

A map of Kazakhstan and its neighboring countries: Russian Federation to the north and east, China to the east, Kyrgyzstan to the south, Uzbekistan to the south, Turkmenistan to the southwest, and Islamic Republic of Iran to the southwest. Major cities in Kazakhstan are labeled: Ural'sk, Aktubinsk, Atyrau, Aktau, Aralsk, Arkalyk, Zhezkazgan, ASTANA, Karaganda, SEMIPALATINSK, Taldy-Korgan, and Bishkek. The Caspian Sea is visible on the west coast. The title 'COMMERCIAL LAWS OF KAZAKHSTAN' is overlaid in large blue letters.

COMMERCIAL LAWS OF KAZAKHSTAN

December 2006

**AN ASSESSMENT
BY
THE EBRD**

This Assessment was last updated during the preparation of the 2006 EBRD Strategy for Kazakhstan and reflects the situation at that time. It does not constitute legal advice. It was prepared by the Office of the General Counsel of the EBRD. For further information please contact ltt@ebrd.com

CONTENTS

1. OVERALL ASSESSMENT	1
2. THE LEGAL SYSTEM	2
2.1. CONSTITUTION AND COURTS	2
2.2. RELATIONSHIP BETWEEN LEGAL TRANSITION AND ECONOMIC PROGRESS	3
2.3. IMPLICATIONS FOR THE INVESTMENT CLIMATE	3
3. EVALUATION OF SELECTED COMMERCIAL LAWS	5
3.1. CAPITAL MARKETS	5
3.2. CONCESSIONS	8
3.3. CORPORATE GOVERNANCE.....	10
3.4. INSOLVENCY.....	12
3.5. SECURED TRANSACTIONS	15
3.6. TELECOMMUNICATIONS.....	19

Basis of Assessment: *This information is based on the experience of the Office of the General Counsel whilst conducting legal assessments on behalf of the Bank. It also draws on EBRD investment and legal reform activities in Kazakhstan (see www.ebrd.law).*

1. Overall Assessment

While in recent years Kazakhstan has introduced notable reforms to its legal environment, the country continues to face considerable challenges in entrenching the rule of law and related institutions upon which its successful transition to a market-orientated economy will depend. The improvements in recent years extend to securities legislation (including the creation of new market regulators in 2004 and 2005 amendments to the securities market law), concessions (in particular the adoption of the new concessions law in 2006) and insolvency (including the 2006 amendments to insolvency legislation).

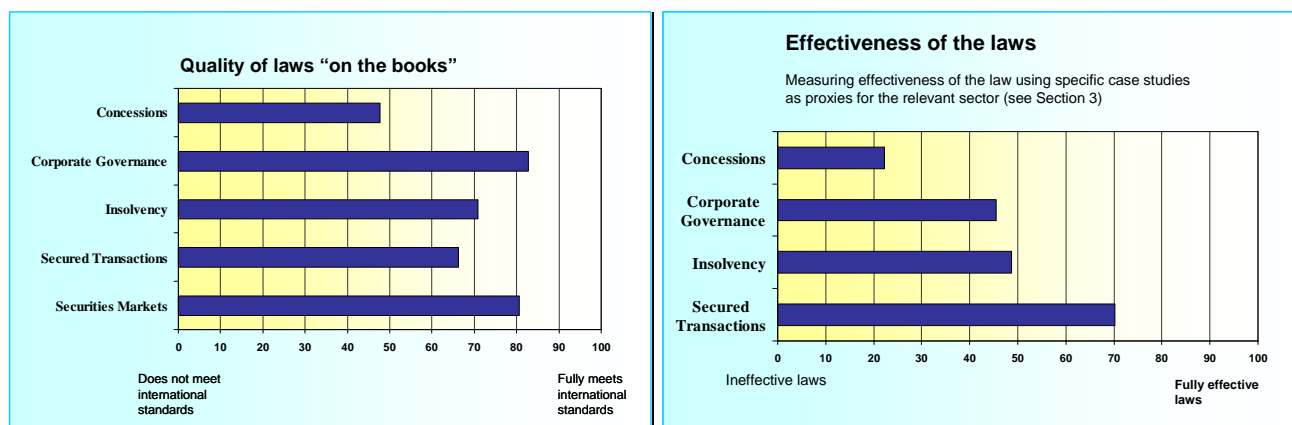
An analysis of key commercial laws that contribute directly to creating a favorable investment climate in Kazakhstan, such as secured transactions, bankruptcy laws, and regulation of financial markets, shows that there is still room for improvement in the regulatory framework and implementation of that legislation. In the capital markets sector the legal framework is relatively new and due to recent amendments has improved on the path towards best international standards and practices. The area that requires extensive revision is related to investment service providers. The corporate governance sector has a solid regulatory basis with some shortcomings regarding the transparency and activity of managing bodies and the financial reporting system.

The new Concession Law was adopted with a view to promoting private participation in the public sector. The EBRD has helped the Kazakh authorities in the process of drafting the Law. Proper implementation of the law is crucial for the sound development of the sector. Recent amendments to the Insolvency law while introducing some useful new features like external oversight during insolvency processes and an increase of regulator's powers have failed to correct many of the existing issues, such as reorganisation process and have treatment of estate assets, etc. Additionally, the practical application of insolvency proceedings is generally regarded as expensive, complex and inefficient. The secured transactions regime seems adequate, but not particularly appropriate for sophisticated transactions. Major concerns exist regarding inefficiency of the registration process and problematic enforcement of pledges. The reform of the telecoms regulatory framework is on-going and the EBRD is taking an active part in this process. Among the issues that need to be addressed are the active state participation in the market operators and the establishment of an independent market regulator.

An implementation gap was noted in all analysed sectors (see Chart 1), which both undermines the utility of the specific laws and diminishes the confidence that Kazakh and foreign investors and traders have in the legal system as a whole, in particular in its ability to uphold contractual rights. The President of Kazakhstan constitutionally holds a vast amount of power not only over the legislative, but also over the executive branch. The judiciary also remains under the control of the President and the executive branch, making it difficult to ensure its independence of the judiciary.

The challenge facing Kazakhstan in 2006 and beyond is to further enhance the quality and competence of the judiciary, tackle corruption, upgrade its commercial laws to standards that are generally acceptable internationally and make those laws fully effective through a strengthening of the court system and the rule of law.

Chart 1 – Snapshot of Kazakhstan’s commercial laws



Source: EBRD legal assessments 2002-2006

2. The Legal System

2.1. Constitution and courts

The Constitution of the Republic of Kazakhstan establishes a bicameral legislature consisting of a Senate and an Assembly (Mazhilis). Working jointly, the two chambers have the authority to amend the Constitution, approve the budget, confirm presidential appointees, ratify treaties, declare war, and delegate legislative authority to the President for up to one year. Each chamber also has exclusive powers.

According to article 44 of the Constitution, the President represents the Republic of Kazakhstan in international relations, conducts negotiations, and signs international treaties of the Republic of Kazakhstan. The President is the head of state and is elected directly for a maximum of two consecutive seven-year terms. The President appoints, with Parliament’s consent, the Prime Minister, other ministers of the cabinet, the chairperson of the National Bank of the Republic of Kazakhstan, and the chairperson of the National Security Committee. The President also appoints the heads of the local government entities, can reverse decisions made by these officials, and has broad authority to issue decrees and overrule actions taken by the ministries.

The court system in Kazakhstan is a three-tier system composed of: regional courts, district courts and the Supreme Court as the highest judicial body in Kazakhstan. The regional courts are of common jurisdiction and try most cases in the first instance. The judgments of regional courts may be appealed to the district courts, while decisions of district courts may be appealed to the Supreme Court. There are also specialized courts including military courts, administrative courts and more recently created economic courts. Cases that are in the competence of the specialized courts are judged in the first instance in the relevant specialized court.

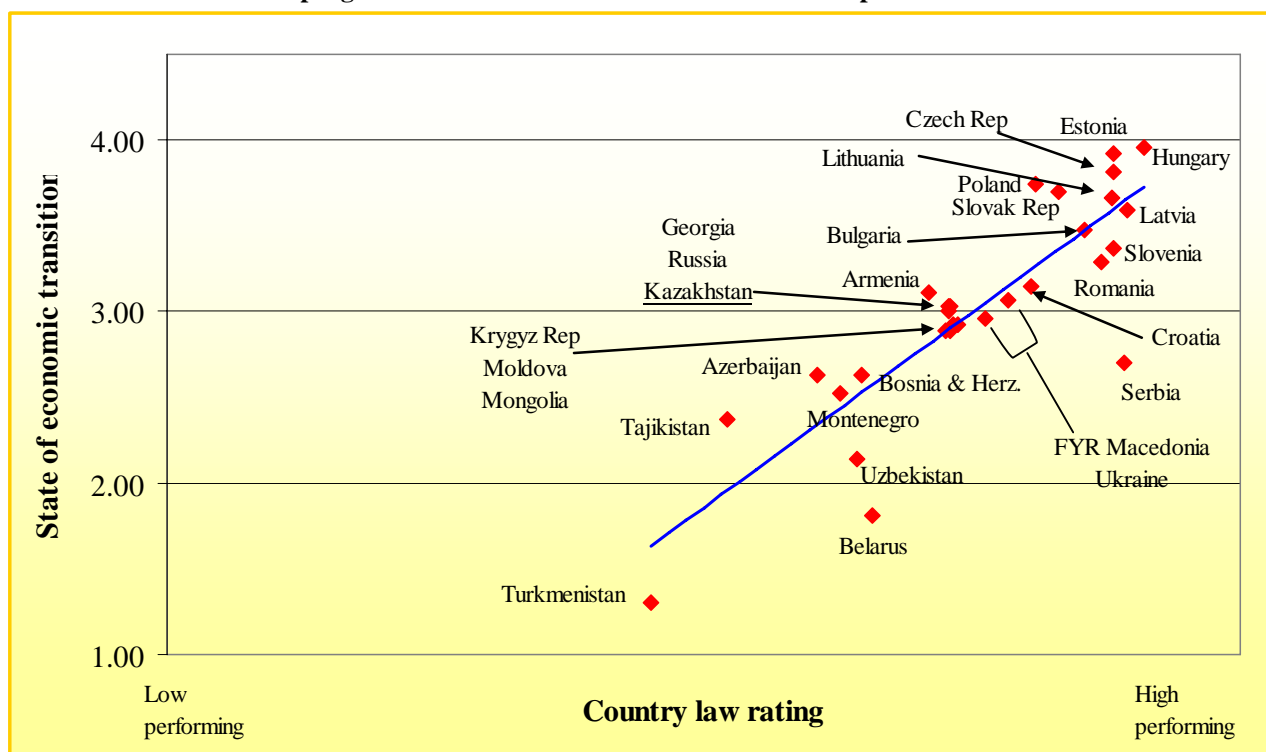
The President nominates judges for appointment to the Supreme Court and the Senate approves them. The President also appoints oblast judges, who are nominated by the Highest Judicial Council, and local judges from a list compiled by the Ministry of Justice. A Constitutional Council, whose members are also appointed by the President and legislature, review, among other things, constitutional questions.

