. The security over land is governed additionally by the Law on land of Mongolia, dated 7 June 2002 (as amended "Land Law") and/or the Law on land ownership of Mongolian citizens, dated 27 June 2002 (as amended "Law on Land Ownership"). This is distinct from possession of land by an individual. In order to mortgage a certain plot of land, its landholders (who possess this plot of land) shall receive the consent of the respective state authorities who are state land managers. In order to create a mortgage over land, landowners (who own the

land) shall register the mortgage with the state agency of property registration, no additional consents are required. Machinery and equipment are movable property. The general requirement for security agreement on movable property is that the security agreement shall be done in a written form. There is no unified register of security agreements on movable property in Mongolia. This could be a disadvantage and a substantial risk for a potential lender since pledge provider will be able to pledge the same collateral to various pledge holders.

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

Security over receivables is provided under Mongolian law and it allows the chargor to hold security and make use of it to exercise its activity and to continue to collect in the receivables, until the chargor is in default and the chargee notifies the debtor in relation thereto. The security agreement over receivables is valid only if it is done in a written form. Parties to the agreement can choose to notarise the agreement for additional safety reasons.

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

Security over cash deposited in bank accounts is permitted under Mongolian Law. There are no special rules addressing the creation and perfection of security over cash deposited in bank accounts. In this case, general provisions of Mongolian law on security over movable property shall apply.

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

Security over shares can be taken in incorporated companies. There is no registration requirement of security over shares of private companies. The private companies can issue a certificate confirming the shareholding, which shall not be deemed a saleable instrument. The security over shares of a private company shall be consented by other shareholders according to the statute of a company.

The Mongolian Securities Clearing House and Central Depository (as amended "Securities clearing house") registers security agreements over shares of public companies. The public company shares can be issued in a certificated form from the Securities clearing house.

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)?

The notarisation fee is related to the property value or an underlying agreement value. The notary fee for agreements under MNT 1 million value (approximately USD 750) is 0.5%. Fees for agreements from MNT 1,000,001 (approximately USD 750) to MNT 500,000,000 (approximately USD 372,000) vary from MNT 10,000 to MNT 300,000 (from USD 7.50 to USD 230 respectively). This does not depend on the types of assets. Only mortgages shall be registered with the state agency of property registration. The

stamp duty for registration transactions involving a mortgage/pledge of assets is 0.05 percent for ordinary service and 0.1 percent for express service of the amount specified in the underlying agreement as the value of a mortgaged/pledged item. An additional MNT 8,000 (approximately USD 6) is charged for the application fee. Fees applicable to state organisations are not high.

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?

The filing, notification or registration requirements in relation to security over different types of assets do not involve a significant amount of time or expense. The Mongolian Government is making every effort to reduce the delay of state services. For example, state registration of a mortgage takes 3 working days for ordinary service and 1 working day for express service.

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.?

A security agreement over land requires the consent from a local land manager if the chargor is a landholder (who owns the land). Otherwise, there are no other regulatory or similar consents required with respect to the creation of security over immovable property, e.g. plant, or movable property, e.g. machinery and equipment.

3 Security Trustee

3.1 Regardless of whether Mongolia 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?

There are no regulations in relation to "security trustee" under Mongolian Law. The enforcement of security interests is performed by the office of bailiffs. With regard to securing charges, the court issues an order for seizure of the secured property to discharge the claims, considering that the security agreement by law constitutes an executive title. Following this, the bailiff, in compliance with the order issued by the court, proceeds with the seizure of the collateral and consigns it to the chargee or to the person authorised by the chargee. The security trustee or agent can be replaced by a lawyer.

3.2 If a security trust is not recognised in Mongolia, 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?

There are regulations under Civil Law regarding parallel debt or joint and several creditor status to achieve the effect referred to above which would allow one party (lawyer) to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately.

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?

With regard to security over movable property, the security agreement by law constitutes an executive title and is enforced by the bailiff upon a court decision. The lender, upon taking possession of the collateral, can proceed either with a private or public sale, auction or restricted bid procedures, provided that 'arm's length' principles are observed. The chargee can proceed with the enforcement, provided that the chargor and any other successive chargees are notified in written form at least 14 days before the sale takes place. Where enforcement involves security over immovable property, notification of the debtor (14 days) is mandatory in order to allow the debtor to voluntarily execute an obligation. In case of failure of the debtor to voluntarily execute an obligation, the bailiff officer proceeds with the enforcement, which shall be organised in the form of a public auction.

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

There are no regulations specified with regard to foreign investors or creditors, as well as no disadvantages/advantages and restrictions. The security over land can be taken only by Mongolian citizens and Mongolian legal entities.

5 Bankruptcy 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?

As a consequence of the creation of a security, upon insolvency of the project company, the project lender shall be regarded as a secured creditor and shall be a third-tier creditor in the waterfall of creditors under the Law of Mongolia on Bankruptcy.

The waterfall of creditors upon insolvency may be summarised as follows:

- court expenses, the remuneration of the liquidator, current utility payments, and claims arising from the obligations assumed in the process of liquidation are always paid before creditors;
- first tier – taxes and other mandatory payments to the budget; wages and tort claims (negligence);
- second tier – payments that are due in connection with mandatory insurance and mandatorily insured local bank loans (retail and depositor loans);
- third tier – payments that are due to secured creditors (secured either by a pledge or by a mortgage);
- fourth tier – payments that are due to unsecured creditors;
- fifth tier – payments that are due to shareholders, participants or founders of the bankrupt entity; and
- sixth tier – all other payments.

The claims of secured creditors may be satisfied only at the expense of proceeds received from the sale of all pledged property within

the bankruptcy proceedings. To obtain these proceeds, the liquidator must first sell the secured assets as well as the unsecured assets of a bankrupt entity, and then distribute the proceeds of secured assets to secured creditors, and the proceeds from unsecured assets to unsecured creditors. Secured creditors are treated as one class with no distinct priority between such creditors on the basis of the property pledged to each. The distribution within the classes of creditors is to be made on a proportionate basis. This risk of proportionate satisfaction of claims of secured creditors under Mongolian laws shall be mitigated by the negative pledge covenant under a facility agreement.

The claims of secured creditors as a class shall not be subject to the obligatory six tiers of claims (as specified above) that must be satisfied from the proceeds of sale of the bankruptcy estate. Rather, the claims of the class of secured creditors shall be satisfied from the pledged property separately from and without regard to the other unsecured creditors, even those with a higher priority (e.g., creditors of first and second tiers). This is the one advantage which the secured creditors may enjoy under Mongolian laws in the event of pledgor's insolvency.

In the meantime, if the proceeds are not sufficient to satisfy in full the claims of all secured creditors, the outstanding claims of any of such secured creditors shall be regarded the claims of the fourth tier (unsecured creditors) and shall be paid from the bankruptcy estate remaining after the satisfaction of claims of two preceding tiers (without regard of the third tier).

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?

There is no express or hidden provision under Mongolian law that gives preference to local banks as unsecured creditors over foreign banks, provided that a Mongolian court or Mongolian state authorities fail to interpret otherwise the provisions of the Civil Code and the Law on Mortgage of Mongolia.

Under the Decrees, a Mongolia bank is entitled to foreclose on the liquid assets of a Mongolia resident should an event of default occur under the loan agreement between such Mongolian bank (as lender) and a Mongolian resident (as borrower). Our interpretation of the related codes are that the secured property of the Mongolia resident, if any, shall fall outside the scope of such liquid assets and, therefore, notwithstanding the provisions of the law, Mongolian banks (as lenders) shall not be entitled to foreclose on the property that has been already secured in favour of foreign banks or other secured parties by the time of such foreclosure. The secured property shall be ring-fenced from the claims of any third parties by the Law on Mortgage of Mongolia and the Civil Code. The latter have superior legal power over the codes in the hierarchy of Mongolian laws and regulatory acts. We therefore refer to the provisions of superior regulatory acts (the Civil Code and the Law on Pledge) when opining on the validity and enforceability of the security created in the lenders' favour. To the best of our knowledge, there are no reported cases in which this question has been considered before the courts in the Mongolia.

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

Please refer to question 5.2.

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?

There are no out-of court proceedings available to creditors, as insolvency procedures, once commenced, are subject to judicial control.

6 Foreign Investment and Ownership Restrictions

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

The treatment of investment projects or, to this extent, of a project company varies subject to the applicable investment regime. For some projects (typically involving investments of USD 50 million or above) in the mining sector the investment agreement can be concluded between the investor and the Ministry of Energy, Geology and Mining under authorisation by the decree of the Cabinet of Ministers.

Subject to the type of project or activity of the company, certain licences, permits or governmental approvals or other authorisations can be required.

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

Foreign investors enjoy legal protection guaranteed and governed by the laws of Mongolia, as well as by international treaties to which Mongolia is a signatory. Mongolia has joined the Washington Convention on the Settlement of Investment Disputes between the States and Nationals of Other States (1965, joined in 1996) and the “Seoul Convention on Investment Insurance” (1985, joined in 1999).

Also, since January 1999, Mongolia has been a full member of the Multilateral Investment Guarantee Agency (MIGA) of the World Bank Group, and investors will, thus, be eligible for risk insurance through MIGA. As of 1998, Mongolia has signed trade agreements with 78 countries and became a member of the World Trade Organization in 1997.

