

**COMMERCIAL LAWS OF  
TURKMENISTAN**  
**May 2010**  
**AN ASSESSMENT BY THE EBRD**

**Office of the General Counsel**



**European Bank**  
for Reconstruction and Development

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**Basis of Assessment:** This document draws on legal assessment work conducted by the Bank (see [www.ebrd.com/law](http://www.ebrd.com/law)) and was last updated during the preparation of the 2010 EBRD Strategy for Turkmenistan, reflecting the situation at that time. The assessment is also grounded on the experience of the Office of the General Counsel in working on legal reform and EBRD investment activities in Turkmenistan. It does not constitute legal advice. For further information please contact [ltt@ebrd.com](mailto:ltt@ebrd.com).

## 1. Overall Assessment

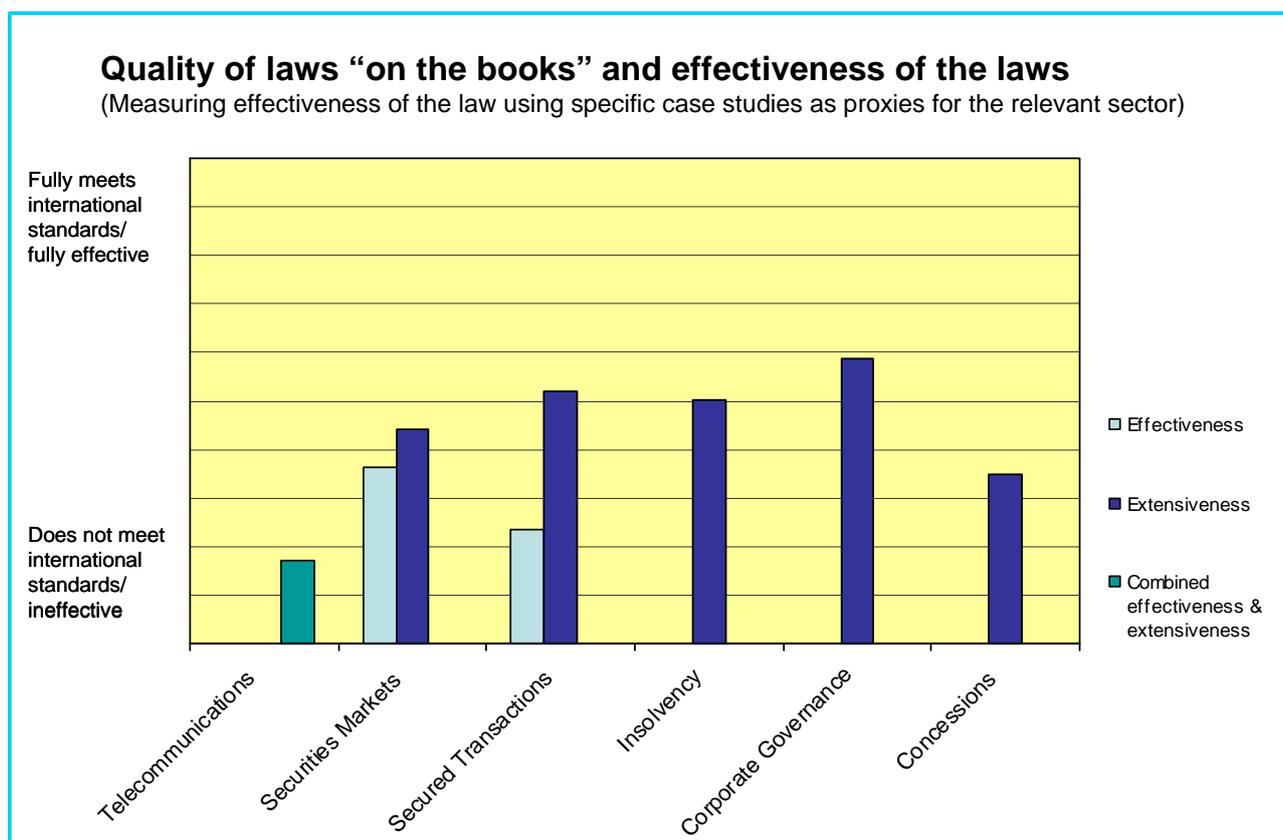
When compared to other EBRD countries of operations Turkmenistan's post-independence transition towards a market-oriented economy supported by democratic and pluralistic institutions can be viewed as slow. Whilst some parts of the legal framework have been changed in order to reflect new realities and encourage investment in particular sectors, the implementation of existing laws remains very haphazard and dependent upon high level state bodies and implementing authorities.

The quality of the regulatory framework in key sectors demonstrates the stage of the country's development. For example, in the securities market field the basic laws were adopted in the early stages of Turkmenistan's independence and have remained unchanged since. Besides the fact that these laws fall short of international best practices, they do not seem to be applied in practice, since there is no functioning stock exchange and there appears to be no public issuance of shares. In addition, the application of good corporate governance practice is hindered by the fact that the state holds the majority stake in most companies.

The current Concessions Law applies only to foreign investors and the concession process is characterised by very limited transparency and predictability. The insolvency framework reveals many deficiencies, such as a lack of clarity and comprehensiveness, and cumbersome procedures. A framework for secured transactions does exist but it is flawed by uncertainty, complex procedures, prohibitive pricing and difficulty of enforcement. The telecommunications sector has changed little since Soviet times and government initiatives to push for its development have been limited.

Consequently, extensive improvements are necessary in order to create an appropriate legal framework for the economic development of the country. However, such changes and further transition will depend to a great extent on a sustained effort by the government. Chart 1, below, graphically represents the status of laws and their effectiveness in the country.