The legal system has made some significant progress since independence and the financial sector, in particular, is well-regulated. Nevertheless, weaknesses remain in several areas and further reform is needed. Moreover, reform of the court system and judiciary is especially pressing; while the former is progressing slowly, several rulings suggest that judicial independence is very much open to doubt.

2.2. Relationship between legal transition and economic progress

Kazakhstan has been relatively successful in the transition process. Experience in transition countries suggests that legal transition and economic development progress or regress hand in hand; Kazakhstan is a typical example of this process (see Chart 2). Further success in adopting and implementing new features of the legal framework and improvements in the judiciary should further advance the overall development of the country.

Chart 2 – Rule of law and progress in transition in the EBRD countries of operations –



Sources: EBRD Transition Report 2006, Table 1.1; EBRD Composite Country Law Index, 2006

Note: The horizontal axis measures the performance of commercial and financial law. The vertical axis displays the EBRD transition index as an average of transition indicators between 1997 and 2006, with 1 referring to very early transition stages, and 4 referring to an advanced transition level.

2.3 Implications for the investment climate

Due to its macroeconomic stability and abundance of natural resources, Kazakhstan has a relatively high possibility of attracting foreign investment. Economic reform has progressed well in Kazakhstan and continues to improve.

However, the government does not currently appear to have a genuine interest in creating an investor-friendly legal climate. There are a number of recent legal initiatives aimed at safeguarding the State's economic interests in various strategic sectors and streamlining the administration of state-owned companies in those sectors. For example, as a result of changes in subsoil legislation in 2004, the State now has a "priority" pre-emptive right allowing it to participate in any proposed

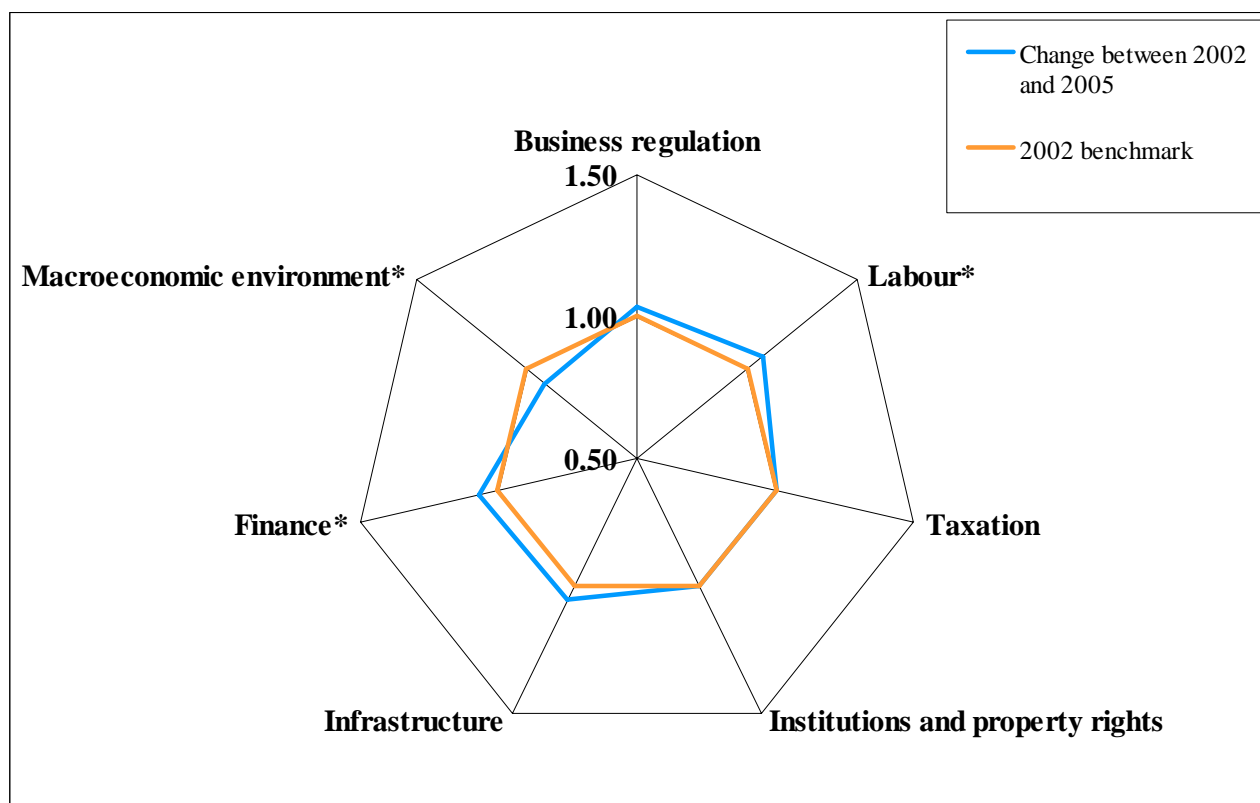
alienation of subsoil use rights. Moreover, in 2006, legislation was adopted establishing: (i) Samruk, a holding company which has been set up to manage the assets of about 20 of the largest state-owned corporations – such as KEGOC (national electricity transmission monopoly) and Kazmunaigaz (national oil and gas company), and (ii) Kazyna Fund, which has incorporated all domestic institutions of development established in 2003-2004, such as the Development Bank of Kazakhstan, and is aiming to improve their corporate management. The impact of these legal initiatives on investor confidence remains to be seen.

The Foreign Investors Council (FIC), set up in 1998 as a consultative body comprising of major foreign investors in the region, and chaired by the President, shapes further improvements to the legislative environment. As such the Legal Working Group of the FIC has successfully contributed to the strengthening of judicial independence (e.g. increase of judges' salary, reforms aimed at independence of the judiciary from local authorities, etc.), creation of Specialized Economic Courts, and drafting laws on maritime, investment, arbitration, etc.

Several areas that need reform in order to support economic growth in the long term should be noted: continuous reform of the court and judicial system, diversification of the economy as opposed to strong concentration on oil and gas industries, improve corporate governance standards, improvement of the legal implementation process, and creation of an anti-money laundering regulatory framework.

Chart 3 below graphically represents what major changes took place during the last couple of years in the key areas that affect the business environment. Improvements should be noted in the macroeconomic environment (a separate component covering inflation and exchange rates). Some deterioration may be noted in the finance field (weighted average of access to financing (for example, collateral requirements or unavailability of bank finance) and the cost of financing (interest rates and charges), labour sector (weighted average of labour regulations, and skills and education of available workers) and infrastructure area (weighted average of telecommunications, electricity, transportation, and access to land).

Chart 3 – Changes in the business environment in transition countries, 2002-05



Sources: BEEPS 2002 and 2005

Notes: The spider charts show changes in seven aspects of the business environment between 2002 and 2005. The 2002 data represent a benchmark of no change. Where the line falls inside the benchmark, this represents an improvement in that aspect of the business environment. Where the line falls outside of the benchmark, this represents a deterioration in the business environment. Wherever the changes are statistically significant, the relevant categories are marked with an asterisk. The business environment was assessed on a scale from 1 (no obstacle) to 4 (major obstacle).

3. Evaluation of selected commercial laws

The EBRD has developed and regularly updates a series of assessments of legal transition in its countries of operations, with a focus on selected areas relevant to investment activities: capital markets, concessions, corporate governance, insolvency, secured transactions and telecommunications. The existing tools assess both the quality of the laws "on the books" (also referred to as "extensiveness") and the actual implementation of laws (also referred to as "effectiveness").

All available results of these assessments can be found at www.ebrd.com/law.