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

The Civil Code and Law on foreign investments, as well as international bilateral and multilateral treaties on mutual protection of foreign investments, regulate nationalisation or expropriation of project companies and assets.

The Constitution of Mongolia protects private property; however, no particular forms of investment are specifically protected from nationalisation and/or expropriation. As a general rule, any assets can be nationalised or expropriated for the purpose of public interest in accordance with legally established procedures on the basis of the non-discrimination principle, with full compensation of the value of such assets.

Investment agreements are concluded in the form of concession, product sharing, marketing and management, as well as franchising, for the implementation of certain projects without the formation of a legal entity in accordance with the Law on foreign investments.

Certain strategic projects and/or companies are provided with a preferential status and tax regime on the basis of an investment agreement that shall be concluded pursuant to the procedure established in Article 29 of the Law on minerals of Mongolia.

7 Government Approvals/Restrictions

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

Coordination of strategic project sectors, such as oil and gas, uranium, cooking coal, mineral extraction and power generation, is executed by the Government of Mongolia. Furthermore, all projects in strategic sectors are approved at the governmental level. Monitoring of the project, as well as facilitation functions are assigned to the governmental agencies (such as ministries, committees, agencies and associations) for the project oversight. These agencies are typically the issuing authorities of licences and permits.

Any projects involving the privatisation of state-owned assets or transactions contemplating the transfer of facilities, in which the Government is a stakeholder, require explicit permission of the *State Property Committee*.

Monitoring of, and compliance with, environmental standards, issuance of special water use and air emission permits, mandatory environmental impact assessments, as well as enforcement of environmental requirements, fall within the authority of the Ministry of Nature and Environment of Mongolia.

Antitrust clearance and general compliance with anti-monopoly legislation are controlled by the *Agency for fair competition and customer protection*.

The *Petroleum Agency of Mongolia* is the licensing authority for granting subsoil rights (e.g. mineral extraction or cement manufacturing projects).

The *Mineral Resources Authority* is the state agency responsible for ensuring safety standards in mining and utility sectors and for licensing of mining works.

The *Central Bank of Mongolia* (CBM) is the regulatory and licensing authority in the banking sector. It issues licences to commercial banks for the purchase of shares in Mongolian banks by foreign banking/investment institutions, as well as for the establishment of representative offices of foreign banks and for opening foreign banks.

The *Financial Regulatory Commission* of Mongolia regulates the microeconomic sector, securities market, currency exchange and insurance market of Mongolia by issuing licences and supervising such activities. It is appointed by the Parliament and is considered autonomous from the Government.

The *Mongolian Agency for Communications and Information* acts as a coordinating hub for projects and as a licensing authority in the telecommunications sector.

The *Inspection and Quarantine Agency* is the state institution for controlling and executing state standards, regulations and laws.

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?

All financing or project documents shall be translated into

Mongolian language if they are originally prepared and negotiated in a foreign language. It is not strictly required that such translation is notarised, except where such documents are filed with relevant authorities. For example, the CBM requires that the Mongolian translation of relevant facility agreements (or other similar financing agreements) are notarised for filing purposes. There are no requirements of notification and registration for financing or project documents. It is, therefore, sufficient if financing or licensing documents are submitted to relevant governmental authorities.

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)?

The ownership of assets alone would not typically trigger licensing requirements under Mongolian law. However, the operation of certain assets, e.g. natural resources, pipeline, telecommunications equipment, etc., is subject to licensing. A foreign entity operating through its Mongolian subsidiary or by virtue of a shareholding in a company, registered in Mongolia, shall be allowed to obtain such a licence.

Operations in key commercial areas, including but not limited to mining, subsoil use, extraction and processing of minerals, telecommunications, pharmaceuticals, wholesale trade, etc., are subject to licensing.

The exhaustive list of licensing operations in Mongolia is approved and regulated by the Law on licensing.

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

Taxes are imposed on royalties in cases where a domestic or foreign company extracts natural resources in Mongolia. The rate of royalty tax depends on the entity paying the tax, i.e. a domestic entity or a foreign entity with or without a permanent establishment.

In relation to a foreign entity without a permanent establishment in Mongolia, the current rate of royalty tax is 20%. This is a profit-based tax.

In relation to a domestic entity or a foreign entity extracting natural resources in Mongolia, the following taxes shall apply:

- Income Tax.
- Royalty Tax.
- VAT.
- Excise Tax.
- Customs Duty.

The above taxes are based on the amount of natural resources extracted or processed in every fiscal year. Tax rates applicable to each type of taxable operations are subject to annual review by the Government. The list of processed products is set out by the Government of Mongolia.

The export of natural resources is subject to the following taxes:

- VAT at 0% (except for precious metals); VAT for precious metals is established by the Cabinet of Ministers.
- Excise tax – the rate varies subject to the type of natural resources.

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

Currency Exchanges are conducted by banks licensed by the

Central Bank and non-banking organisations licensed by the Financial Regulations Committee. The official currency of Mongolia is Mongolian national tugrik (MNT) pursuant to the Law on making payments and settlements in the national currency of Mongolia, dated 9 July 2009. According to the Law, it is prohibited to set prices, carry out settlements, run advertisements in foreign currencies, and operate settlement units without the official approval of the Central Bank of Mongolia.

However, there are no restrictions applied to the banks and non-banking organisations for opening cash deposit accounts, issuing credits and carrying out other financial services in foreign currencies. There are also no restrictions for national legal entities, foreign investment companies, affiliates and representative offices to transfer, pay, and receive payments in foreign currencies. However, the Central Bank examines agreements, closes accounts and suspends transactions if suspicious circumstances occur. Such actions shall be carried out in accordance with national and international regulations concerning anti-money laundering. Banks shall examine transactions over USD 20,000.

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?

There are no restrictions preventing a foreign shareholder from receiving and repatriating dividends. The return of capital is also possible provided that a valid legal basis exists. Such legal basis includes either: (i) the exit of a foreign shareholder from a resident company by selling its stake to another party; (ii) the withdrawal of a foreign shareholder by selling its stake to a resident company (redemption of shares by the issuer of these shares); this option is limited to open joint stock companies in certain cases only; no limitations apply with respect to limited liability companies where any shareholder can exit at any time; or (iii) liquidation of a resident Mongolian company. No threshold, however, exists for buying a stake in a Mongolian bank by a foreign participant. A prior anti-trust clearance is required before entering into a sale and purchase agreement. A shareholder shall not be entitled to sell its stake and withdraw from a resident company unless the purchaser of such stake obtains the required anti-trust clearance. No fee is applicable with respect to anti-trust clearance.

The other control procedure, applicable to the withdrawal of capital, relates to the manner of calculation of the amount of capital withdrawn in cases (ii) and (iii) above. Redemption of a participating interest in a limited liability company shall be based on the latest balance sheet value. No fair or market value shall be applicable in such a case. Therefore, the right of the exiting foreign shareholder to demand the payment of fair value or market price for its stake is limited by the applicable law.

There are no restrictions that prevent a resident company from making payments of principal, interest or premiums on loans or on bonds (issued by a Mongolian joint stock company) to parties in other jurisdictions (all collectively referred to as “payments”). The payments, with respect to loans, shall be transferred by a Mongolian authorised bank (where a resident company holds a foreign currency account) to a non-resident bank provided that a loan is registered with the CBM. The amount of annual interest payable under a loan agreement shall not exceed 20% at the risk of investigation under Mongolian anti-money laundering and transaction-monitoring regulations. Any payments shall be made from hard currency funds accumulated in a resident company’s local bank account from export proceeds or other ‘own sources of currency receipts’, otherwise a resident company will have to apply for a contingent and sustainable conversion procedure. As a matter

of practice, conversion of local currency into a foreign currency is carried out with frequent delays due to limited access of local commercial banks to foreign exchange reserves. There are no restrictions in Mongolian laws for direct transfer outside Mongolia of hard currency proceeds from a resident company's foreign currency account to a non-resident bank in order to discharge its obligations for interest and principal payments under a loan agreement. However, any transfers to an account located in an offshore jurisdiction triggers the special financial screening procedure mentioned above. There are no restrictions under Mongolian law as to the payment of interest at the expense of borrowed money.

From a tax perspective, interest or premiums on loans, as well as any other fees and commissions, penalties and/or default interests, payable in connection with a loan or bonds (issued by Mongolian joint stock companies) shall be considered an income and subject to withholding tax at the rate of 20% payable at the payment source, i.e. by a resident company by virtue of deduction, unless otherwise provided in a bilateral double taxation treaty concluded with a country of a non-resident bank.

From a tax perspective, dividends or interest (on participating interest in a Mongolian LLC), as well as income generated from the sale of capital shall be subject to Mongolian withholding tax. In relation to dividends and interest, a 10% withholding tax shall apply, while in relation to income generated from sale or withdrawal of the capital, a 20% withholding tax shall apply.

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

Project companies are entitled to open and maintain onshore foreign currency accounts. There are no regulations and restrictions with respect to opening, closing and managing offshore bank accounts for registered legal entities of Mongolia.

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 Mongolian or abroad?

Please refer to question 7.6 for certain aspects of dividends payments. With respect to dividends, there is no maximum or minimum threshold established by Mongolian law for repatriation of dividends. Dividends can be paid annually, semi-annually and on a quarterly basis, subject to satisfactory financial performance of a resident company.