**Chart 1 – Snapshot of the commercial laws of Turkmenistan**



Source: EBRD legal assessments 2002-2009

## 2. The Legal System

### 2.1 Constitution and courts

The 1992 Constitution declares Turkmenistan as a secular democracy in the form of a presidential republic. According to the Constitution, power is separated between the executive branch (Cabinet of Ministers), headed by the President; the legislative branch, consisting of the 50 seat Parliament (“Milli Mejlis”); and the judicial branch, embodied in the courts.

In addition to the above structure, Turkmenistan has an additional entity – the Khalk Maslakhaty (“People’s Council”). The People’s Council is an overarching advisory council designated as the supreme representative body, overseeing the other branches and even the President. The composition of the Council is similarly overarching, including the President, members of the Parliament, members of the Cabinet of Ministers, People’s Advisors (elected for five years), heads of the Supreme Court, the Prosecutor General, and heads of regional and local administrations, NGOs, youth organisations and trade unions.

In addition to its mandate to oversee all the other branches, the Council has the power to approve the overall direction of the social, economic and political policies of the country, to adopt and amend the Constitution and constitutional laws, to name the date for presidential and parliamentary elections, and to ratify participation in international organisations and unions.

The court system comprises the Supreme Court and lower courts which handle civil, criminal, and administrative cases. The President appoints judges for all courts for a period of 5 years. The head of the

Supreme Court is appointed by the President upon approval by the Parliament. There is no Constitutional Court in Turkmenistan.

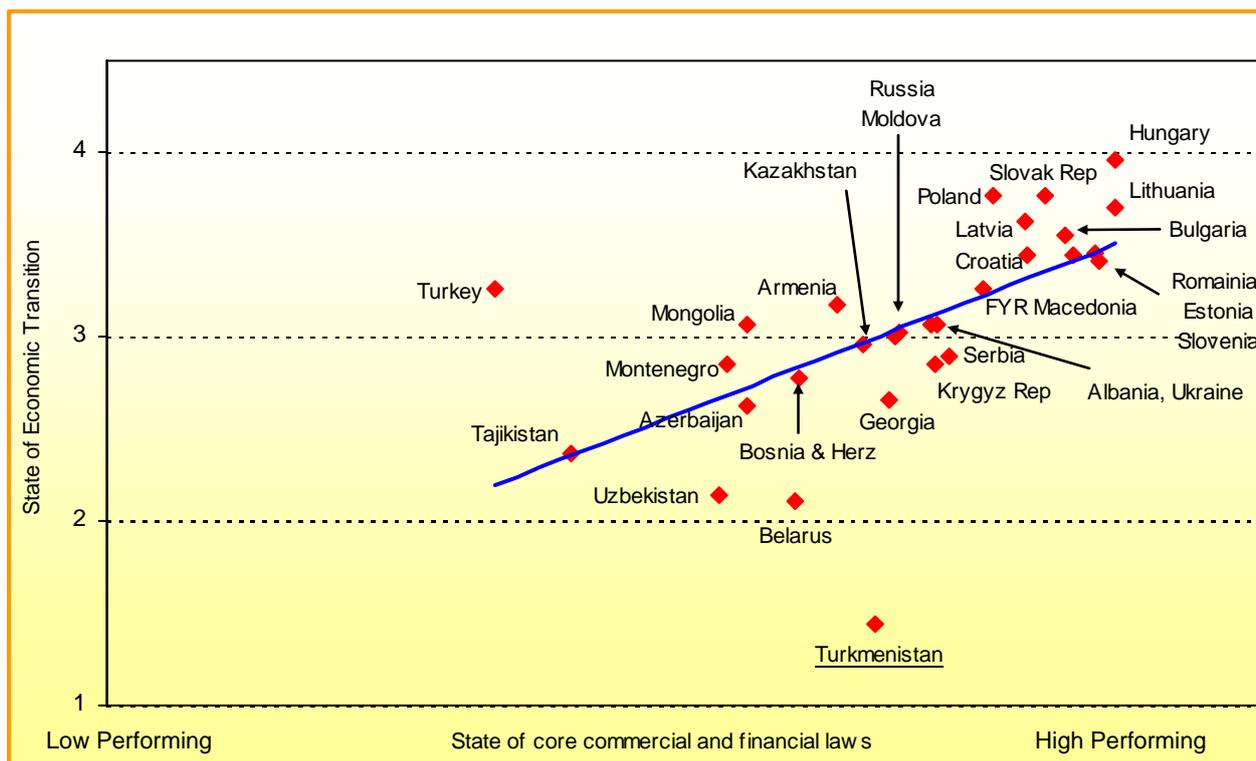
The judicial system is affected by the authoritarian regime that exists in the country. According to the courts are characterised by haphazard decision making processes, together with widespread bureaucracy and corruption. The independence of judges is another issue that would need to be addressed in any comprehensive programme of judicial reform.

The Prosecutor’s Office has retained from the Soviet era the power to oversee and investigate the activities of all bodies and branches of the state, including the judiciary.

## 2.2 Relationship between legal transition and economic progress.

Experience in the EBRD’s countries of operations suggests that the degree of respect for the rule of law and progress in economic transition go hand in hand. Given the positive correlation throughout the Bank’s countries of operations between these two dimensions, i.e., legal transition and overall economic progress, it is reasonable to expect that the future success of the transition process in Turkmenistan will be dependent on further improvements to the legislative framework, successful implementation of the legislation and on improving the quality of the courts (See Chart 2 for Turkmenistan’s position in terms of legal and economic progress compared to other countries in the region).