3.1. Capital markets

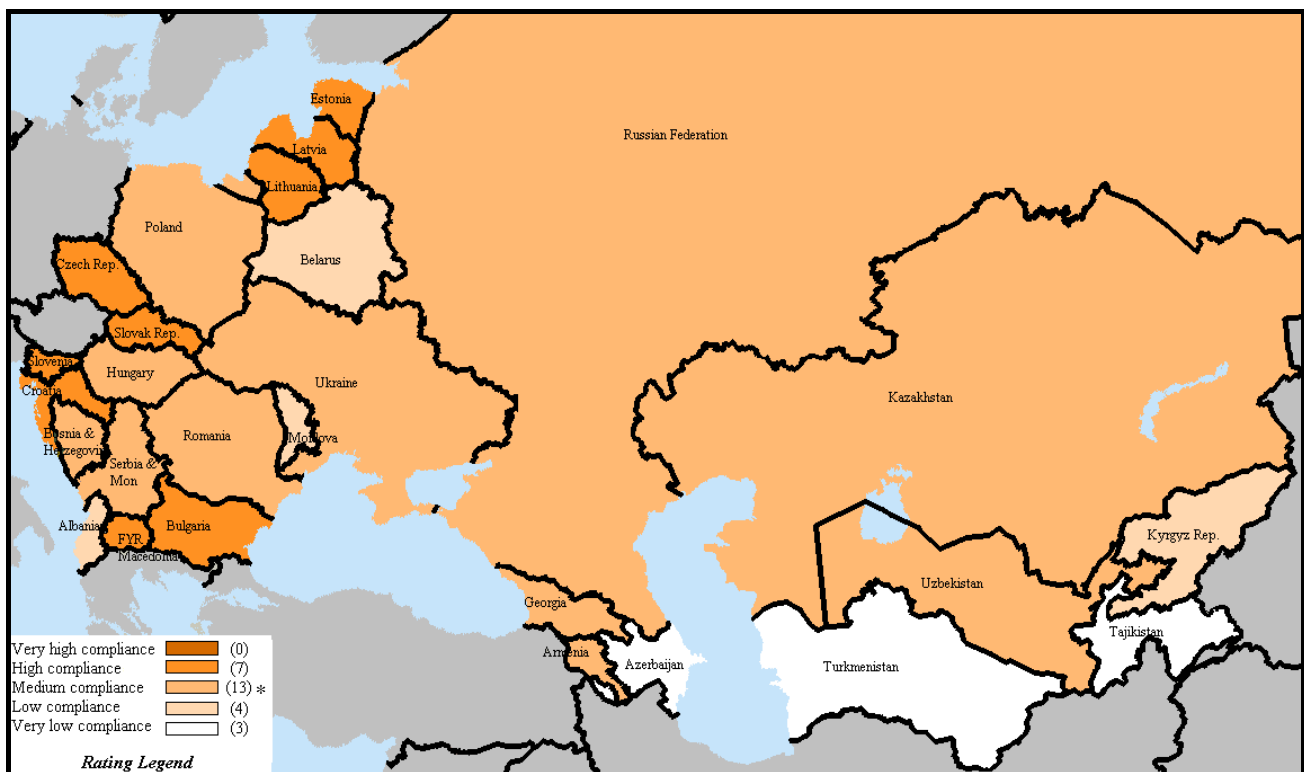
The Securities Markets Law (the 'SML') regulates the issue, placement, circulation and redemption of securities and other financial instruments, the securities market participants and the protection of investors' rights and securities holders. The SML also details state regulation of the securities market, special terms for bond issue and circulation and for the placement of securities.

The securities market is supervised by the Agency for Regulation and Supervision over the Financial Market and Financial Organisations (the “Financial Regulation Agency”), which was established in January 2004 pursuant to the Law “On State Regulation and Supervision over Financial Market and Financial Organisations”, adopted in July 2003.

The Kazakhstan Stock Exchange was established in November 1993 by the National Bank of Kazakhstan and 23 commercial banks as a currency exchange for the development of the domestic currency market following the introduction of the national currency “tenge”. In April 1996 the exchange was renamed the “Kazakhstan Stock Exchange” and in November 1996 it obtained a license for trading securities. The Exchange is now divided into four major sectors: the foreign currency market, the government securities market, the market of shares and corporate bonds and the derivatives market. In 2004 the total volume of stocks and corporate bonds transactions reached KZT 248.0 billion (around USD 1.83 billion), an increase of KZT 95.3 billion (around USD 804.8 million) or 62.4% (78.5% in USD terms) compared with 2003.

In 2004, the EBRD benchmarked Kazakhstan’s securities markets legislation with the “Objectives and Principles of Securities Regulation” published by the International Organisation of Securities Commissions (IOSCO). The results of this benchmarking demonstrated that Kazakhstan’s legislation is in “medium compliance” with international standards (see Chart 4). The assessment was updated in 2005 and the results confirmed the 2004 scoring but with some improvements registered, bringing the scoring very close to the “high compliance” category.

Chart 4 – Quality of securities market legislation in the EBRD Countries of operation



Source: Securities Markets Legislation Assessment, 2005 update

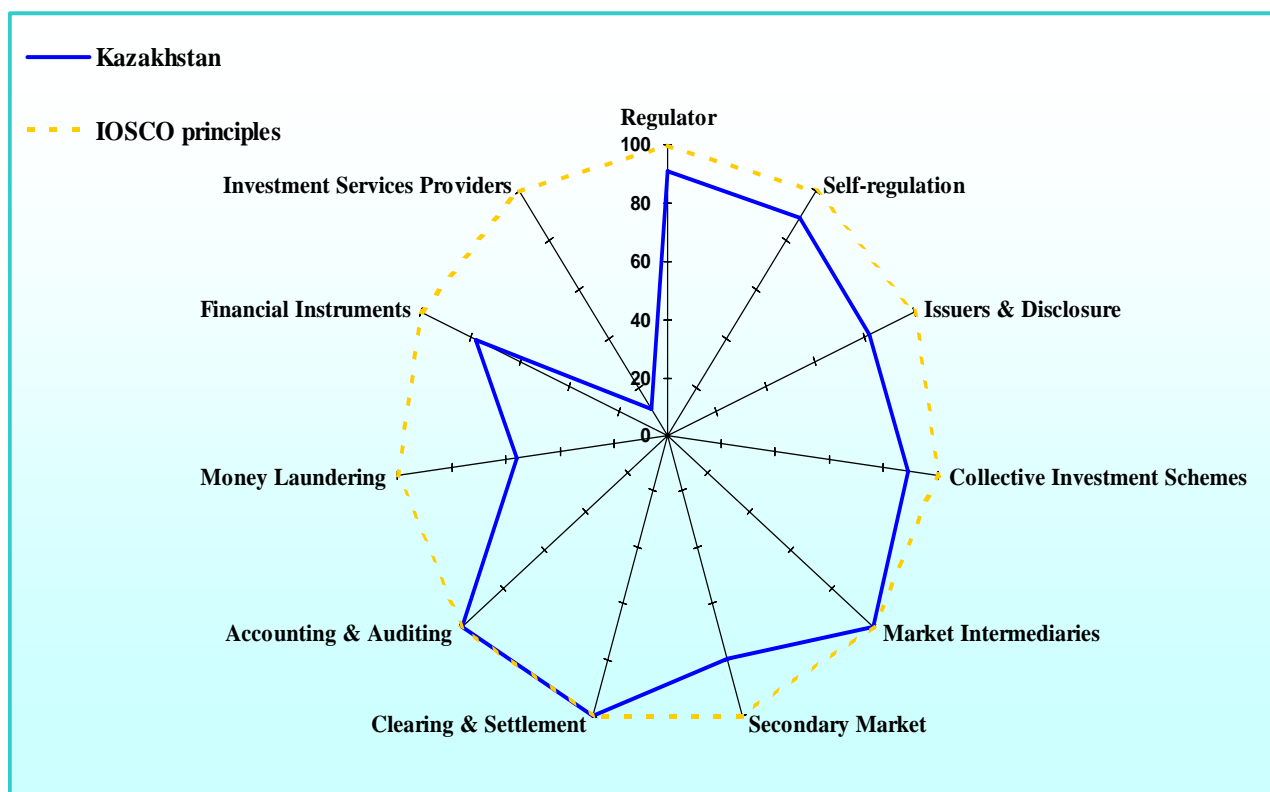
Note: The various categories represent the level of compliance of a given country’s legislation (the “laws on the books”) with international standards such as the IOSCO Principles. The asterisk indicates in which category Kazakhstan ranks.

Two market regulatory authorities were created in the second half of 2004: the Committee for the Protection of Competition of the Ministry of Industry and Trade and the Agency for the Regulation

of Natural Monopolies (AREM), each with clearly and objectively defined responsibilities. Although there are specific new provisions in the general law on advertisement restricting the production, distribution or placement of advertisements on securities, this law does not extend to underwriters or advisors. In the area of Collective Investment Schemes (“CIS”), there has been some improvement in the protection of investors. More particularly, the regulator now has several means for protecting investors in conflict-of-interest situations, such as prohibition of certain transactions, forced disclosure by management companies or verification with the custodian of the composition of assets. Further, CIS operators are now subject to a general disclosure obligation. System operators of Secondary Markets are now subject to a long list of information requirements they must provide, and AREM has powers to suspend circulation of securities.

While there have been the advances described herein, as can be seen from the spider graph below (see Chart 5) there is still much progress to be made especially in regulating investment service providers and countering money laundering.

Chart 5 - Quality of securities market legislation – Kazakhstan, 2005



Source: EBRD Securities Market Legislation Assessment, 2005 update

Note: The extremity of each axis represents an ideal score in line with international standards such as the IOSCO Principles. The fuller the ‘web,’ the more closely the country’s capital markets laws approximate these standards.

3.2. Concessions

The new Kazakh Concessions Law No. 167-III was approved on 7 July 2006 and became effective on 19 July 2006 (the “Concession Law”). The Concession Law was motivated by government policy to promote PPPs (including numerous sector-specific and municipal policy framework documents) and sets forth the legal framework for concession-type arrangements in various industries, except for those involving subsoil use (oil, gas and mining). Subsoil use concessions are specifically exempt from application of the Concession Law and are subject to special subsoil use regulations.

The Concession Law defines concession as “transfer, by way of a concession contract of state owned assets into temporary possession and use of the concessionaire with the goal to improve and effectively operate such assets; and also transfer/grant of the right to create/construct new facilities by a concessionaire using his own funds, with such concessionaire being granted the right to possess, use and dispose of such assets (or, as the case may be, without such rights being granted to the concessionaire but still with mandatory financing by the concessionaire) with subsequent transfer of such facilities to the State”.

The Concession Law states that the President of Kazakhstan may define a list of assets/facilities which may not be transferred into concession. Only legal entities (presumably, but not explicitly, both foreign and local) may become concessionaires.

The State Property and Privatisation Committee under the Ministry of Finance (the “State Property Committee”) is the principal state authority charged with (i) organising and conducting concession

tenders, (ii) executing concession contracts, and (iii) maintaining the register of the executed concession contracts. However, concession of certain assets/facilities as defined by the Government is dealt with by the specific industry regulator (e.g., Ministry of Energy) rather than the State Property Committee. Similarly, municipal property concession contracts are dealt with by local authorities. The Concession Law entitles the State to offer certain incentives (support) for concession projects (e.g., guarantees on infrastructure bonds, government guarantees of loans, transfer of exclusive rights to operate concession-related facilities). Such state support measures will be offered on a case-by-case basis and will be subject to a common statutory threshold providing that the overall value of such support measures cannot exceed the value of the particular project itself.