Dividends shall not be distributed and repatriated until all taxes are paid in full by the borrower. Any payment of dividends by a resident company to a foreign shareholder is subject to the special financial monitoring procedure conducted by tax authorities. Taxation of dividends shall be carried out at two stages: corporate; and individual. At a corporate level, the profit of a resident company shall be subject to income tax and all other applicable taxes. When all taxes at a corporate level are paid by a resident company, the net profit shall constitute the dividends of a foreign participant (shareholder). Such dividends shall be subject to withholding tax in Mongolia payable at the payment source (i.e. subject to withholding obligations of a resident company) at 20%, unless otherwise provided in a bilateral 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?

Mongolian companies are subject to environmental, health and safety laws and regulations.

The following are public authorities of Mongolia responsible for developing and amending the Investment Programme of Mongolia:

- Ministry of Labour and Social Protection – regulatory authority with respect to industry labour standards;
- Ministry of Health – regulatory authority with respect to health and sanitary standards;
- Petroleum Agency – regulatory and executive authority of licensing of petroleum exploration, as well as contracting and licensing of export and import of petroleum products; and
- Inspection and Quarantine Agency – the state institution for controlling and executing state standards, regulations and laws.

Any investment projects are subject to obtaining prior environmental approvals by the Mongolian Ministry of Nature, Environment and Tourism. Under Mongolian environmental laws, the Ministry of Nature, Environment and Tourism is a competent state authority with powers to monitor environmental compliance.

Investment projects, involving construction or any other type of physical infrastructure development, or that are likely to cause any impact on the environment, are subject to mandatory prior environmental screening (environmental impact assessment or EIA).

The process of obtaining EIA approval from the Ministry of Nature, Environment and Tourism for individual projects is divided into three phases. Under phase I, before any project-related works are cleared for financing, the applicants are required to submit a draft environmental statement (Phase I). Following approval of the draft under Phase I and prior to the approval of the feasibility study, the applicants are required to proceed with an environmental impact statement (Phase II). At the final stage and prior to the commencement of any project-related works, the applicants are required to obtain approval for a statement of environmental effects (Phase III). No financing is allowed under any projects unless the relevant EIA approval has been obtained.

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

Public procurement is subject to specific regulatory framework in Mongolia. Procurement by project companies, where procurement involves financing arranged by private funds or through foreign lending institutions and not guaranteed by the Government in Mongolia, is subject to general commercial regulations and procurement practices. In this case, a “freedom of contract” principle shall govern procurement mechanics under relevant contractual arrangements.

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?

According to Article 17.1 of the Law on insurance of Mongolia, only insurance companies licensed in Mongolia are allowed to insure risks in Mongolia. Pursuant to the list of licensed insurance

companies, there is no foreign insurance company licensed under Mongolian law. Therefore, on the basis of Articles 46 and 47 of the Law on insurance of Mongolia, Mongolian insurance companies are entitled to insure risks under reinsurance with foreign insurance companies.

As a matter of practice, the following mechanisms are common for insuring risks by foreign insurance companies. In case an insured is willing to insure risks with a foreign insurance company, the insured pays an insurance premium to a foreign insurance company through a Mongolian licensed insurance company. It depends on the jurisdiction of a foreign insurance company. According to the reinsurance agreement, in case of insurance casualty, a Mongolian licensed company examines such insurance casualty for a commission fee. Such proceeding is conducted under supervision and with the participation of the Financial Regulatory Commission.

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

As a matter of practice and rule, if foreign (secured) creditors are appointed as loss payees under insurance policies over project assets, Mongolian law allows the payment of such insurance policy.

9 Foreign Employee Restrictions

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

According to Article 30 of the Law on legal status of foreign citizens, foreign citizens seeking employment in Mongolia shall obtain work permits. Work permits are issued by the Ministry of Labour and Social Protection to the employer. For issuing work permits, the Ministry of Labour and Social Protections shall obtain references from several state authorities depending on the activity of an employee and employer. As a general rule, the Ministry refers to the labour and social welfare departments, as well the migration office. The order of obtaining a work permit is established by Order No. 139/327 of 2007.

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?

There are standard customs and security rules that apply to imports of equipment to Mongolia. In certain cases, where special-purpose equipment (such as weapons, explosives, drugs, etc.) enters Mongolia, prior entry clearance shall be obtained from a relevant governmental agency or the Government.

Customs duties and excise taxes applicable to each type of imported equipment vary subject to the purpose and origin of the equipment and commodities.

The Law on value added tax of Mongolia does not provide special regulations on construction related equipment and other materials.

The Parliament issues special legislation acts for any exemption from VAT and customs duties. For example, for equipment, imported for the implementation of particular projects established by an international loan agreement or agreement on financial assistance, the Parliament has issued several laws on exemption from customs duties and VAT.

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

The following duties are paid in case of the import of equipment, spare parts, components and raw materials to Mongolia.

- Customs duties (rates vary from 0-15%).
- VAT (at the rate of 10%).

Customs duties vary subject to applicable trade regimes: the regular regime; or the most favoured nation regime. Customs duty for regular regime commodities is doubled in comparison to the most favoured nation regime. The most favoured nation regime applies under the following conditions:

- commodities, originated or imported from the countries that are signatories to free trade agreements with Mongolia or other agreements; and
- other countries included in the list of the most favoured nations approved by the Government.

Mongolian legislation allows certain exemptions with respect to the import of specific goods. According to the Law on customs duties, exemption for some materials, equipment, machinery and mechanisms, 17 specifically named types of machines and equipment, such as cranes, excavators, cement processing machines, and elevators, are exempted from customs duties, if they are imported for technical innovations in the construction sector. The Law also provides exemptions for several types of raw materials and equipment imported for technical innovations in the construction industry.

11 Force Majeure

11.1 Are force majeure exclusions available and enforceable?

Force Majeure exclusions are enforceable under Mongolian laws.

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?

International organisations and anti-corruption authorities assert that the level of corruption in Mongolia stays at a high level. A special anti-corruption agency investigates corrupt practices in Mongolia. Meanwhile, the Parliament adopted the Law on corruption, as of 6 July 2006, and the Law on prevention and separation of personal interest in public services in 2012. Giving or accepting bribes and mediating in bribes are criminal offences that are severely punishable.

According to the Law on corruption, for the prevention of corrupt practices, public officers shall provide income declarations to anti-corruption authorities, while declarations of high-profile state officials are subject to annual publication.

Mongolia has ratified a number of bilateral and multilateral treaties against corruption and money laundering, including the 2003 Convention Against Corruption and the 1999 International Convention for the Suppression of the Financing of Terrorism.

13 Applicable Law

13.1 What law typically governs project agreements?

The Civil Code and Law on foreign investments are the main laws governing project agreements in the private sector. If the transactions/project agreements require special permission and registration, they are governed by other laws, such as the Law on state registration of ownership rights and other relevant rights over assets and the Law on concessions. It should be noted, however, that if an international agreement, to which Mongolia is a member, establishes different rules, such international agreement's provisions shall prevail.

13.2 What law typically governs financing agreements?

Financing agreements are governed by the Law on the financial regulatory commission, the Law on banking, the Law on Central Bank, the Law on securities market, as well as the laws and regulations of foreign exchange. The choice of foreign law applicable to financing agreements is not acceptable.

13.3 What matters are typically governed by domestic law?

Please refer to question 13.2. Financial, employment and pledge related matters are typically governed by domestic law.

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?

Mongolia has concluded agreements on legal assistance in civil procedures with 17 countries. These agreements provide for recognition and enforcement of court decisions of foreign jurisdictions.

In accordance with Article 7.3 of the Civil Code of Mongolia, the state, administrative regions and other administrative units participate in civil law relationships as legal entities. This provision clearly states that the state does not enjoy any special treatment and sovereign immunity in private relationships, particularly carried out in commercial activities.

15 International Arbitration

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

Mongolia is a party to the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Accordingly, a foreign arbitral award obtained in a state which is a party to that Convention shall be recognised and enforced by Mongolian courts according to the procedures set out by the Code on Civil Procedure of Mongolia. As a matter of practice, delays in enforcement procedures are common in Mongolia.

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

Please refer to question 15.1.

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

Disputes on administrative, family and employment matters are solved only by the courts of Mongolia. Contractual disputes shall not be subject to arbitration, unless otherwise provided by a specific arbitration clause in the agreement.

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

There are no such types of disputes that are subject to mandatory domestic arbitration proceedings.

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?

To the best of our knowledge, there have been no calls for political risk protections.

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?

Under the current laws of Mongolia, there are no requirements to deduct or withhold tax from interest payable on loans made to domestic or foreign lenders or the proceeds of a claim under a guarantee or the proceeds of enforcing security.

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?

There is no preferential tax regime applicable to foreign investors or creditors. Specific tax incentives can be granted by the Government under an investment agreement entered between the investor and the Government of Mongolia. An investment agreement is designed to grant tax, customs, payments and other exemptions and waivers, in addition to those existing under the general legal framework. Certain fees and procedures are required for the registration of foreign investment companies.

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 Mongolia?

We do not anticipate any other material considerations.

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COLIBRI LAW

COLIBRI Law firm is a group of transactional lawyers working in emerging markets, with coverage in Georgia, Kazakhstan, Kyrgyzstan, Mongolia, Tajikistan, Turkmenistan, Uzbekistan and UAE.

The types of clients its team has assisted range from Fortune Global 500 corporations to small start-up companies with operations in a variety of sectors.