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



**Note:** The **horizontal axis** measures the performance of commercial and financial laws. The **vertical axis** displays the EBRD transition index as an average of transition indicators between 1997 and 2009, with 1 referring to very early transition stages, and 4 referring to an advanced transition level.

**Source:** EBRD Transition Report 2009, Table 1.1; EBRD Composite Country Law Index, Mar 2009

### *2.3 Recent developments in the investment climate.*

A slow transition has discouraged the flow of foreign investments in the economy. Most companies remain state owned and managed by the state which inhibits competition and market entrance by investors. Additionally, the economy lacks a clear, comprehensive and market oriented legal framework, which, coupled with a rudimentary infrastructure, acts as a deterrent to foreign investment.

Despite its reluctance to adopt market-orientated policies, the country has nevertheless undertaken a number of measures aimed at promoting investment in the sectors deemed to benefit from an investment surge, such as oil and gas. To this end, limited legal initiatives such as implementing tax holidays and allowing free economic zones have been adopted. However, given the status of legal enforcement and state interference in private business, few foreign investors have ventured to participate in local companies. Even fewer investors have managed to maintain their business in the country and continue to operate.

## **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: concessions, corporate governance, insolvency, secured transactions, securities markets 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 such laws (also referred to as “effectiveness”). This annex presents a summary of the results accompanied by critical comments of the Bank’s legal experts who have conducted the assessments.

All available results of these assessments can be found at [www.ebrd.com/law](http://www.ebrd.com/law).

### *3.1 Concessions*

The Law on Foreign Concessions, (“the FC Law”) of 1993 governs concessions to foreign persons in the country and permits concessions to be granted for any type of activity, including industrial or natural resources exploration, provided such concessions are not otherwise prohibited by law. Infrastructure projects like transport or municipal concessions are not expressly mentioned in the FC Law.

Pursuant to the FC Law, concessions are granted on a competitive basis for a period of 5 to 40 years. While the FC Law contains a basic set of rules on tender procedures, these rules are very limited and the scope of their application unclear, arguably leaving room for arbitrary decisions by the authorities from case-to-case. The FC Law provides that concession agreements may only take the form of Build Operate Transfer arrangements, thus limiting flexibility of arrangements between the parties.

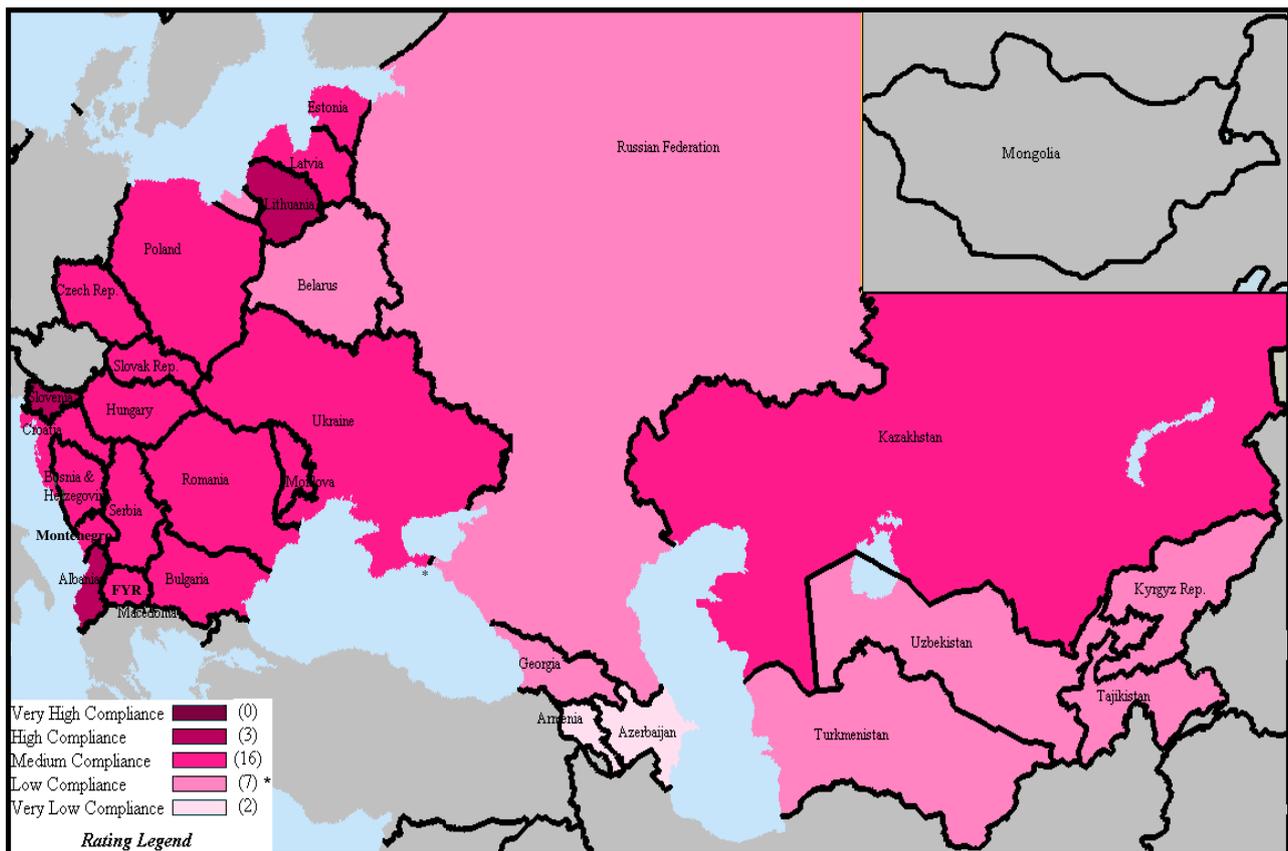
Concession is defined as "a permission by the state to carry out a specific type of business activity". The Contracting Authority is not clearly defined and sectors that may be subject to concessions are not specified and the selection procedure is not sufficiently developed. The FC Law refers to the Cabinet of Ministers’ decisions on this account but no publicly available document, other than in the oil and gas sector, can be identified. Disputes are to be resolved by the courts of Turkmenistan and there is no provision for international arbitration.