The Concession Law provides that specific implementing legislation (government regulations) will be issued to set forth additional specific terms and conditions for the tender process. Pursuant to the Concession Law, all tender-related information must be published in the official press.

Overall, the Concession Law is a long awaited piece of legislation that largely lives up to expectations. However, it does have a number of shortcomings and certain provisions are somewhat ambiguous. It is fairly rigid and lacks flexibility as far as property issues are concerned. For example, ownership (title) of the transferred assets/facilities will remain with the State, and on termination of a concession contract, all rights of the concessionaire with respect to the assets/facilities will be returned to the State. Similarly, in the case of newly constructed facilities, title will be registered in the name of the State immediately after completion of construction. The concessionaire will have no right to pledge the assets/facilities constituting the subject of concession without the State's prior written consent. All the above may create significant obstacles for the feasibility of potential projects. A concession contract must be executed within 30 days of the selection of the winner of the tender procedure which may prove unrealistic for some more complex projects.

The Concession Law gives the State the right to unilaterally change or terminate an executed concession contract on the grounds of protecting State/public interests. It is unlikely that any concession contracts will be awarded under the Concession Law until the necessary implementing regulations are adopted, including the list of public assets which cannot be transferred into concession and regulations concerning concession tender procedures (including a standard concession agreement). There is currently no indication when such regulations will be adopted. Furthermore, the Concession Law does not include a stability clause and it is therefore unclear whether adverse changes in legislation enacted after the date of the concession contract would apply to the concession project and the concessionaire.

The Concession Law is a bit vague as to whether a particular concession is within the authority of the State Property Committee or a relevant industry regulator. It states that the choice will be made by the Government, though it is unclear how that choice will be made. All of the above factors make it difficult to attract investors to long-term concession projects and it is yet to be seen whether the newly adopted legislation will work in practice and to what extent it will require amendments.

The EBRD has assisted the Task Force responsible for drafting of the new Concession Law and has provided commentary and suggestions on earlier drafts. The Bank might consider further assistance to the Government in the development of a workable PPP regime, in particular, with the secondary/enabling legislation, rules and standard agreements.

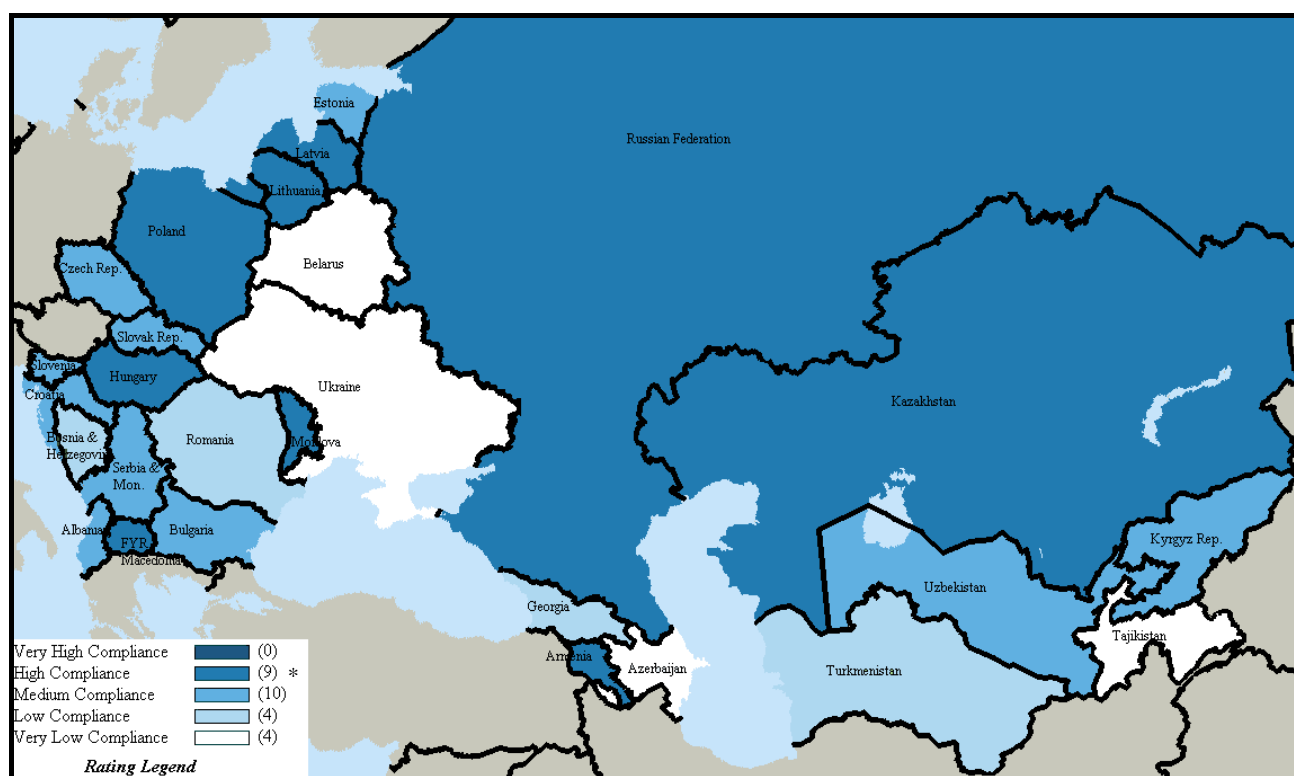
3.3. Corporate Governance

The principal legislation dealing with corporate governance in Kazakhstan is the Law on Joint Stock Companies (JSCs), which was enacted in May 2003, replacing its predecessor law of 1998. The 2003 Law was last amended in July 2005 in order to improve the system of state regulation of JSC activity and the protection of shareholders' and investors' rights.

JSCs in Kazakhstan are organised under a two-tier system where the management board is appointed by a supervisory Council which is in turn appointed by the general shareholders meeting.

According to the results of the 2004 EBRD Corporate Governance Sector Assessment, Kazakhstan is a country whose existing corporate governance related laws (i.e., "law on the books", not how the relevant legislation is being implemented), when compared to the OECD Principles of Corporate Governance, were rated among "high compliance" countries. (See Chart 6)

Chart 6 – Quality of Corporate Governance legislation in the EBRD Countries of operation



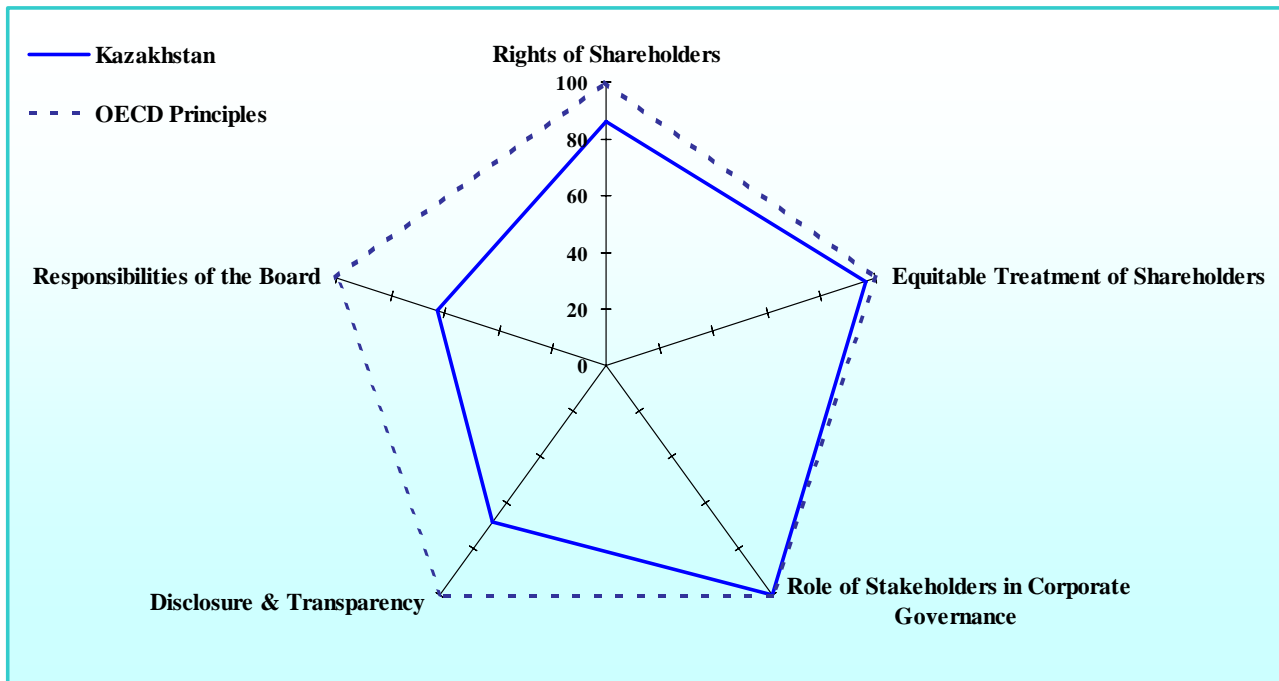
Source: EBRD Corporate Governance Sector Assessment 2004

Note: The various categories represent the level of compliance of a country's legislation (the "laws on the books") with international standards as set out in the OECD Principles of Corporate Governance. The asterisk indicates in which category Kazakhstan ranks.