Having advised on complex transactions across the region which span from pioneering multibillion energy and upstream projects to first public-private partnership medical projects, the firm specialises in a wide range of products generated by the firm's organically interacting practices staffed with lawyers coming from different cultures, industries and backgrounds. Most of the partners and associates graduated from oldest US, German and UK law schools, and have previously worked in international law firms.

Uzbekistan

Sofia Shakhrazieva



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Colibri Law Firm

1 Overview

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

Uzbekistan has been consistently commended by the IMF, ADB and World Bank for its tight monetary policy and resilience to the global economic downturn. This is largely attributed to the country's selective approach to foreign borrowings and the conservative level of reliance on world capital markets for generating domestic growth. Investment in key energy and manufacturing sectors, coupled with priority infrastructure development, remain dominant areas of the project finance in Uzbekistan. Infrastructure development is, by and large, funded by the state, occasionally raising much needed financial resources from IFIs or financial institutions and state development funds in Asia or the Middle East, predominantly China, South Korea and oil rich Arab countries. Both before and throughout the world financial crisis participation of the private sector in infrastructure development remained very limited. The Government of Uzbekistan is keen to see domestic banks and financial institutions play a more prominent role in propelling the economy towards the targeted objectives. Project finance is increasingly becoming a popular instrument of implementing large strategic investment projects across different government priorities. The project finance niche in Uzbekistan is steadily growing larger, albeit still at a slow pace given competing priorities and restricted access to resources.

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

Uzbekistan is rich in minerals, in particular gas and precious metals. The oil and gas sector, as well as related processing industries, has been for years the main area for project finance in Uzbekistan. This trend is likely to persist in the future. Over the 2008-2011 period, Uzbekistan has attracted and continues to benefit from major oil and gas industry investments, including, among others, the US\$2bn Uzbekistan-China Gas Pipeline Project, the US\$2bn Gas-To-Liquid (GTL) Plant Project and the US\$4bn Uzbek-Korean Surgil Natural Gas Chemicals Project. The China-Uzbekistan deal includes over US\$2bn investment in the form of loans to build the Uzbek section of a dual China-Turkmenistan natural gas pipeline to bring much needed energy supplies from Central Asia to the Western Chinese province of Xinjiang. Alongside the existing China-Turkmenistan pipeline project, Uzbekistan has secured a project financing from Chinese banks which will be used partly to develop Uzbekistan's own gas production and transportation capacity. The Uzbek-

Korean investment project in the Karakalpakstan region is backed by the ADB political risk guarantee and financing from Export Import Bank of Korea, Korea Trade Insurance Corporation, China Development Bank, National Bank of Uzbekistan, European export credit agencies and international commercial lenders. The GTL project, bringing together the South African energy and chemical group, Sasol, the Malaysian Petronas and Uzbek state corporation Uzbekneftgaz, marked a new era in developing Uzbekistan's domestic capacity to convert natural gas into transport fuel.

In addition to oil and gas, other project financings have taken place in the telecommunications, textile and energy sectors.

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?

Uzbekistan's basic laws governing the creation and application of the different types of security interest include the Civil Code of the Republic of Uzbekistan, made effective as of 1 March 1997 (the "Civil Code"), the Law of the Republic of Uzbekistan On Pledge, dated 1 May 1998, as amended (the "Law On Pledge"), and the Law of the Republic of Uzbekistan On Mortgage, dated 4 October 2006 (the "Law On Mortgage"). Under the Uzbek Civil Code, there are generally two types of proprietary security interests: mortgages; and pledges. Accordingly, security agreements are typically clustered together on the basis of the type of a security interest they represent. Preparation of a written instrument granting a lien is a pre-requisite requirement to the creation of each security interest permitted under Uzbek law. Each type of a security interest requires a separate agreement. In a commercial transaction, an agreement governing the creation of a security interest over movable assets must contain a description of the collateral, identification of the grantor and the grantee of collateral, a principal place of business of the parties thereto, type of collateral, pledged item(s) and its value, and the nature, scope and maturity period of the obligation secured by such collateral. The agreement must also clearly identify a party which retains the collateral throughout the life of the agreement.

Under Uzbek law, a security interest granted over immovable property with land rights thereto is subject to a mortgage agreement. The same content requirements as stated above shall apply in respect of a mortgage agreement.

A security interest over a whole enterprise comprising of movable and immovable property and any rights to a claim, as well as exclusive rights, are subject to an enterprise mortgage.

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 Civil Code makes a distinction between moveable and immoveable property. Land parcels, subsoil rights, water rights and everything firmly connected to the land (i.e. other objects which cannot be removed without causing a disproportionate harm to their use such as forests, perennial plantings, buildings and structures, pipelines, aircrafts, etc.), are categorised as immoveable assets. Items which are classified as moveable property are equipment, machinery, money, commercial paper, securities and other intangibles (such as contract rights or other rights).

Under Uzbek law, there is little conceptual difference between a mortgage and pledge. A mortgage is considered a specific type of pledge. As a general principle, a mortgage is a pledge over immoveable assets and a pledge is a security interest over any assets or rights that are not immoveable property.

The collateral package for an Uzbekistan based company typically includes multiple types of collateral comprising real estate, machinery and equipment, as well as any rights against shares held in such company.

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

A security interest over receivables is permitted under Uzbek law. A charge over a bank account on which rent income is generated would be a valid and legally binding security instrument under Uzbek law. The issue arises as to what will be the subject matter of such pledge. The options are as follows: (i) a pledge over receivables entering the bank account; (ii) a pledge over a bank account; or (iii) a pledge over the rights to the bank account. In practice, the above options are almost duplicating in nature. Any bank account or receivables credited to any bank account held in an Uzbek bank may be pledged under Uzbek law. To create a pledge over receivables, a bank account pledge agreement must be entered into by the borrower (as a chargor), a pledge holder (as a chargee) and a servicing bank. The chargor shall be permitted to operate its account(s) or otherwise collect in the receivables in the absence of a default. The terms and conditions of maintaining and operating the accounts charged in favour of the chargee must be agreed and set out in detail in the underlying agreement. Should the transaction structure contemplate several bank accounts to be opened by the borrower with a servicing bank (e.g. revenue receipts account, debt service account, debt service reserve account, etc.), we would recommend that a bank account agreement be entered into between the pledge holder, a servicing bank and the borrower that would outline, *inter alia*, the obligations of a servicing bank in relation to maintaining several bank accounts and operating the proceeds that are paid in. Apart from the pledge of the rent income account, the pledge holder may wish to obtain a pledge over other bank accounts of the borrower (if opened).

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

As outlined in question 2.3 above, a charge over bank accounts is permitted under Uzbek law. There are no special rules addressing the creation and perfection of security interests in receivables or

cash proceeds deposited in bank accounts. In this case, general Uzbek law provisions would apply.

The bank account pledge agreement shall become valid and enforceable from the date of its execution by the parties thereto. No registration or notarisation requirement would apply in respect of a bank account pledge in Uzbekistan. The signatories must be duly authorised to sign the pledge agreement. In Uzbekistan, a signatory representing a company is regarded to be duly authorised if she/he acts on the basis of a charter or a power of attorney. Under Uzbek law, a general manager (for companies, a general director, and for banks, a chairman of the management board) may act without power of attorney on the basis of the articles of association and resolution of the supervisory board or other executive body approving his/her appointment/election. A power of attorney to be issued to the representative of a foreign party must be notarised and legalised by an Uzbekistan consulate in that country (or the nearest consulate responsible for legalisation of documents in that country) to be admissible in Uzbekistan.

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

Securities and rights may also be pledged as collateral provided always that the pledgor is the owner of such securities and rights. A security interest over shares in an Uzbek registered company is created on the basis of a pledge agreement. The perfection requirements applicable to a share pledge agreement vary depending on the type of shares pledged. In Uzbekistan, a limited liability company does not issue shares. In a joint stock company, shares are issued and recorded in electronic form only and not in certificated form. A share in an Uzbek LLC is represented by a participating interest. Under Uzbek law, the only document that confirms the title to a participating interest and rights arising therefrom shall be articles of association of the LLC and its foundation agreement. In a limited liability company, certificates are issued to confirm paid up share capital. However, in reality, issuing certificates in an LLC is a rare practice. There is also no requirement under Uzbek law that an LLC keeps and maintains a register of participating interests. A shareholder entering into a pledge of participating interest agreement would need to secure a prior corporate resolution approving the transaction.

In a transaction contemplated in respect of shares in a joint stock company, the underlying pledge agreement would be subject to certification with a Notary Public and registration with the shares depositary (custodian). No notarisation and registration requirement would apply in respect of shares (participating interest) pledged in an Uzbek registered limited liability company.

There is no unified register of lien created over shares (participating interest) in Uzbekistan. Giving of public notice is not contemplated by Uzbek law. This appears to be a disadvantage for a potential lender since, in the absence of perfection requirements for participating interest in an LLC under Uzbek law, there is a substantial risk that the pledge provider would be able to pledge the same collateral (participating interest) to different pledge holders.

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)?

Under Uzbek law, transactions involving mortgage, pledge of motor

vehicles and shares in a joint stock company are subject to mandatory notarisation and registration requirements. The mandatory registration and notarisation requirement shall not apply in respect of any moveable collateral other than the pledge of vehicles and shares in joint stock company. The notary fee for registering transactions involving a pledge (mortgage) of assets is 0.1% of the amount specified in the underlying agreement as the value of a pledged (mortgaged) item. The registration fees applied by the registering authority (the cadastre, a depository and the State Department of Motor Vehicles) vary from agency to agency. With the exception of notary and registration fees applicable in respect of the above collateral, no other stamp, registration or similar tax or charge is imposed in Uzbekistan in respect of security.