Notwithstanding these deficiencies, there are a number of positive elements. The FC Law declares that any amendments to the concession's terms may only be exercised by mutual agreement and provides for compensation where the concession is terminated by the grantor. However, the rule is somewhat declarative and vague and does not provide for any mechanism for determining such compensation. Also worth mentioning as a positive feature is a general principle of government assistance in "achieving objectives" of concession agreements. The FC Law, together with the recently enacted Hydrocarbon Resources Law, forms the basis for the government to grant concessions to several multinational energy companies to participate in the development of Turkmenistan's large oil and gas reserves through production sharing and joint venture agreements.

On balance, despite some positive components, the FC Law does not constitute a sufficiently solid legal basis for the development of Private Sector Participation (PSP) in infrastructure and utility services. There have been reports of plans to draft a new concessions act for but nothing of substance has appeared yet in this respect.

As can be seen from the charts below, the 2007/8 EBRD Assessment of Concessions Laws indicates that there is much room for improvement in all key elements of the regime of PSP in public infrastructure, works and services.

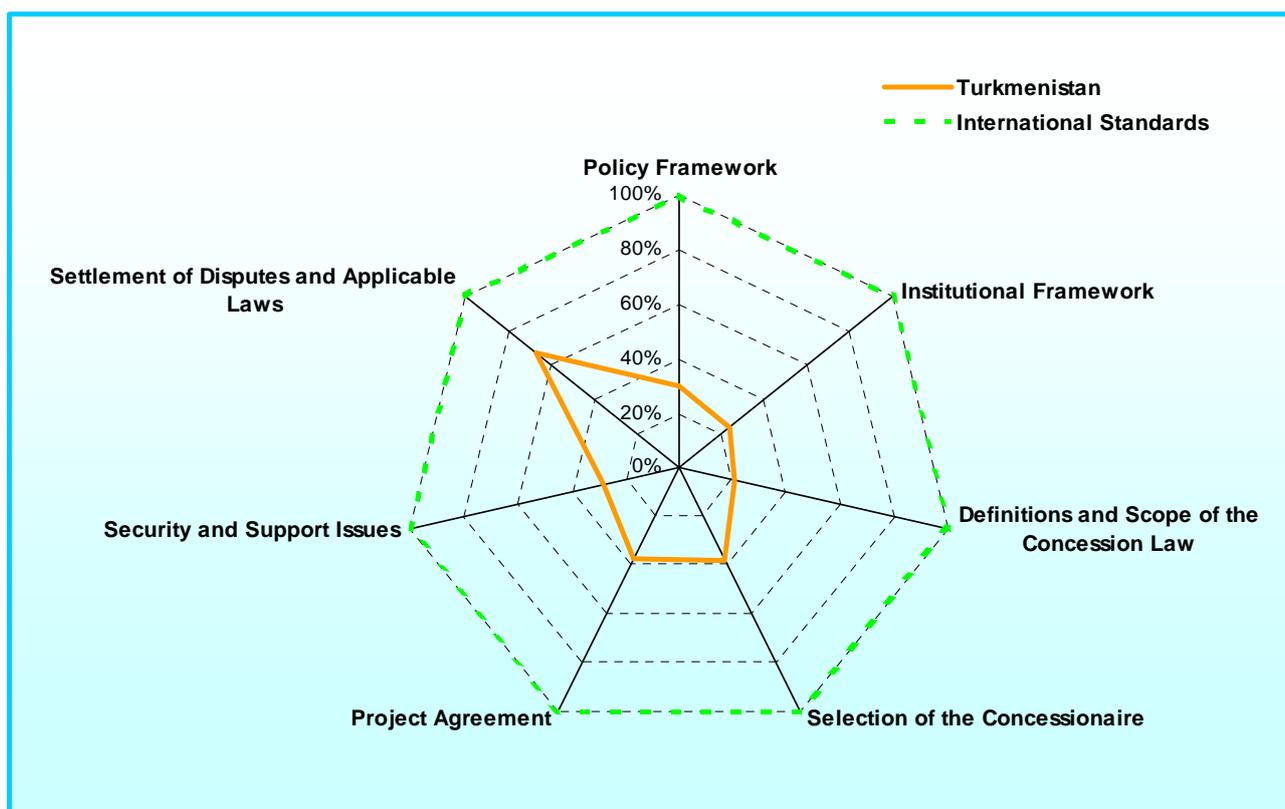
**Chart 3 - Quality of concessions related legislation in the EBRD countries of operations**



**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 UNCITRAL Model Legislative Provisions on Privately Financed Infrastructure Projects. The asterisk indicates in which category Turkmenistan ranks.

**Source:** EBRD concessions sector assessment 2007/08

Chart 4 - Quality of concession legislation –Turkmenistan (2007/8)



*Note:* the extremity of each axis represents an ideal score in line with international standards such as the UNCITRAL Legislative Guide for Privately Financed Infrastructure projects. The fuller the ‘web’, the more closely concessions laws of the country approximate these standards.