"High compliance" means that the existing corporate governance related laws in Kazakhstan are relatively sound when compared to the OECD Principles of Corporate Governance. Though in the case of Kazakhstan the assessment identified some weakness in the areas of the board's responsibilities and disclosure and transparency (see Chart 7). Other deficiencies in the law identified by the Assessment include the fact that the law does not require all shares to be fully paid before they can be transferred and to publish the list of shareholders not having fully paid the amount due. The law is also silent on board responsibilities in ensuring a formal and transparent nomination process for board members; ensuring the integrity of the JSC's accounting and financial

reporting systems; and, ensuring that appropriate systems of control are in place - particularly, systems for monitoring risk, financial control, and compliance with the law. Finally, the board is not required by law to have separate committees for dealing with financial reporting, executive and board remuneration and board nominations.

Chart 7 – Quality of Corporate Governance legislation – Kazakhstan, 2004



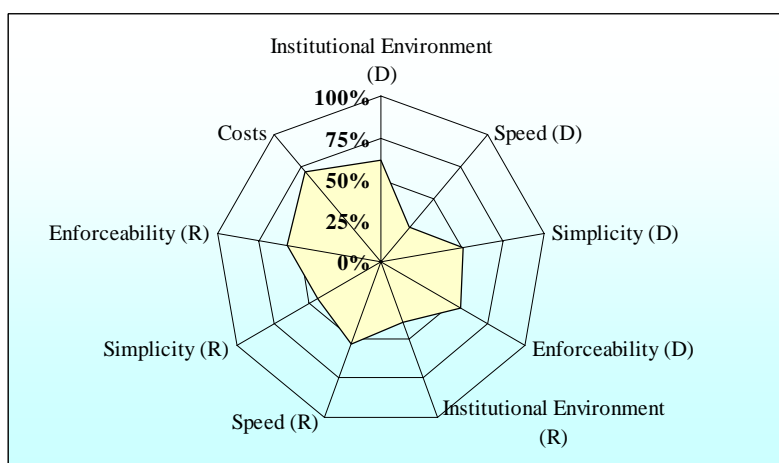
Source: EBRD Corporate Governance Legal Assessment, 2004

Note: The extremity of each axis represents an ideal score in line with international standards such as the OECD Principles of Corporate Governance. The fuller the ‘web,’ the more closely the country’s corporate governance laws approximate these standards.

In 2005, the EBRD conducted a survey for testing the effectiveness of corporate governance (how the law works in practice). A case study dealing with related-party transactions was designed. The case study investigated i) the position of a minority shareholder seeking to access corporate information on a presumed related-party transaction was indeed entered into by the company and ii) how compensation could be obtained in case damage was suffered. Effectiveness of the system for both questions was assessed based on four principal variables: complexity, speed, enforceability and institutional environment.

The survey revealed that there are a number of procedures for obtaining disclosure in Kazakhstan, but their effectiveness might be undermined by their complexity, the difficulty of the enforcement and the length of the proceedings, which might last more than one year in order to obtain an executable court order. Complexity was also identified as a problem when assessing the procedures for obtaining redress. (See Chart 8)

Chart 8 – Effectiveness of corporate governance in Kazakhstan, 2005

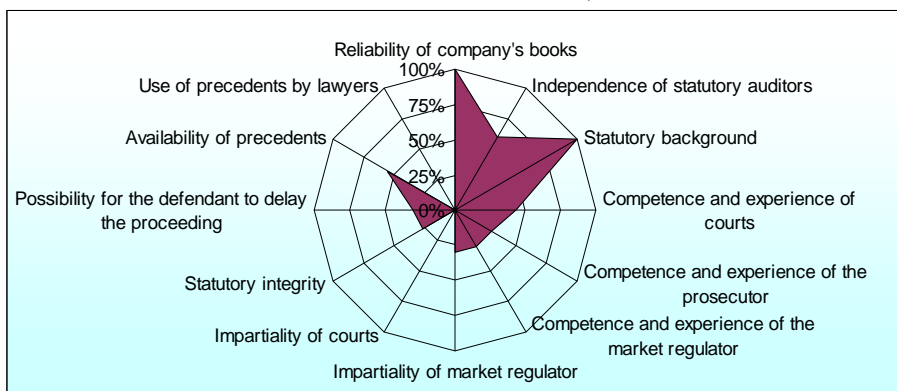


Note: The graphs show disclosure, redress and the institutional environment in the transition countries. The average results from the case study scenarios are shown. Disclosure refers to a minority shareholder's ability to obtain information about their company. Redress refers to the remedies available to a minority shareholder whose rights have been breached. Institutional environment refers to the capacity of a country's legal framework to effectively implement and enforce corporate governance legislation. Costs refer to the expenses a minority shareholder must pay to take legal action. The extremity of each axis represents an

ideal score: the fuller the 'web', the better the corporate governance framework.

When considering the institutional environment, while the survey evidenced that company information is generally of good quality, the statutory auditors fairly independent and the legal framework on related party transactions adequate, the partiality of courts and the market regulator, and corruption are considered to be major problems. Enhancing the experience and competence of courts, prosecutors and market regulators should be tackled as priorities. (See Chart 9)

Chart 9 – Institutional Environment in Kazakhstan, 2005



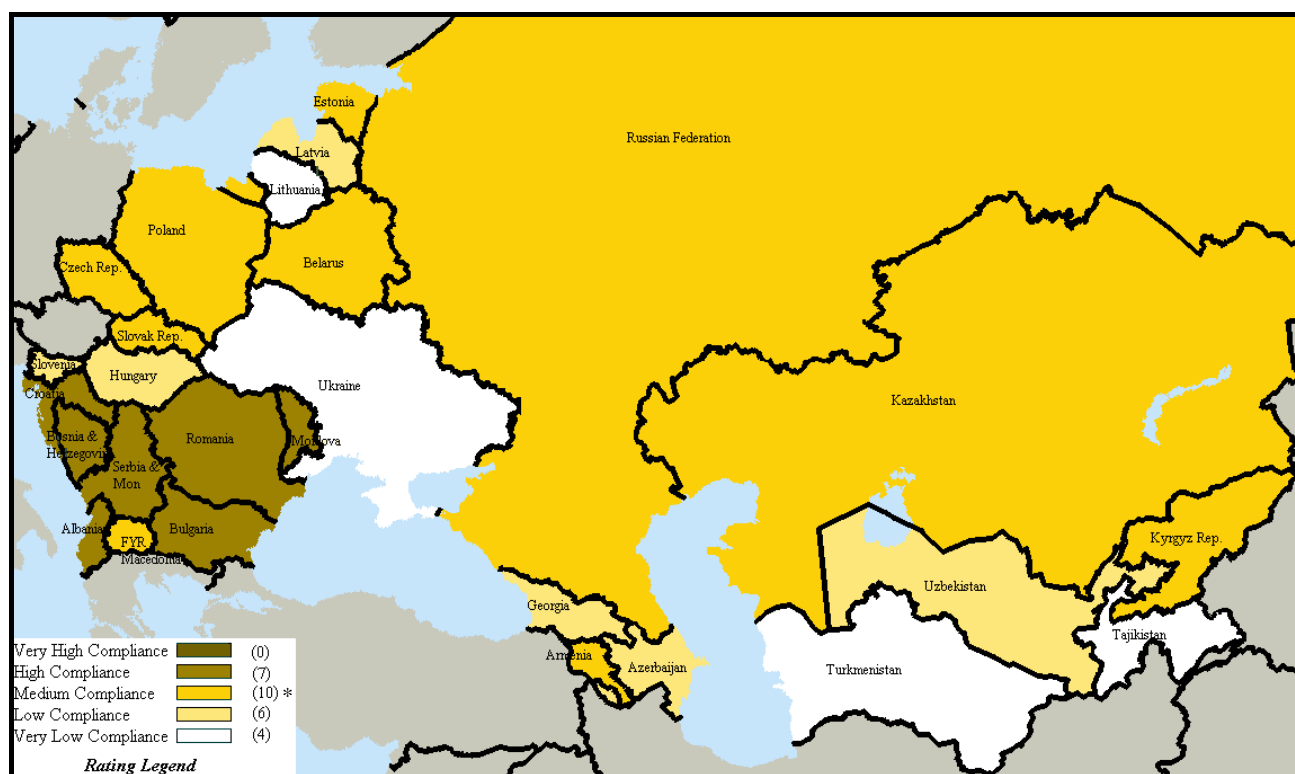
Note: Institutional environment refers to the capacity of a country's legal framework to effectively implement and enforce corporate governance legislation. Statutory background relates to how comprehensive, clear and well structured a country's definition of related-party, self-interested, self-dealing, or conflict of interest transactions

is. In particular, whether this definition covers transactions in which the director or the dominant shareholder has an indirect interest (for example, the party to the transaction is a dominant shareholder's subsidiary). Statutory integrity refers to the level of corruption within a transition country, as determined by Transparency International's Corruption Perception Index 2005. This index is measured on a scale from 1 to 10, with 1 being the most and 10 the least corrupt environment. The extremity of each axis on the graph represents an ideal score: the fuller the 'web', the better the institutional environment.