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?

Perfection of a security interest in the context of Uzbekistan law means its registration with the appropriate authorised government agency. In particular, immovables mortgage agreements and share pledge agreements are subject to registration with the cadastre (for buildings and construction) and the relevant depository (where pledged shares are held), respectively. Furthermore, immovable mortgage agreements and moveables pledge agreements (for vehicles and shares in a joint stock company), as well as agreements for pledging certain rights to a property as a security for performance of obligations thereunder, are subject to notary certification. The mandatory registration or notarisation requirements shall not apply in respect of any moveable collateral other than the pledge of vehicles (any motor vehicles, trailers) and shares in a joint stock company which are registered with the State Department of Motor Vehicles and relevant depository respectively. Similarly, no registration and/or notarisation requirement shall apply in respect of receivables and a bank account charge in Uzbekistan.

Execution of relevant security in the presence of a notary public shall be subject to review by such notary public of the following documents supplied in certified copies:

- company deeds (charter, foundation agreement, if applicable); evidence of due incorporation of the company pursuant to the laws of its jurisdiction of incorporation;
- minutes of the general meeting of shareholders (for joint stock companies) or general meeting of participants (for limited liability companies) or any other executive supervisory board authorising: (i) the transaction; (ii) execution of relevant security documents by representatives of the company duly authorised to execute relevant security documents on behalf of the company; or (iii) filing duly executed relevant security documents with the appropriate registering authority by duly authorised company representatives;
- an instrument pursuant to which the company undertakes to perform the obligations to be secured by the collateral;
- title documents confirming the title to the collateral;
- in respect of the mortgaged assets, a certificate from the cadastre certifying that the collateral is not pledged and is free from any encumbrances (issued in standard approved form and valid for one month from the date of issue);
- evidence of payment of applicable notary fees; and
- passports of the authorised representatives signing on behalf of the parties.

Formalities relating to notarisation and creation of a lien over pledged (mortgaged) property with the appropriate registering authority typically take up to two working days to complete.

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.?

In general, no governmental or regulatory consents are required for granting a mortgage or pledge, except for the mortgage of state-owned immovable property. If the latter is the case, a resolution of the Cabinet of Ministers would be required to authorise the creation of security.

Land in Uzbekistan is property of the state. Mortgage of immovable property is not permitted under the Law On Mortgage unless otherwise accompanied by transfer under the same mortgage of the title to land including leasehold rights thereto. Where immovable property over which a mortgage is created includes land under lease, the consent of the appropriate local authority would be required unless otherwise specified in the lease agreement.

3 Security Trustee

3.1 Regardless of whether Uzbekistan 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?

Only project lenders in their capacity as pledgees are permitted to act as holders of security under Uzbek law. Agents or trustees are generally engaged for the purpose of facilitating transactions with purely technical functions.

3.2 If a security trust is not recognised in Uzbekistan, 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?

A parallel debt or joint and several creditors status are not concepts recognised in Uzbek project finance transactions. Under security arrangements among the parties, title to assets which are being pledged to a lender remains with the debtor. Enforcement of claims is performed with or without recourse to legal action in court based on security arrangements of the parties in a project finance transaction.

Whichever provision the parties agree upon, the subject matter of a pledge may only be sold through a public auction. Uzbek law, therefore, does not contemplate the transfer of ownership rights in relation to the pledged property upon a default as is the case in western jurisdictions. Rather, the discharge of a secured obligation is made from the proceeds of the pledged property sold through such a public auction. Public auctions are time-consuming and it may take months for a payment to reach the beneficiary. In addition, Uzbek court has the right, at the pledge provider's request, to suspend the sale of the pledged property for a period of up to 12 months.

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?

Under Uzbek law, security can be enforced in the event of failure to perform or improper performance by the pledge provider or the borrower (if the borrower and pledge provider are not the same person) of the secured obligation. An Uzbek court may refuse to enforce a pledge if it determines that the non-performance is ‘extremely insignificant’ and the pledge holder’s claim is ‘manifestly disproportionate’ to the value of the pledged property.

The enforcement procedure for mortgages (charges over immovables) is different from that of pledges (charges over moveables or other collateral). However, there are basic principles governing enforcement procedures which are universally applicable to both types of collateral.

Enforcement claims in respect of pledges are typically made through judicial proceedings involving an Uzbek court, unless expressly excluded in an agreement between the pledge holder and the pledge provider (separate and in addition to the basic pledge agreement). As a rule, this agreement does not have to be notarised and may be entered into at any time, including any time before non-performance of the secured obligation has occurred. Enforcement provisions can be set out in the original pledge agreement. Both the pledge agreement and any subsequent enforcement agreement can provide that the pledge holder has the right to enforce the pledge at its own discretion, in certain circumstances. Usually, either failure to perform or improper performance of the secured obligation triggers a foreclosure process.

As mentioned in question 3.2 above, enforcement of security is performed through public sale. No private sale or transfer of security collateral is contemplated under Uzbek law. This can be rather cumbersome and time consuming. The sale of pledged collateral outside Uzbekistan is permitted under Uzbek law provided this provision is agreed by the parties in the original pledge agreement or any further agreement to be completed between the parties after an event of default.

The parties are strongly recommended to use out-of-court remedies in the event of a default. The most notable out-of-court remedies are enforcement agreements. Set-off and novation, among others, are the means of discharging the original obligation under the Civil Code.

We note that a new law of the Republic of Uzbekistan was signed off on the 29th of August 2010 tightening up on the legislative environment governing the use of a pledge in Uzbekistan. The law provides for the respective amendments to the Civil Code, the Law of The Republic of Uzbekistan “On Enforcement of Judicial Acts and Acts of Other Bodies” and to the Law On Mortgage. The amended laws became effective as of 23 September 2010.

In accordance with the amended Civil Code, if a court ruling is in place in respect of pledged property under an enforcement procedure or as a result of actions brought by state authorities, pledge holders are now entitled to call for acceleration by the pledgor of a secured obligation, upon failure to perform which, the pledge holder shall have the right to proceed with a claim against the subject of a pledge. Failure by the pledge holder to exercise its right to call for acceleration shall result in termination of a pledge, other than in cases where pledged assets have not been sold from

public auction and unsecured creditors waived their right of claim against the borrower.

Pursuant to the amended Law of The Republic of Uzbekistan “On Enforcement of Judicial Acts and Acts of Other Bodies” voluntary compliance under an enforcement proceeding instituted on the basis of a court ruling ordering payment of a fine shall now be limited to six months. Also revised under the above amended law were the procedures for enforcement and ranking of the security interest.

The Law On Mortgage details legal ramifications of enforcing the creditors’ right upon enforcement orders issued by court and state authorities.

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

No specific restrictions apply to foreign investors or creditors.

5 Bankruptcy 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?

As a consequence of the creation of a security, upon insolvency of the project company, the project lender shall be regarded as a secured creditor and shall be a third-tier creditor in the waterfall of creditors under the Law of the Republic of Uzbekistan on Bankruptcy.

The waterfall of creditors upon insolvency may be summarised as follows:

- court expenses, the remuneration of the liquidator, current utility payments, claims arising from the obligations assumed in the process of liquidation are always paid before creditors;
- first tier – taxes and other mandatory payments to the budget, wages and tort claims (negligence);
- second tier – payments that are due in connection with mandatory insurance and mandatory insured local bank loans (retails depositors loans);
- third tier – payments that are due to secured creditors (secured either by a pledge or by a mortgage);
- fourth tier – payments that are due to unsecured creditors;
- fifth tier – payments that are due to shareholders, participants or founders of the bankrupt entity; and
- sixth tier – all other payments.

The claims of secured creditors may be satisfied only at the expense of proceeds received from the sale of all pledged property within the bankruptcy proceedings. To obtain these proceeds, the liquidator must first sell the secured assets as well as the unsecured assets of a bankrupt entity, and then distribute the proceeds of secured assets to secured creditors, and the proceeds from unsecured assets to unsecured creditors. Secured creditors are treated as one class with no distinct priority between such creditors on the basis of the property pledged to each. The distribution within the classes of creditors is to be made on a proportionate basis. This risk of proportionate satisfaction of claims of secured creditors under Uzbek laws shall be mitigated by the negative pledge covenant under a facility agreement.

The claims of secured creditors as a class shall not be subject to the obligatory six tiers of claims (as specified above) that must be satisfied from the proceeds of sale of the bankruptcy estate. Rather, the claims of the class of secured creditors shall be satisfied from

the pledged property separately from and without regard to the other unsecured creditors, even those with a higher priority (e.g., creditors of first and second tiers). This is the one advantage which the secured creditors may enjoy under Uzbek laws in the event of the pledgor's insolvency.

In the meantime, if the proceeds are not sufficient to satisfy in full the claims of all secured creditors, the outstanding claims of any of such secured creditors shall be regarded the claims of the fourth tier (unsecured creditors) and shall be paid from the bankruptcy estate remaining after the satisfaction of the claims of two preceding tiers (without regard of the third tier).

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?