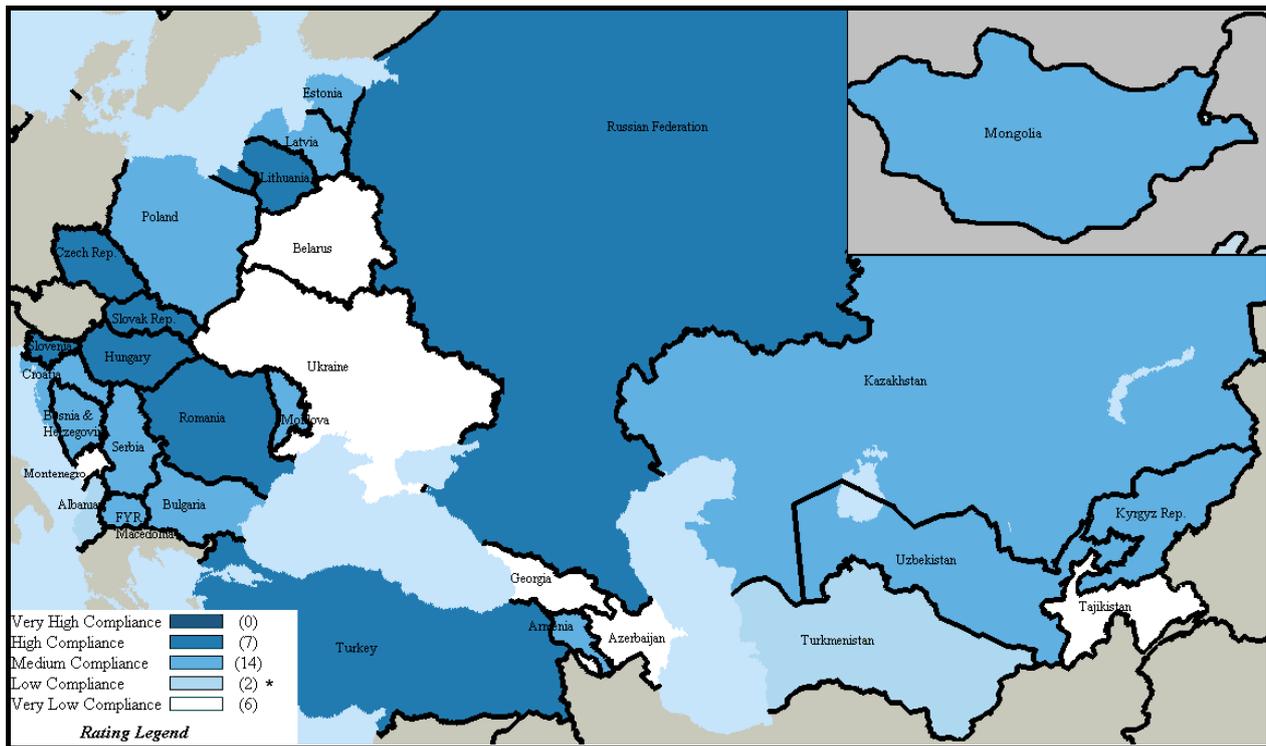
*Source:* EBRD Concessions Sector Assessment 2007/8

### 3.2. Corporate Governance

The principal legislation on corporate governance is contained in the Enterprise Law of Turkmenistan, dated 15 June 2000 and the Joint Stock Companies (JSC) Law of Turkmenistan, dated 23 November 1999. The JSC Law provides the basic legal framework for the establishment, functioning, re-organisation and liquidation of joint stock companies and the rights and duties of shareholders. Turkmenistan does not have a voluntary national code of corporate governance good practice.

According to the results of EBRD’s 2007 Corporate Governance Sector Assessment through which the quality of corporate governance legislation in force in November 2007 was assessed, Turkmenistan was assessed as being in “low compliance” with the OECD Principles of Corporate Governance, showing a number of substantial shortcomings especially on disclosure and transparency, and equitable treatment of shareholders (see chart 6 below). Among the major flaws highlighted by the assessment, were the weak disclosure and reporting requirements, the lack of protection for minority shareholders, the absence of specific regulation on related party transactions and the weak regulation of conflicts of interest.