3.4. Insolvency

Bankruptcy and insolvency are governed by the Law Concerning Bankruptcy, as amended (the "Insolvency Law"). This law scored "medium compliance" when compared with international standards in the EBRD's 2004 Insolvency Sector Assessment but is amongst the strongest of the insolvency laws in central Asia. (See Chart 10)

Chart 10 – Quality of Insolvency legislation in the EBRD Countries of operation

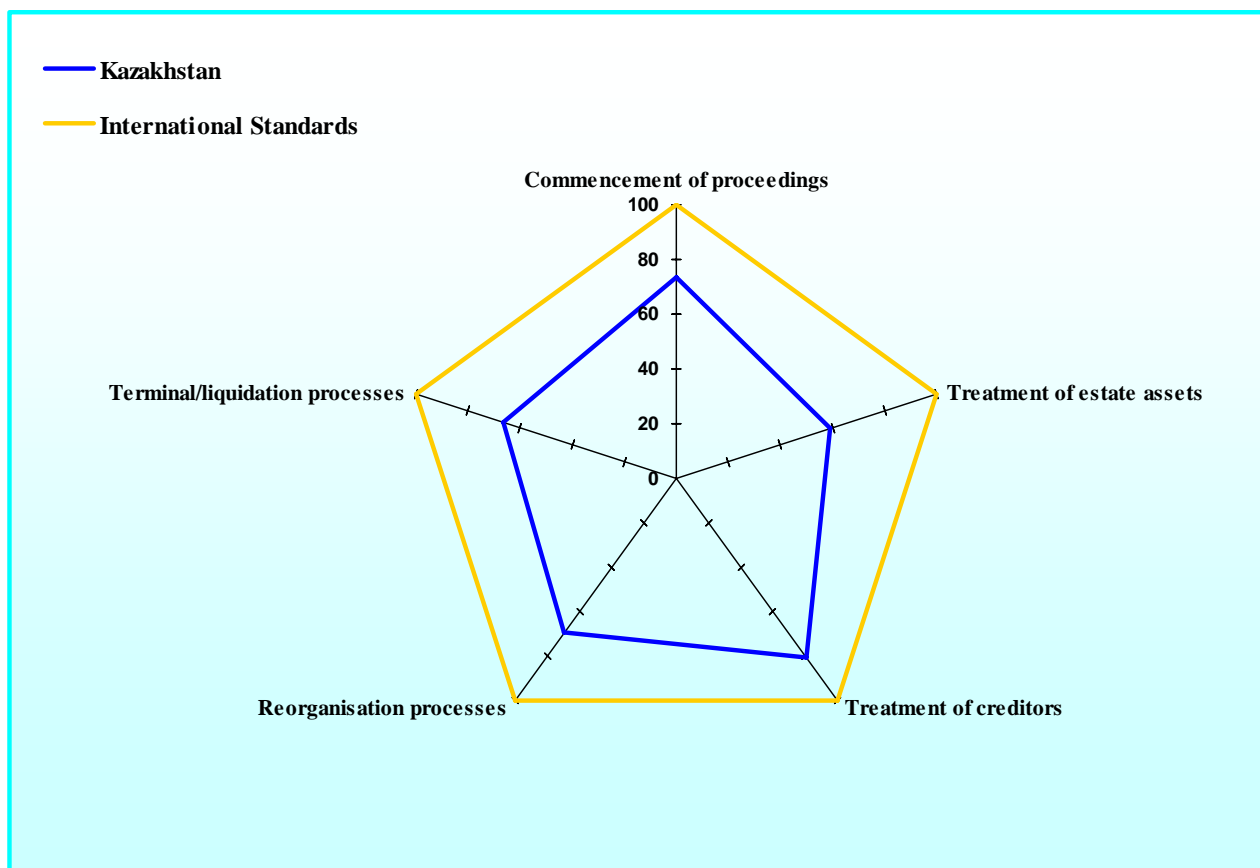


Source: EBRD Insolvency Sector Assessment 2004

Note: The various categories indicate the level of compliance of each country’s legislation (the “laws on the books”) with international standards, such as the World Bank’s Principles and Guidelines for Effective Insolvency and Creditor Rights Systems, the UNCITRAL Working Group on Legislative Guidelines for Insolvency Law, and others. The asterisk indicates in which category Kazakhstan ranks.

The Assessment showed the Insolvency Law to be relatively weak in addressing reorganisation processes, terminal/liquidation processes and the treatment of estate assets. A number of flaws were noted, including: the requirement that a debtor’s debts must be three months past due before they can be used as evidence of insolvency; a lack of clarity with regard to the definition of insolvency, the evidence required as proof of insolvency, and the effect of insolvency proceedings on secured creditors; and, a failure to address international insolvencies. (See Chart 11)

Chart 11 – Quality of Insolvency legislation – Kazakhstan, 2004



Source: EBRD Insolvency Sector Assessment 2004

Note: The extremity of each axis represents an ideal score in line with international standards, such as the World Bank’s Principles and Guidelines for Effective Insolvency and Creditor Rights Systems, the UNCITRAL Working Group on Legislative Guidelines for Insolvency Law, and others. The fuller the ‘web,’ the more closely the country’s insolvency laws approximate these standards.

The Insolvency Law was amended on a number of occasions since 2004, most recently in February 2006. The changes do not appear to have addressed many of the flaws noted above, focussing instead on reducing the use of the insolvency system for fraudulent purposes. The major change to the statute is the creation of an institution for external oversight of debtors during liquidation, reorganisation and restructuring processes. Amongst other responsibilities, the administrator of the external supervision will be responsible for ensuring the safe-keeping of the debtor’s property, revealing instances of deliberate bankruptcy and analysing the financial position of the debtor and the debtor’s acts or omissions that had the effect of evading performance of obligations owed to creditors. The external supervision regime came into effect on 19 January 2006, so it is too early to assess the overall effectiveness of the provisions. These provisions provide a third party with substantially more review power than previously available under the law and if properly implemented, they should meet their goal of reducing fraudulent use of the insolvency system.

Recent amendments also provided the Authorised Body (the regulator) with new and expanded powers. The Authorised Body now has authority to approve rules for training bankruptcy commissioners, administrators of external supervision and rehabilitation managers. Other new powers include the ability to intervene in insolvency proceedings, design the process for approving the application of a rehabilitation proceeding to a debtor, and overseeing/approving the expenses of the insolvency professionals.

Other notable changes to the law include extended periods for the restructuring of companies (now nine months) and for strategically important businesses (three years) and an expansion of the period for reviewing transactions of the debtor from two years to three years.

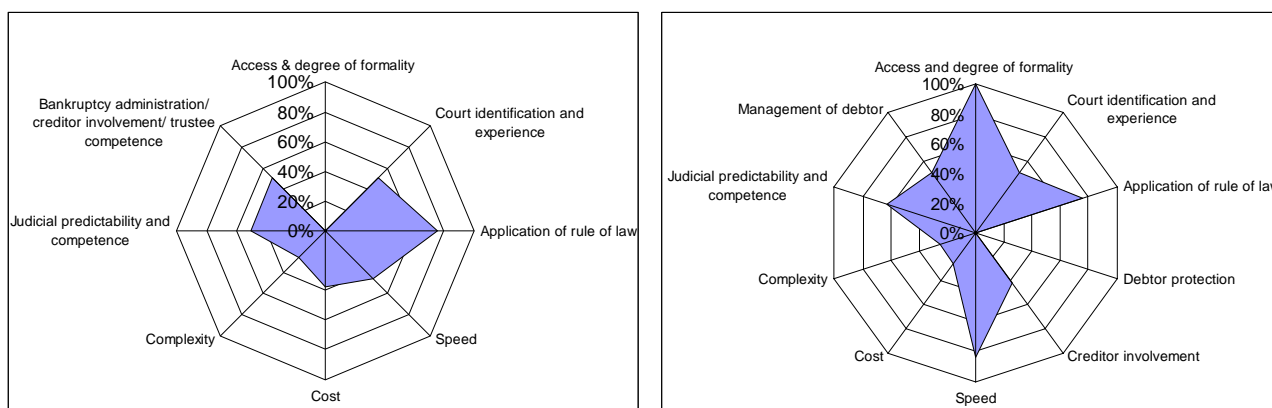
It is worthwhile to point out some of the positive features of the Insolvency Law. This law provides for both good interim protective relief of the debtor and the strengthened reversal of fraudulent transaction provisions should have the effect of enlarging the pool of assets available for distribution from the estate. In addition, to help avoid fraudulent or unnecessary proceedings, the Insolvency Law requires the report of an auditor to independently analyse and confirm whether a restructuring is truly viable.

Several problems with the application of insolvency law in Kazakhstan were revealed in EBRD’s 2004 Legal Indicator Survey, which measured the effectiveness of insolvency legislation (see Chart 12). In particular, the Insolvency Law appears to be an ineffective weapon, or an insufficiently credible threat, for creditors to induce recalcitrant debtors to pay their debts. Access to the insolvency system is overly formal and complex and the process is generally regarded as being expensive and inefficient. Kazakhstan was found to have one of the largest “implementation gaps” (the difference between the overall quality of its insolvency law and the effective implementation of that law) amongst the EBRD’s countries of operations. Time will tell whether the new amendments improve the situation.

Chart 12 – Effectiveness of Kazakhstan insolvency regime

Creditor-Initiated Insolvency

Debtor-Initiated Insolvency



Source: EBRD 2004 Legal Indicator Survey on Insolvency

Note: The results have been derived from stakeholder responses to questions about the practical functioning of the insolvency regime. The fuller the “web,” the more effective the country’s insolvency regime is.