There is no express or hidden provision under Uzbek law that gives preference to local banks as unsecured creditors over foreign banks, provided that an Uzbek court or state authorities of the Republic of Uzbekistan fail to interpret otherwise the provisions of Decree No. UP-3047 issued by the president of the Republic of Uzbekistan on 30 March 2003 and Decree No. PP-56 issued by the president of the Republic of Uzbekistan on 15 April 2005 (the Decrees). Under the Decrees, an Uzbek bank is entitled to foreclose on the liquid assets of an Uzbek resident should an event of default occur under the loan agreement between such Uzbek bank (as lender) and an Uzbek resident (as borrower). Our interpretation of the Decrees is that the secured property of the Uzbek resident, if any, shall fall outside the scope of such liquid assets and, therefore, notwithstanding the provisions of the Decrees, Uzbek banks (as lenders) shall not be entitled to foreclose on the property that has been already secured in favour of foreign banks or other secured parties by the time of such foreclosure. The secured property shall be ring-fenced from the claims of any third parties by the Law On Pledge and the Civil Code. The latter have superior legal power over the Decrees in the hierarchy of Uzbek laws and regulatory acts. We therefore refer to the provisions of superior regulatory acts (the Civil Code and the Law On Pledge) when opining on the validity and enforceability of the security created in lenders' favour. To the best of our knowledge, there are no reported cases in which this question has been considered before the courts in the Republic of Uzbekistan.

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

Please refer to question 5.2 above for discussion.

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?

There are no out-of-court processes available to the creditors as insolvency procedures once commenced are subject to judicial control.

6 Foreign Investment and Ownership Restrictions

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

The treatment of investment projects, or to this end of a project

company, varies depending on the applicable investment regime. For some projects (typically involving investments of US\$20 million or above), a preliminary decree of the Cabinet of Ministers would be required setting out preferential terms and conditions including tax concessions. To proceed smoothly, a project must be negotiated with the government from the very beginning. During negotiations, a specific regime may be discussed if the project involves large amounts of investment and will promote local production and employment. To commence the operations, certain licences, permits or governmental approval or other authorisations may be required.

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

Bilateral treaties with most western and a number of key Asian jurisdictions are in place for mutual protection of foreign investments.

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

The key laws regarding the nationalisation or expropriation of project companies and assets include the Civil Code and the Law on Foreign Investments, as well as international bilateral and multilateral treaties on mutual protection of foreign investments.

Although private ownership is protected by the Constitution, no particular forms of investment are specially protected from nationalisation and expropriation under Uzbek law. Certain strategic projects and/or companies are given preferential status and tax and customs concessions on the basis of special government decrees.

7 Government Approvals/Restrictions

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

Overall coordination of strategic project sectors such as oil and gas, mineral extraction and power generation is performed routinely by the Cabinet of Ministers. Any projects in strategic sectors are approved at the level of the government. Priority investment projects are granted specific tax concessions and privileges on the basis of a presidential decree. A presidential decree sets out important parameters and deliverables of the project, appoints government agencies responsible for overseeing the project, and extends specific privileges to project partners (project companies or individual investors including but not limited to financial institutions).

The project monitoring and facilitation functions are assigned to the government agencies (ministries, committees, departments, agencies and associations) in the field to perform project oversight. These agencies are typically the issuing authority for licences and permits.

Any projects involving privatisation of state-owned assets or transactions contemplating the transfer of facilities in which the government is a stakeholder require explicit permission of the State Committee of the *Republic of Uzbekistan for State Property Management (GKI)*.

Monitoring and compliance with environmental standards, issuance of special water use and air emission permits, mandatory environmental impact assessments and enforcement of environmental requirements fall within the remit of the *State Committee of the Republic of Uzbekistan for Nature Protection*.

Antitrust clearance and general compliance with anti-monopoly legislation are dealt with by the *State Committee of the Republic of Uzbekistan for Demonopolisation and Development of Competition*.

The *State Committee of the Republic of Uzbekistan for Geology and Mineral Resources* is the licensing authority for granting subsoil use rights (mineral extraction or cement manufacturing projects).

Sanoatgeokontekhnazorat is the government agency responsible for ensuring safety standards in the manufacturing industry, mining and the utility sectors and for licensing mining works.

Uzbekneftgaz, the state oil and gas holding entity, is the main partner and coordinator for oil and gas sector projects on behalf of the government in Uzbekistan.

The *Central Bank of Uzbekistan (CBU)* is the regulatory and licensing authority in the banking and financial sector. It issues licences to commercial banks (including for foreign currency operations), credit and microcredit institutions and pawnshops, acts as the registering authority for cross-border lending transactions, and issues approvals to resident companies for opening offshore accounts. CBU approval is required for opening offshore accounts, purchase of shares in Uzbek banks by foreign banking/investment institutions, establishment of representative offices of foreign banks and opening foreign banks.

The *Uzbek Agency for Communications and Information* acts as a coordinating hub for projects and the licensing authority in the telecommunications sector.

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?

All the financing or project documents must be translated into the Russian/Uzbek language if they were originally prepared and negotiated in another language (e.g. English). It is not strictly required that this translation be notarised, except where such documents are filed with relevant authorities e.g. the CBU requires that the Russian/Uzbek translation of the relevant facility agreement (or other similar financing agreement) be notarised for filing purposes.

An investment agreement must be filed with the Ministry of Foreign Economic Relations and Investment Trade and becomes legally effective upon its approval by the resolution of the President/Cabinet of Ministers of Uzbekistan.

A facility agreement or similar financing instrument (e.g. foreign lease agreement) must be registered by the CBU. No draw-down payments under the facility are allowed to be made unless the underlying agreement is duly registered with the CBU.

In a typical investment project, a feasibility study would be required. Once prepared, it must be duly filed and approved by the relevant Uzbek government department. It would not be regarded effective unless approved by a resolution of the President/Cabinet of Ministers.

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)?

Ownership of assets alone would not typically trigger a licence

requirement under Uzbek law. However, the operation of certain assets e.g. natural resources, pipeline, telecommunications equipment, etc., is subject to a licence. A foreign entity operating through its Uzbek subsidiary or by virtue of a shareholding in an Uzbek registered company would be allowed to hold such a licence. Operations in key commercial areas including but not limited to mining, subsoil use, extraction and processing of minerals, telecommunications, pharmaceuticals, whole sale trade, etc. are subject to a licence. The exhaustive list of licensing operations in Uzbekistan is approved by the Oliy Majlis, the lower house of Uzbek parliament, pursuant to its Resolution No.222-II issued on 12 May 2001.

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

Tax on royalties exists when a domestic or foreign party extracts natural resources in Uzbekistan. There is distinction in defining the tax base for the royalty tax depending on the entity paying tax, i.e. a domestic entity, or a foreign entity with or without a permanent establishment.

In relation to a foreign entity without a permanent establishment in Uzbekistan, the current rate of royalty tax is 20%. This is a profit-based tax.

In relation to a domestic entity or foreign entity extracting natural resources in Uzbekistan, the following taxes shall apply:

- tax on subsoil use;
- tax on extra profit (not applicable to foreign companies acting on the basis of a product-sharing agreement); and
- bonus (fixed or relating to each commercial discovery).

The above taxes are based on the amount of natural resources extracted or processed in anyone fiscal year. The tax rates applicable to each type of taxable operations is subject to annual review by the government. The list of processed products is established by the Cabinet of Ministers.

Export of natural resources is subject to the following taxes:

- VAT at 0% (except for precious metals); VAT for precious metals is established by the Cabinet of Ministers; and
- excise tax – the rate varies depending on the type of natural resources.

Other restrictions on the export of natural resources include prior approvals of the state authority or prior registration of an export contract with the state registration authority. For instance, an export contract for supply of gold, crude oil, uranium or natural gas from Uzbekistan shall be subject to registration with the Ministry of Foreign Economic Relations, Investments and Trade.

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

The main foreign exchange control restrictions in Uzbekistan that are applicable to foreign currency transactions (export-import, foreign loans, derivatives, foreign lease operations, etc.) are set out below:

- all export proceeds received by an Uzbek counterparty must be credited to its Uzbek bank account unless there is a express permission of the CBU allowing an Uzbek company to open and maintain an offshore account; failure to ensure this requirement shall result in the application of financial and penal sanctions;
- all export proceeds must be credited to an Uzbek account of an Uzbek counterparty not later than 60 days after the dispatch of goods for export. Unless specific permission of the CBU is obtained, sanctions will apply if the above rule is

not complied with. This rule will apply to the export of goods only and, accordingly, will not be relevant to non-physically settled transactions;

- goods must be imported to Uzbekistan within, at latest, 180 days from the date when the payment under the import contract was made. This rule will apply to the import of goods only;
- any export receivables in foreign currency are subject to a mandatory statutory requirement whereby 50% of such export proceeds must be converted into local currency;
- no assignment under export contracts is permitted under applicable Uzbek foreign exchange rules;
- no offshore account payment is allowed to be made from Uzbekistan by an Uzbek counterparty unless CBU permission to do so is obtained; and
- capital transactions (foreign loans, deferred import contracts, leasing operations) shall be subject to prior registration with the CBU if their maturity period exceeds 360 calendar days.

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?