**Chart 5 - Quality of corporate governance legislation in the EBRD countries of operations**



*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 Turkmenistan ranks.*

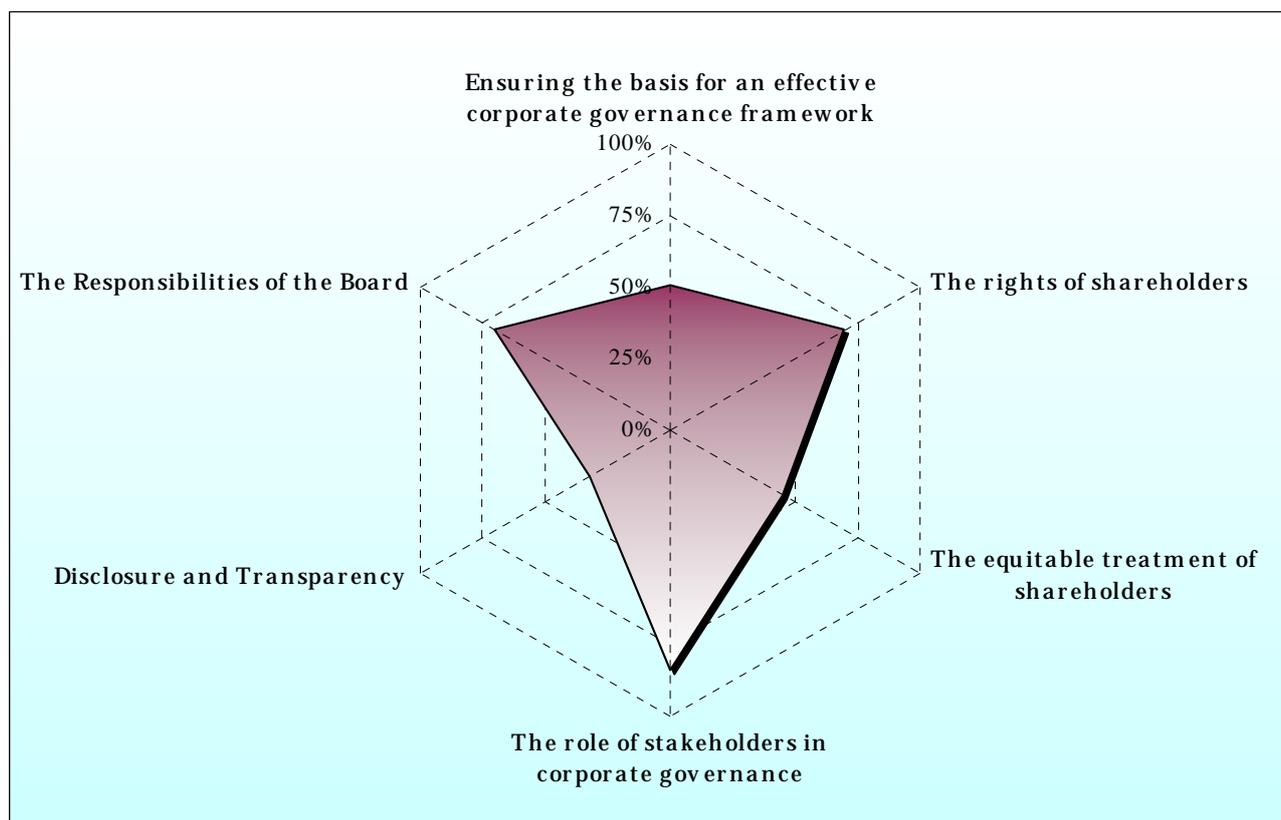
*Source: EBRD corporate governance sector assessment 2007*

At a broader level dialogue between the government and the private sector on corporate governance improvements, generally accepted as essential for the development of a sound and effective legal framework, is absent in Turkmenistan. Starting a constructive dialogue with the private sector and building up consensus for a constructive reform programme which improves the legislation in line with international standards should be a priority action for the government.

### 3.3. *Insolvency*

A complete assessment of all insolvency laws in the EBRD’s countries of operations, including Turkmenistan, was completed in 2009. The general insolvency assessment indicates that the Turkmen laws “on the books” are in very low compliance with recognised international standards of best practice (see Charts 7 and 8 below).

**Chart 6 - Quality of corporate governance legislation in Turkmenistan (2007)**



*Note:* The extremity of each axis represents an ideal score, i.e., corresponding to OECD Principles of Corporate Governance. The fuller the 'web', the more closely the corporate governance laws of the country approximate these principles

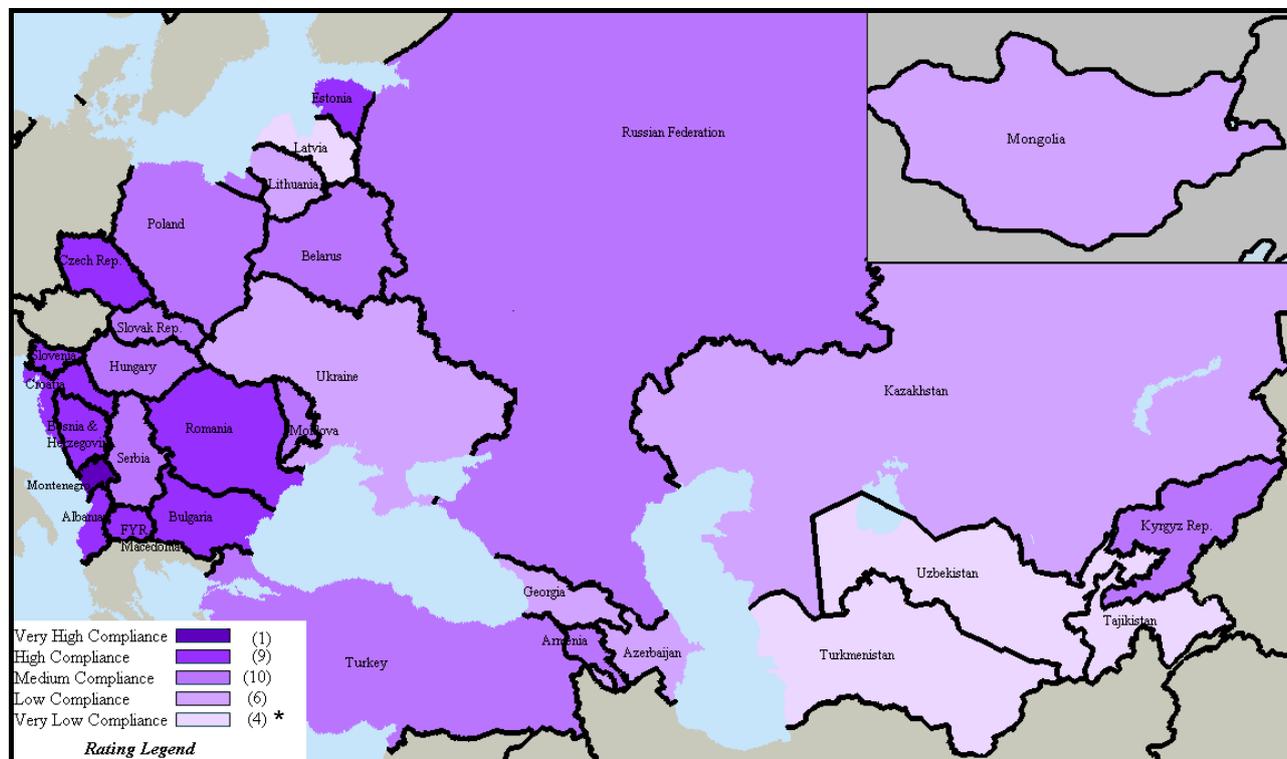
*Source:* EBRD Corporate Governance Sector Assessment, 2008 assessment