3.5. Secured Transactions

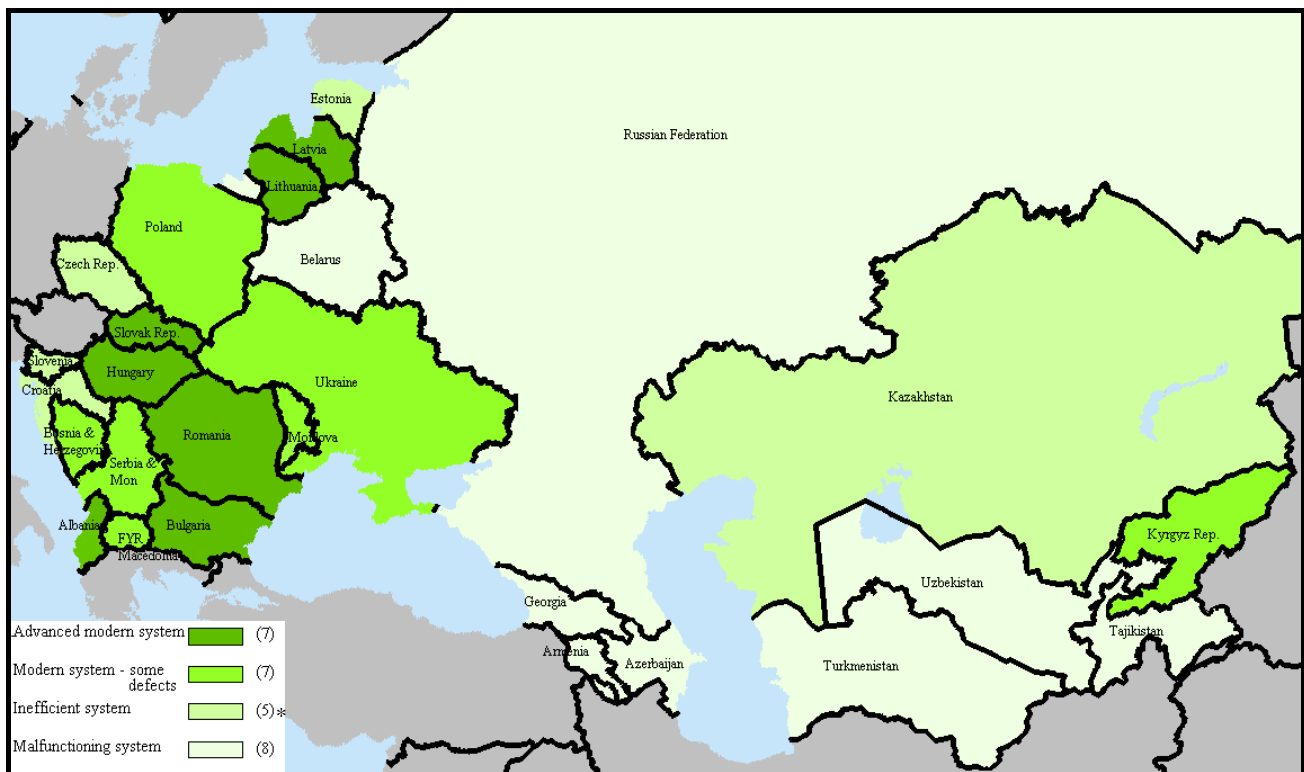
Security rights over movable assets (also referred to as pledges) are regulated by the Civil Code of the Republic of Kazakhstan, adopted in December 1994 and other laws.

There are two main types of security over movable assets under Kazakh law: possessory (where the possession of the collateral is transferred to the creditor) and non-possessory (where the debtor may retain and use the collateral during the life of the security). The registration system is two-tier: there is a mandatory registration, which applies to specific types of assets such as motor vehicles and aircraft. These assets are registered in specific registries and the pledge should be registered there too (e.g. the police for pledges over motor vehicles). For all other types of assets, pledge

registration is voluntary only and is conducted in the Centres for Registration of Immovable Property and their subsidiaries. There is no centralised registry but 16 separate centres in two major cities, Astana and Almaty, and in each region. The registries are supervised by the Committee on Registration Service under the Ministry of Justice in Astana. Most of the registries have computerised databases which are accessible through the respective registrar.

Based on the EBRD assessment, the secured transactions legal regime is adequate, although not particularly enabling for sophisticated transactions. (See Charts 13, 14 for graphical presentation of the assessment of secured transactions legal basis)

Chart 13 – Quality of secured transactions legislation in the EBRD Countries of operation

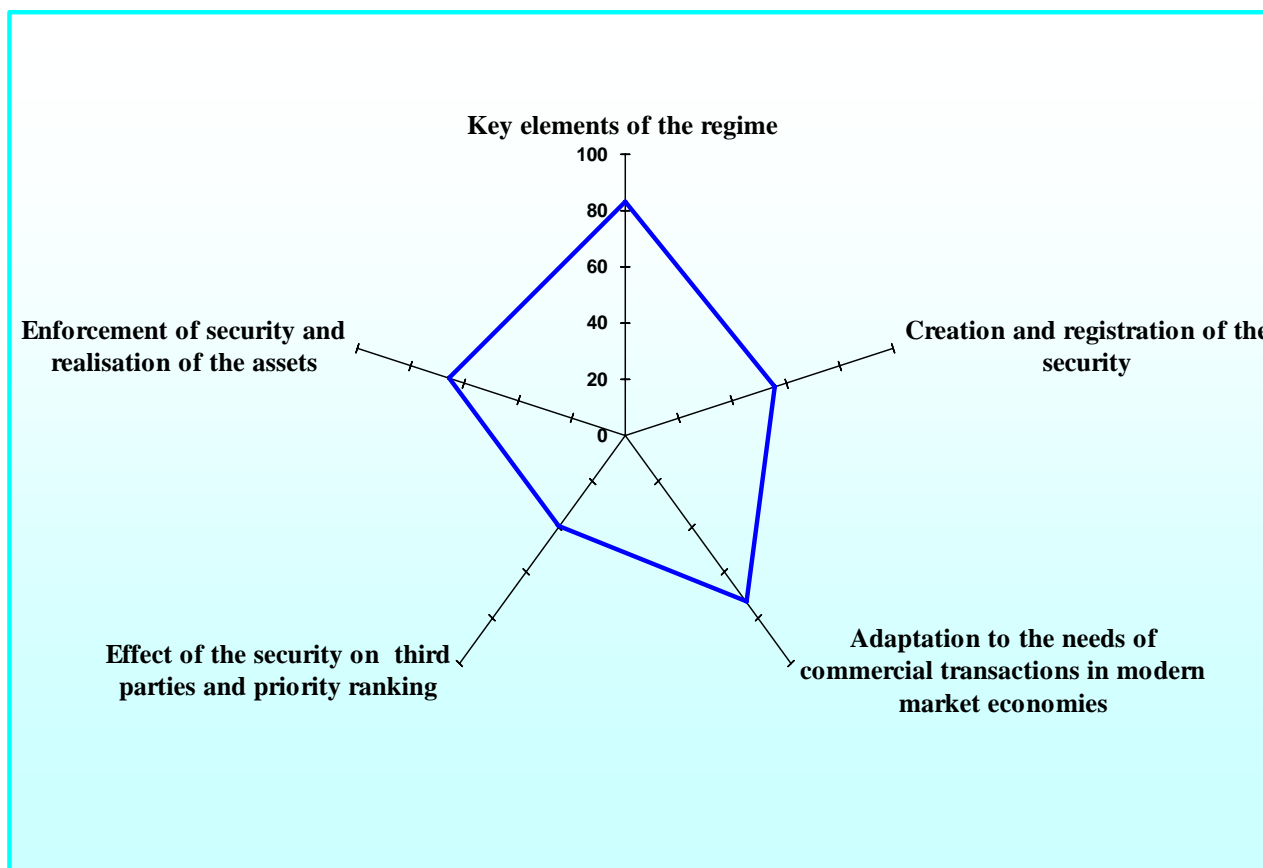


Source: EBRD Regional Survey of Secured Transactions Legislation 2004

Note: The level of reform referred to in the legend above is assessed in relation to the EBRD's Model Law on Secured Transactions and the 'ten core principles of secured transactions law.' The asterisk indicates in which category Kazakhstan ranks.

Some transactions remain complex to achieve. For example, a pledge over assets described generally would not be a viable option to secure a transaction since the law provides that the pledge agreement must *specify* the assets and their value or a method for their valuation. If the pledge is registered, a list and description of the pledged assets must be entered in the registry. A general description would be possible for pledges over goods in circulation and processing (merchandise stock, raw materials, materials, semi-finished products, finished products, etc.), where the debtor could change the composition and natural form of the pledged assets provided that their overall value would remain the same as prescribed in the pledge agreement. However, such condition would be difficult to fulfil where a debtor would have to renew its stock on an ongoing basis.

Chart 14 – Quality of secured transactions legislation – Kazakhstan, 2004



Source: EBRD Regional Survey of Secured Transactions Legislation 2004

Note: Scoring is done on a scale of 1 to 100, with 100 representing the most advanced legal regime. The fuller the 'web,' the more advanced the country's secured transactions legal system is.

Practitioners have expressed some concerns on the efficiency of the registration process - bureaucracy and a corrupt environment makes it hard to use the system. Search requests take up to five days, depending on work load, though considerable delays are also reported. The EBRD has, in the past, experienced unacceptably long delays in perfecting its security rights over the borrower's assets in Kazakhstan.

Finally, though the means of enforcement provided by the law seem adequate on the books, in practice, enforcement is reported to be problematic because of deficiencies in the court system; uncertainty regarding the enforcement mechanisms; incidents of non-compliance of the government with enforcement rules and decisions; difficulties in locating and ensuring control of the pledged assets; and, possible application of exchange control rules to repatriation of enforcement proceeds. Serious delays could occur due to the right of the court to postpone the sale of the pledged property by up to one year upon the debtor's request. These problems were confirmed by a survey that the EBRD conducted in 2003, focusing on the enforcement of pledges (charges) in the region (see Charts 15, 16). Whereas Kazakhstan provided very encouraging overall results in terms of the return that a lender could expect from enforcing its security over the charged assets and the time and simplicity involved in such process (certainly the best in the region), the survey also highlighted serious problems, in particular the high risk of court corruption and the lack of training of key enforcement officers, such as the bailiffs.