There are no restrictions preventing a foreign shareholder from receiving and repatriating dividends. Return of capital is also possible provided that a valid legal basis exists. The legal basis includes: (i) exit by a foreign shareholder from a resident company via a sale of its stake to another party; (ii) withdrawal of a foreign shareholder by selling its stake to the resident company (redemption of shares by the issuer of these shares) - this option is limited to open joint stock companies to certain cases only; no limitations apply in respect of limited liability companies where any shareholder may exit at any time; or (iii) as a result of liquidation of the resident Uzbek company. Under scenario (i), the rule applies if the stake at question amounts to 35% plus one share of the resident company's charter fund. No threshold, however, exists for buying a stake in an Uzbek bank by a foreign participant. A prior anti-trust clearance would be required to enter into a sale and purchase agreement. A shareholder would not be entitled to sell a stake and withdraw from the resident company unless the purchaser of such stake obtains the required anti-trust clearance. No fee is applicable in respect of anti-trust clearance.

In respect of control and regulation applicable to the remittance of capital, we further note that in case (ii), the ability of a shareholder to exit an Uzbek joint stock company and ask this company to redeem its shares is limited to several cases only. These cases include, *inter alia*, a situation when a shareholder refuses to vote for a certain item on the agenda at the shareholders' meeting but a corporate resolution on such agenda item is still adopted. Such shareholder may claim that his right has been violated by this resolution and may ask the company to redeem his shares within the limited period of time. With the lapse of this period, the shareholder would be deprived of the right to claim redemption of his shares by the company. No such limitations are applicable to limited liability companies.

Another control applicable to the withdrawal of capital relates to the manner of calculation of the amount of capital withdrawn in cases (ii) and (iii) above. Redemption of a participating interest in a limited liability company shall be based on the latest balance sheet value. No fair or market value shall be applicable for this. Therefore, the right of an exiting foreign participant to demand the payment of fair value or market price for his stake is limited by law.

There are no restrictions that would prevent a resident company from making payments of principal, interest or premiums on loans

or on bonds (issued by an Uzbek joint stock company) to parties in other jurisdictions (all collectively referred to herein as "payments"). The payments with respect to loans will be transferred by an Uzbek authorised bank (where the resident company holds a foreign currency account) to the non-resident bank provided that a loan is registered with the CBU. The amount of annual interest payable under a loan agreement should not exceed 20% at the risk of investigation under Uzbek anti-money-laundering and transaction-monitoring rules. The payments with respect to domestically issued bonds will be transferred to the non-resident payee provided that these bonds are duly registered by the Uzbek authorised agency. Any payments shall be made from hard currency funds accumulated on the resident company's local bank account from export proceeds or other 'own sources of currency receipts', otherwise the resident company will have to apply for a contingent and sustainable conversion procedure. In practice, conversion of local currency into a foreign currency is fraught with frequent delays owing to limited access of local commercial banks to foreign exchange reserves. There are no restrictions in Uzbek laws for the transfer outside Uzbekistan to a non-resident bank of hard currency proceeds directly from the resident company's foreign currency account so that to discharge its obligations for interest and principal payments under the loan agreement. However, any transfers to an account located in an offshore jurisdiction triggers the special financial screening procedure mentioned above. There are no restrictions under Uzbek law as to the payment of interest at the expense of borrowed money.

From a tax perspective interest or premiums on loans, as well as any other fees and commissions, penalties and/or default interests, payable in connection with a loan or bonds (issued by Uzbek joint stock companies) shall be considered an income and subject to a withholding tax at the rate of 20% payable at payment source, i.e. by the resident company by virtue of deduction unless otherwise provided for in a bilateral double tax treaty entered into with the country of the non-resident bank.

From a tax perspective, dividends or interest (on participating interest in an Uzbek LLC), as well as income generated from the sale of capital, shall be subject to the Uzbek withholding tax. In relation to dividends and interest, 10% withholding tax shall apply. In relation to income generated from the sale or withdrawal of the capital - 20%. In the latter case, income would be only considered generated if there is a positive difference between the sale price of capital and its original price (specified in the constituent documents).

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

Project companies are entitled to open and maintain onshore foreign currency accounts. Under Uzbek foreign exchange control, Uzbek companies are not allowed to open offshore accounts in other jurisdictions unless expressly permitted by the CBU. The process for obtaining such approval is time consuming and requires top level government support. As a rule, only strategic investment projects are granted such governmental approvals.

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 Uzbekistan or abroad?

Please refer to question 7.6 for certain aspects of dividend

payments. With respect to dividends, there is no maximum or minimum threshold established by Uzbek law for repatriation of dividends. Dividends may be paid annually, semi-annually and on a quarterly basis subject to satisfactory financial performance of the resident company. Any distribution of dividends on a monthly basis is not permitted except as otherwise provided by shareholders in the articles of association of an Uzbek borrower. Payment of dividends, however, is subject to certain restrictions; dividends cannot be distributed unless charter capital is paid-up in full by shareholders. No dividends are payable in the event of an insolvency proceeding in respect of an Uzbek borrower (or if it is expected that it would face insolvency as a result of dividend distribution) or if the net assets of an Uzbek borrower become less than its charter capital (and reserve fund).

Dividends are not distributed and allowed for repatriation until all taxes due and payable by the borrower are paid in full. Any payment of dividends by the resident company to a foreign shareholder are subject to special financial monitoring scrutiny procedure by the tax authorities. Taxation of dividends shall be made at two levels, corporate and individual. At the corporate level, the profit of the resident company shall be subject to income tax and all other applicable taxes. When all taxes at corporate level are paid by the resident company, the net profit shall constitute the dividends of a foreign participant (shareholder). Such dividends shall be subject to withholding tax in Uzbekistan payable at payment source (i.e. subject to withholding obligations of the resident company) at 10%, unless otherwise provided for in a bilateral double tax 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?

Uzbek companies are subject to key environmental, health and safety laws and regulations, e.g.: the Law On Industrial Safety On Hazardous Manufacturing Objects, dated 26 September 2006; and the Law On Labour Protection, dated 6 May 1993. In the oil and gas sectors: the Unified Rules On Safety Systems In Oil and Gas Sector, as of 2001, developed by Uzbekneftegas (UNG) and approved by the Works Safety Inspection; and the Instruction On Prevention Of Wild Flowing During The Construction, Exploitation And Capital Maintenance Of Oil And Gas Wells, approved by the UNG.

In the mining sector, the following laws and regulations are applicable: the Rules On Safety On Use Of Mining Vehicles, as registered by the Ministry of Justice No. 1579, dated 7 June 2006; the Rules On Safety On Tailing Works, as registered by the Ministry of Justice No. 1577, dated 31 May 2006; and the Rules On Safety On Crushing, Sorting, Concentration and Agglomeration of Ore And Concentrates, as registered by the Ministry of Justice No. 1575, dated 23 May 2006.

The following are the public authorities of the Republic of Uzbekistan responsible for developing and amending the Investment Programme of the Republic of Uzbekistan:

- *Sanoatgeokontekhnazorat* – regulatory authority on industrial safety matters;
- Ministry of Labour and Social Protection – regulatory authority in respect of industry labour standards;
- Ministry of Health – regulatory authority in respect of health and sanitary standards;
- Oil and Gas Inspection – regulatory and controlling authority at the Cabinet of Ministers; and
- UNG – state oil and gas holding company, develops technical and industrial standards, policies and requirements.

Any investment projects are subject to prior environmental approvals by the State Committee of the Republic of Uzbekistan for Nature Protection (the “Nature Protection Committee”). Under Uzbek environmental laws, the Nature Protection Committee is a competent state authority with powers to monitor environmental compliance. Investment projects involving construction or any other type of physical infrastructure development or likely to cause any impact on the environment are subject to mandatory requirement for prior environmental screening (Russian: *Gosudarstvennaya ekologicheskaya ekspertiza*) (the “Environmental Impact Assessment” or “EIA”). The process of obtaining EIA approval from the Nature Protection Committee for individual projects is divided into three phases. Under phase I, before any project-related works are cleared for financing, the applicants are required to submit a draft environmental statement (the “Phase I”). Following approval of the draft under Phase I and prior to approval of the feasibility study, the applicants would be required to proceed with the environmental impact statement (the “Phase II”). At the final stage and prior to commencement of any project-related works, the applicants are required to obtain approval for a statement of environmental effects (the “Phase III”). No financing is allowed under any projects unless relevant EIA approval has been obtained.

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

Public procurement is subject to a specific regulatory framework in Uzbekistan. Procurement by project companies where procurement involves financing arranged by private funds or through lending institutions from abroad and not guaranteed by the state in Uzbekistan is subject to general commercial rules and procurement practices. In this case a “freedom of contract” principle will govern procurement mechanics under relevant contractual arrangements.

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?

Only Uzbek-licensed insurance companies are allowed to insure risks in Uzbekistan. Once insured with an Uzbek insurance company, these risks may be reinsured by a foreign insurance company. Reinsurance is customarily required by foreign investors under major project finance projects.

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

It is a standard practice permitted by Uzbek law that foreign (secured) creditors are appointed loss payees under insurance policies over project assets.

9 Foreign Employee Restrictions

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

Any foreign workers (without distinction between different categories) seeking employment in Uzbekistan must obtain work permits prior to starting their assignment. Applications are

submitted by employers on a standard form and are reviewed by the Ministry of Labour and Social Protection (Labour Ministry) within 30 calendar days. Work permits are issued for a period of a maximum of one year and may be renewed if necessary upon application from the employer. In addition, Uzbek law requires that employers bringing in foreign workers must possess a valid licence for engaging foreign labour, which is issued by the Labour Ministry. Any foreign nationals residing in Uzbekistan must register with the immigration service either directly or through the Diplomatic Service Department of the Ministry of Foreign Affairs. Failure to ensure compliance may result in deportation of the employee and sanctions against the employer.