The law, although surprisingly clear and strong in some respects, is rudimentary and seriously deficient in many areas as, for example:

- Vague financial condition criteria.
- Inadequate stay/suspension of actions/proceedings against a debtor enterprise in respect of which a case has been opened.
- Inadequate provisions relating to the hearing and determination of applications to open a case under the law.
- Absence of any statement regarding the effect of the opening of an insolvency case in respect of secured creditors and owners of property used, occupied or in the possession of the debtor.
- Absence of notice to creditors of the opening of an insolvency case.
- Absence of any qualifications for insolvency administrators.
- Absence of any provision for the removal of an insolvency administrator.
- Absence of any provisions relating to the provision of information by the debtor and third parties concerning the property and financial affairs of the debtor.
- Absence of a provision permitting set off.
- The complete absence of any provisions dealing with the avoidance of pre-bankruptcy transactions of the debtor.
- Inadequate provisions relating to the representation of creditors in the conduct of an insolvency administration.

- Inadequate controls and safeguards concerning the reorganisation process.  
Absence of a provision concerning the discharge of debts upon the completion of a case of insolvency.

**Chart 8 – Quality of Insolvency legislation in the EBRD countries of operations.**

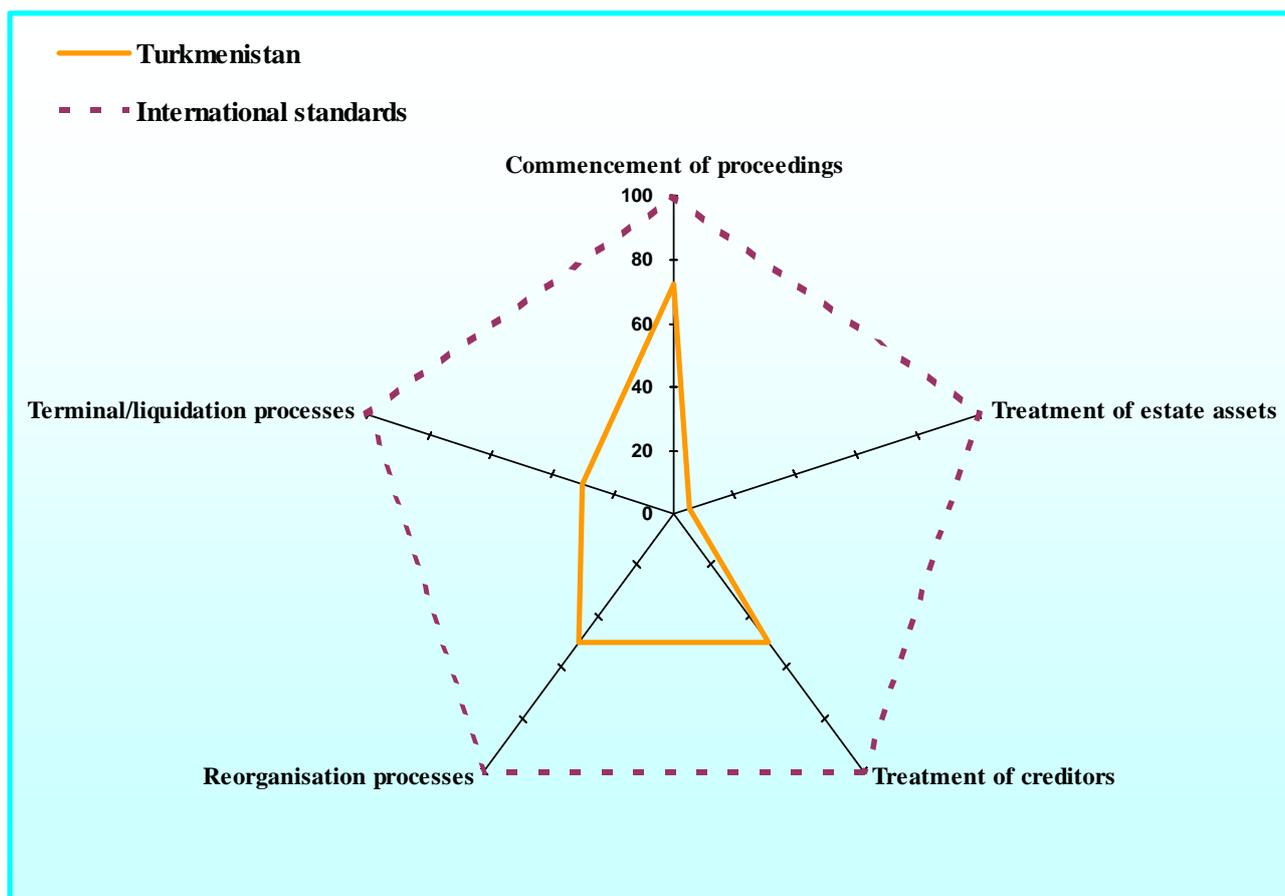


**Note:** The various categories indicate the level of compliance of each country’s legislation (the “laws on the books”) with international standards, such as the World Bank’s Principles and Guidelines for Effective Insolvency and Creditor Rights Systems, the UNCITRAL Working Group on Legislative Guidelines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

Source: EBRD Insolvency Sector Assessment, 2009

The assessment included a special part (part F) on the law relating to insolvency office holders (trustees, administrators etc.). The assessment in this area was based upon the EBRD Office Holder Principles (‘the principles’) that were developed in 2007. It is an important area for assessment since in almost every case the respective laws of the countries that are assessed require the appointment of an office holder to administer the case. The quality of insolvency office holders, their appointment and supervision may have a crucial impact on efficient implementation of the law. This area was therefore selected to be assessed in depth and rated separately. The law is totally inadequate in this area. There are practically no provisions directed at insolvency office holders.