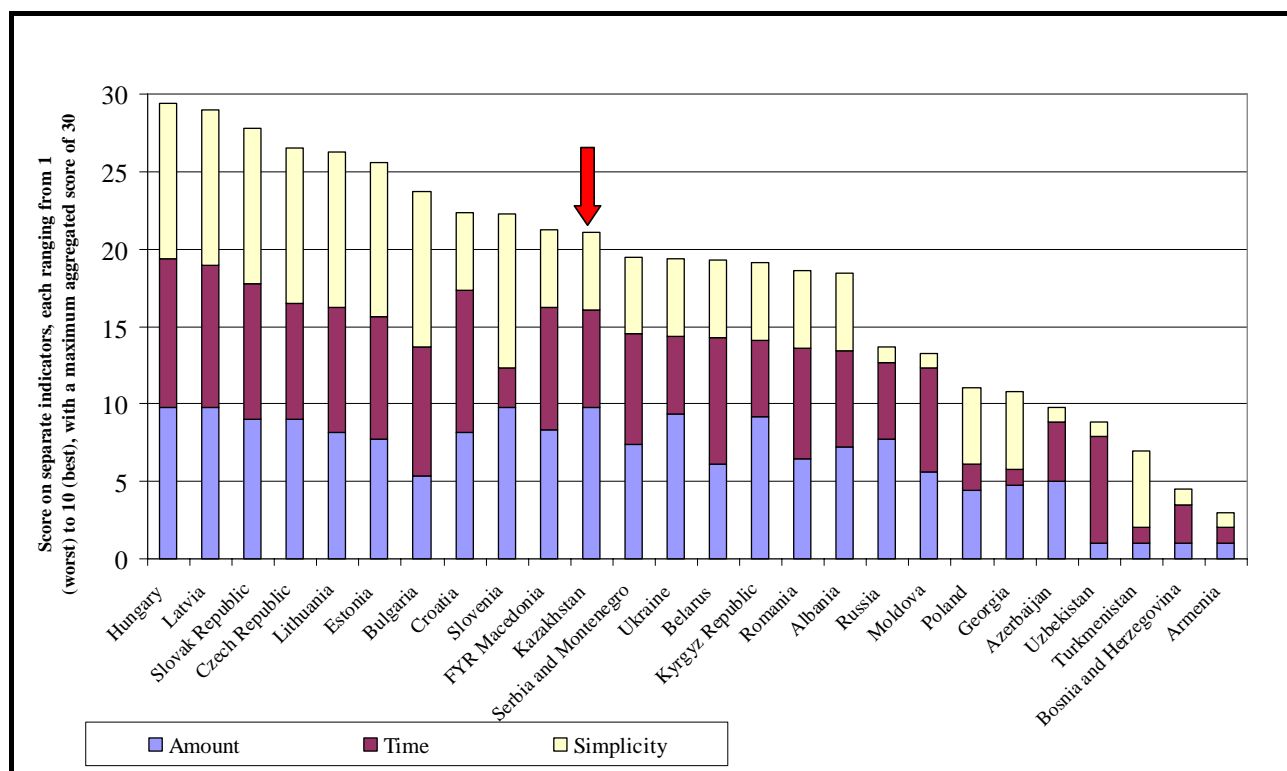
Security over immovable assets (mortgages) is covered primarily by the 1995 Presidential Decree (having the force of law) on Mortgage of Immovable Property. An enterprise can be charged by

way of a mortgage, where the security will cover all the enterprise's movable and immovable assets, claims and exclusive rights, including those obtained during the mortgage period, "main and circulating funds", and securities on its balance sheet.

Mortgages are not required to be notarised but they have to be registered with the Centre for the Registration of Immovable Property of the Ministry of Justice, as mentioned above. Should the borrower default on its obligations under the relevant mortgage loan agreement, the secured mortgage lender has priority rights with regard to other creditors to be compensated (from the proceeds of the sale of the property) for the principal amount of the mortgage as well as interest and other expenses incurred as a result of the default, such as default penalty, legal and other fees associated with the foreclosure on the mortgaged property.

Mortgage foreclosure can be either enforced through the court or settled out of court. Settling out of court is the preferred option. The main difficulty stems from the requirement of Kazakh law to notify the borrower in person of the conduct of the auction (failure to do so would invalidate the auction process). If for whatever reason it is impossible to notify the borrower in person, the matter must then be taken to court. If an auction is successful, then the lender is considered to be paid off in full, irrespective of whether the auction proceeds cover the amount claimed/owed on the mortgage. If, however, the auction proceeds exceed the claim, the difference is given back to the borrower.

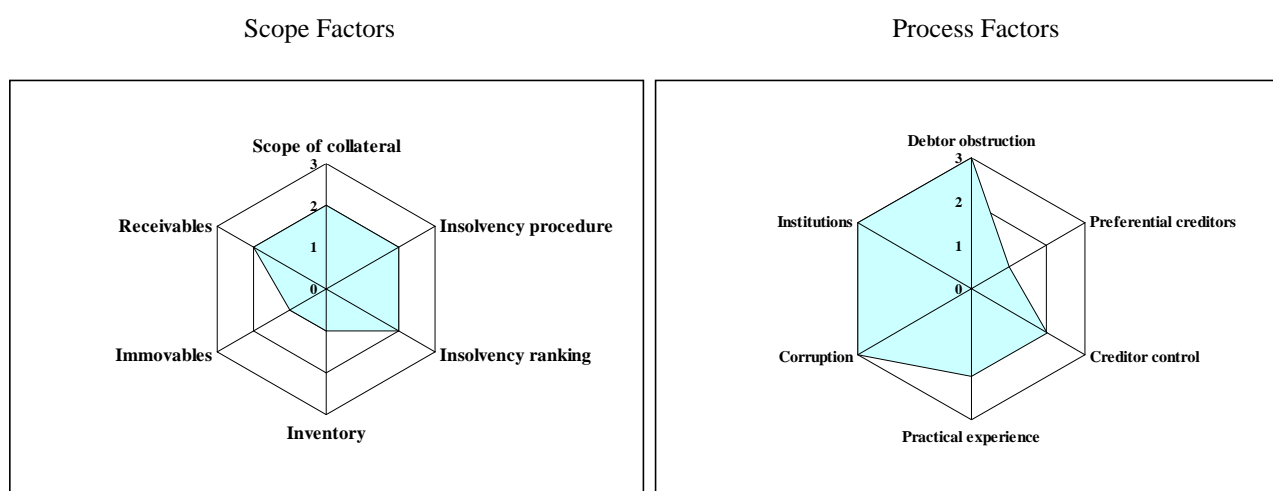
Chart 15 – Effectiveness of the Charge Enforcement Process – Kazakhstan, (2003)



Source: EBRD New Legal Indicator Survey 2003

Note: The chart shows how much a secured creditor can expect to recover (amount), how quickly (time), and how simply (simplicity). The higher the bar, the more efficient and creditor-friendly the system is.

Chart 16 - Obstacles to Charge Enforcement Process – Kazakhstan (2003)



Source: EBRD Legal Indicator Survey 2003

Note: “Process” factors measure the impact that specific obstacles would have on the enforcement proceedings. “Scope” factors give an indication of how effective enforcement would be when conducted on various types of collateral and in the context of debtor insolvency. The fuller the coloured area, the more serious the problems are.

There are several challenges ahead in order for the Kazakh government to achieve the advanced legal regime for secured transactions that the country’s continued economic progress certainly requires.

3.6. Telecommunications

The telecommunications sector in Kazakhstan is currently governed by the Communications Law of 2004 (the “Communications Law”) and regulation is split amongst three main agencies: the Agency for Informatisation and Communications (AIC), the Agency for Regulation of Natural Monopolies (AREM) and the Competition Protection Committee of the Ministry for Industry and Trade (CPC). AIC was established to replace the Communication and Informatisation Committee of the Ministry of Transport and Communication. Among the areas AIC is specifically responsible for is licensing operations, technical procedures for interconnection and determination of accounting principles for regulated operators. AIC is also responsible for both formulating and implementing policy/strategy in the telecommunications sector as well as responsibility for greater information communications technology (ICT) policy making. AREM regulates natural monopolies, which parts of the telecommunications network is still considered to be in Kazakhstan, and is responsible for tariff and cross subsidisation issues. CPC regulates dominant operators in the market and is responsible for retail tariff setting.

The Communications Law represents a significant improvement in the environment for telecommunications in Kazakhstan and covers all major areas in the sector, providing a legal basis for liberalisation, equal network access for market participants, universal service provisions, etc. The passage of the Communications Law was accompanied by additional legislation limiting foreign ownership in Kazakh companies providing international or long-distance fixed-line calls to 49%.

While formal liberalisation occurred in January 2006, the incumbent partly state-owned operator, Kazakhtelekom (KTC), is dominant in virtually all market segments through its control of the majority of local and backbone telecommunications infrastructure. Though there is limited competition in the fixed-line, satellite and value-added/data markets, meaningful competition has

yet to take hold. Fixed line teledensity currently stands at approximately 20%, with 7 operators of significance competing for the small part of the market not dominated by KTC. The perceived abuse by KTC of its dominant position in the market has led the Government to examine the feasibility of vertical separation of the company (separation of networks and services), relieving it of its backbone network in an effort to facilitate open access for competing operators. While the government has repeatedly announced an intention to further privatise KTC (50% Government shareholding), no meaningful steps appear to have been taken to make this intention a reality.

The mobile sector in Kazakhstan is quite competitive with in excess of 30% teledensity at the beginning of 2006. The leading players within the mobile market are Altel (50% KTC shareholding), K-cell (KTC also a shareholder) and K-mobile (currently wholly owned by Russian operator VimpelCom). Both K-cell and K-mobile operate GSM networks while Altel operates an older AMPS network. An attempt to licence a third GSM in 2004 failed, apparently due to the absence of sufficient interest and possible concerns about legislation limiting foreign investment in the sector.

Whilst significant reform has been undertaken, a number of fundamental elements remain outstanding. On the legislative side, the Communications Law requires revision to be made more consistent with international best practice and better support the now liberalised marketplace. Going forward, the success of these legal reforms will hinge upon their full implementation over the short to medium term. The authorities should ensure that such implementing legislation and instruments are adopted and enforced without delay, particularly in the areas of tariff rebalancing and interconnection. On the institutional side, establishment of an independent sector specific regulator is a critical requirement to make liberalisation work in a meaningful way. It is understood that Government accepts the case in principle for such a regulator – every effort should now be made to ensure that an appropriately empowered and resourced regulator is established in the quickest reasonable timeframe. Similarly, the continuing regulation of parts of the telecommunications sector by AREM, as a natural monopoly, does not reflect current sector realities. Accordingly, telecommunications should be removed from the list of natural monopolies forthwith and the authority to regulate transferred to an appropriately empowered sector regulator as soon as it has sufficient capacity in this area. In addition to a sector specific regulator, the Government should ensure that CPC is also provided with sufficient resources to perform its duties in the sector. As an interim step, while a sector specific regulator is becoming operational, the establishment of a joint interim regulatory working group, consisting of AIC, AREM and CPC should be considered. This working group would bring together all the sector regulatory expertise to address sector regulatory issues ahead of appropriate formal reassignment of sector regulatory functions.