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?

There are standard customs and security rules that apply for any equipment due for importation to Uzbekistan. In certain cases, where special-purpose equipment (arms, explosives, drugs, etc.) is entering Uzbekistan, prior entry clearance must be obtained from a relevant government agency or the Cabinet of Ministers. Any equipment entering Uzbekistan under an import contract must have a valid passport of import transaction issued by a servicing bank of the resident company. Import contracts must be registered with the customs service and a servicing bank of the resident company. No fees are charged for registering equipment with the customs and servicing bank other than customs declaration fees. Customs duties and excise tax applicable to each type of imported equipment vary depending on the purpose and origin of equipment.

Certain types of machinery and equipment are exempt from customs duties and VAT under the “List of imported technological equipment and spare parts exempt from customs duties and VAT”, which was approved by the joint Resolution of Ministry of Economy, Ministry of Finance, State Customs Committee and Ministry of Foreign Economic Relations, Investment and Trade of the Republic of Uzbekistan No.1802 (registered with the Ministry of Justice on 3 March 2008). If a commodity of the transaction falls within one of the categories under this List, then its importation into Uzbekistan will be exempt from customs duties and VAT.

Customs duties are also waived in relation to imported machinery if a project company is enrolled in a state localisation programme. Further tax and customs concessions may be applicable in respect of imported equipment if a special treatment regime is agreed by or under international commitments of the Government of Uzbekistan.

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

The importation to Uzbekistan of equipment, spare parts, components and raw materials may be implemented using one of the sixteen available customs regimes. However only the “free circulation” customs regime allows the use of equipment and goods in Uzbekistan with no restrictions.

The following customs payments are charged if the commodity is imported under the “free circulation” regime:

- customs duties (rates vary from 5% to 40%);
- excise tax (rates vary from 5% to 200%);
- import VAT (at the rate of 20%); and
- customs clearance fee (at the rate of 0.2%).

Uzbekistan has signed trade agreements with certain “favoured” countries. The list of favoured nations includes 45 countries. The commodity that originate from countries other than the “favoured” nation countries are subject to a double customs duties rate.

The goods that originate from the countries with which Uzbekistan had concluded the free trade agreements are exempt from the customs duties. These countries include the countries within the Commonwealth of Independent States (CIS), except for Turkmenistan. Although Georgia is not part of the CIS it is, however, a party to the free trade agreement.

Uzbek legislation allows certain exemptions in respect of the import of specific goods. Special equipment and its components and spare parts could also be imported with the following benefits: exemption from the customs duties and import VAT.

In order to qualify for the above benefits, the equipment should be included in the official list of the equipment which is recognised by the Uzbek statutory authorities as “technological”. The components and spare parts should be specifically included in the same purchase agreement as the technological equipment in order to qualify for these benefits.

11 Force Majeure

11.1 Are force majeure exclusions available and enforceable?

Force Majeure exclusions are enforceable under Uzbek laws.

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?

Uzbekistan has ratified a number of bilateral and international treaties against corruption and anti-money laundering, including the 2003 New York Convention Against Corruption and the 1999 United Nations International Convention for the Suppression of the Financing of Terrorism (Terrorist Financing Convention). In addition, Uzbekistan has adopted laws targeting the financing of terrorism and money laundering, in particular the Anti-Money Laundering and Financing of Terrorism Law effective as of 1 January 2006 (the “AML Law”). In accordance with the AML Law, monitoring and preventive efforts targeting prohibitive practices are arranged at three levels: (i) monitoring at the level of a designated government authority; (ii) internal control exercised by legal entities; and (iii) operations involving banking and financial institutions. Prohibitive and suspicious practices as defined in the AML Law and other related legislation are subject to mandatory reporting at all three levels as appropriate.

The applicable civil and criminal penalties include sanctions against both the corporate entities and officers found in breach of the AML rules. The applicable sanctions include up to ten (10) years of imprisonment for individuals and the confiscation of the instrument of crime in respect of the corporate entities.

13 Applicable Law

13.1 What law typically governs project agreements?

Although the application of Uzbek law is mandatory in certain types of transactions (e.g. transactions between Uzbek legal entities

or between an Uzbek legal entity and a foreign investor in relation to a lease or mortgages over Uzbek real estate registered with the Uzbek immovables cadastre), the choice of foreign law by an Uzbek legal entity in other contracts with a foreign counterparty should be recognised and given effect to by the Uzbek courts unless the consequences of the application of foreign law contravene Uzbek public order. Therefore, there is no particular need for a project agreement to be governed by local law in order that such agreement be valid and enforceable in the context of Uzbek laws.

When foreign law is the choice of governing law, the mandatory provisions under Uzbek law in respect of methods and procedure involving performance of the agreement, shall still apply. Hence for a project agreement to be enforceable by an Uzbek court, it must be valid under Uzbek law even though the governing law is foreign law. The foreign law shall be used by the Uzbek court to interpret provisions of the project agreement with regard to the rights and obligations of the parties, as well as to the consequences of non-performance or undue performance of the obligations. However, the enforcement procedures shall be performed in accordance with Uzbek law, should the agreement be enforced locally.

If a court judgment is obtained outside Uzbekistan, it will still need to be enforced in Uzbekistan. To do so, recognition of the judgment in Uzbekistan would be required. However, Uzbekistan is not a party to treaties on the reciprocal enforcement of judgments with most jurisdictions normally used to international financing documents (such as the United States and the United Kingdom) and thus foreign judgments will not be enforced automatically in Uzbekistan. To this end, a re-hearing of the foreign judgment in an Uzbek court will be necessary to enforce the ruling obtained in a foreign court.

13.2 What law typically governs financing agreements?

English law is typically a choice of foreign law in cross-border transactions. Under Uzbek law, this choice of foreign law for financing agreements is acceptable (except for security transactions involving Uzbek based real estate). However, the mandatory rules of foreign exchange, bankruptcy rules, etc., remain applicable.

13.3 What matters are typically governed by domestic law?

Collateral documents are required by law to be governed by the laws of Uzbekistan.

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 Republic of Uzbekistan is not a party to any multilateral or bilateral treaties with any Western jurisdiction or the United States for the mutual enforcement of court judgments. Consequently, should a judgment be obtained from a court in any Western jurisdiction or the United States, it is highly unlikely to be given direct effect in Uzbek courts.

In accordance with article 79 of the Uzbek Civil Code, the state (represented by the government) takes part in relationships regulated by civil legislation on an equal basis with other participants and is liable for its undertakings with its own property. The Uzbek Civil Code is therefore clear that if the government

enters into a commercial activity, it loses special treatment or sovereign immunity. It is widespread practice in Uzbekistan when dealing with the government directly that the government, as a public person, waives its sovereign immunity. From our experience of direct contracts with the government, whether investment agreements or PSAs, the waiver of sovereign immunity was not an issue. It is quite natural for a foreign investor to request the government of a host country to waive immunity as, otherwise, the governmental concessions and privileges granted to an investor may appear revocable at any time by a public act.

15 International Arbitration

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

The Republic of Uzbekistan is a party to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Accordingly, a foreign arbitral award obtained in a state which is party to that convention should be recognised and enforced by an Uzbek court, subject to the qualifications in the UN Convention and compliance with Uzbek civil procedure and the procedures established by Uzbek laws on commercial arbitration for the enforcement of arbitration decisions. We note, however, that, in practice, reliance upon international treaties may require that relevant Uzbek officials be supplied with more information as to the effect and procedures under the treaty, which may not be entirely consistent with the legislation relating to procedure or with court rules. This could delay enforcement procedures in Uzbekistan.

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

Yes, please refer to question 15.1 above.

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

Disputes relating to administrative, family and employment relations are not arbitrable under Uzbek law.

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

There are no types of disputes that are mandatory to domestic arbitration proceedings.

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?

To the best of our knowledge, there have been no calls for political risk protection in our practice.

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?

Under Uzbek law, withholding tax at the rate of 10% from an interest payable on loans made to domestic or foreign lenders is deducted at source of payment. The withholding tax is applicable unless otherwise specified in a bilateral double tax treaty with the foreign lenders' country of residence. The proceeds of a claim under a guarantee or the proceeds of enforcing security shall apply to the extent they involve any amounts of interest.

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?

There are no general tax incentives applicable to foreign investors or creditors. Specific tax incentives may be granted by the government under certain project on the basis of a resolution of the President/Government of Uzbekistan and an investment agreement entered between the specific investor and the Uzbek government.

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By way of explanation, an investment agreement is one of the two legal instruments designed to grant tax, customs, payments and other exemptions and waivers additionally to those existing under the general legal framework. We note that, ideally, additional guarantees and remedies, exemptions and waivers are granted to foreign investors if investing in: (a) *priority development sectors to ensure sustainable economic growth, progressive structural changes in the country's economy;* (b) *prioritised projects ensuring the strengthening and extending of the production and export potential of the republic, its integration into global connections;* or (c) *projects in the sphere of small entrepreneurship whose implementation is directed at the processing of raw materials, production of consumer goods and services, provision of employment for the population.*

This list seems to be exhaustive and does not contain any indication that other projects qualify for the status of investment agreement.

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 Uzbekistan?

There are no other material considerations other than those already mentioned above.

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