Chart 7- Quality of insolvency legislation in Turkmenistan (2009)



*Note:* The extremity of each axis represents an ideal score, i.e. corresponding to international standards such as the World Bank's Principles and Guidelines for Effective Insolvency and Creditor Rights Systems, the UNCITRAL Working Group's "Legislative Guidelines for Insolvency Law", and others.

*Source:* EBRD Insolvency Sector Assessment, 2009

### 3.4. Secured Transactions

Security rights on movable and immovable assets in Turkmenistan are governed by the Civil Code of 1 December 1998 (arts 267-299, 325-329), enacted on 1 March 1999, and the Law on Pledge (Pledge Law) of 1 October 1993. The Pledge Law can only apply to the extent that it does not contradict the Civil Code. The Civil Code primarily covers security over immovable assets (mortgages), possessory pledge (i.e. when the debtor must transfer possession of the collateral to the creditor or a third party) and also the rules of enforcement. The Pledge Law provides more detailed provisions on non-possessory charges and envisages the establishment of a registration system through which non-possessory charges would be publicised. Despite attempts to create a modern system for secured transactions, the legal regime remains very limited in many respects. EBRD is not aware of recent attempts to modernise the legal framework, although the current developments of micro and SME lending (assisted by organisations such as the EBRD) may create momentum for such reform.

Current issues include the requirement that the collateral must be specifically identified in the charge agreement, together with its value and the location of the assets. When inventory is offered as collateral, changes in the composition is only allowed providing the assets' total value does not fall below the amount agreed in the charge agreement. This makes security over inventory impractical and, thus, of limited use.

Formalities of creation are complex and slightly confused. The law provides that the charge agreement must be in writing and subject to authentication and registration at a notary office. However, as implementing rules were lacking at first, notaries did not accept applications. A Presidential Decree issued in December 1997 introduced rules and fixed fees but these are considered to be prohibitively high. Furthermore, notarisation requires presentation of many documents and titles as well as the establishment of an inventory, and this is bound to make the process slow and subject to delays. After notarial authentication of the charge agreement, the agreement must be registered, depending on the type of charge. It was probably envisaged that notaries could run a general registration system in parallel with specific asset-based registries. However, this system was never put in place.

Enforcement remains a challenging process for secured creditors. Enforcement can be initiated either by way of inscription of execution by public notary, or on the basis of court decision (judgement), followed by realisation by a court enforcement officer. In the first case, the chargeholder must submit the notarised charge agreement to a notary public who is authorised to execute an execution inscription on it, in order for realisation to proceed. A state duty of 2% of the claimed amount is charged for execution of the inscription of execution by a public notary. In the case of enforcement via court, the state charges a duty of 10% of secured debt. Whatever the chosen route, realisation may only be carried out by way of public auction at the State Commodity and Raw Materials Exchange of Turkmenistan. A remuneration of 5% of the recovered sum has to be paid to the enforcement officer. One of the problems faced in enforcement is the obstruction that the debtor could exercise - by challenging the inscription of execution executed by a public notary or even the judgement, in which case the court could decide to suspend the enforcement. This is common practice. On enforcement (whether or not the debtor is insolvent), the creditor will be satisfied after alimony claims and salary arrears, as well as tax claims. All this makes the recovery of the secured debt highly uncertain.

Turkmenistan has not followed the pace of reform that many neighbouring countries in central Asia have taken in the last decade, started by Kazakhstan, the Kyrgyz Republic and also Russia. As a result, it is equipped with a very rudimentary legal framework for secured lending, which does not encourage sound banking practices.

### 3.5. *Securities markets*

The basic legislation on the securities market is comprised of the Law on Securities and Stock Exchanges, dated 28 December 1993; the Regulation on Securities and Stock Exchanges, approved by the Presidential Decree No. 1576 dated 22 November 1993, which in turn underpin the Rules of Securities Issue and Registration, the Rules of Securities Transactions Conduct and Registration, and the Licensing Rules for Stock Exchange Activity at Securities Market, all approved by the Ministry of Economy and Finance on 24 December 1993.

The Law on Securities and Stock Exchanges sets uniform principles of securities issue and circulation, the general principles of stock exchanges and investment institutions operations and regulates the rights and obligations of securities market participants. The Regulation on Securities and Stock Exchanges was approved before the enactment of the Law on Securities and is practically identical to the Law on Securities. No amendments to securities and stock exchange legal framework have been made since established. The securities market regulator is the Ministry of Economy and Finance, which is competent for registration of securities, supervision on issuance and circulation of securities and regulation and supervision over the insurance activities. The Central Bank of Turkmenistan is competent for registration of securities issued by the commercial banks. There are no stock exchanges or collective investment schemes in the country and there is no active over-the-counter trading.

In 2007 EBRD benchmarked securities markets legislation against the “Objectives and Principles of Securities Regulation” published by IOSCO, finding the national framework in “very low compliance” with international standards (see charts below). The assessment showed a framework in urgent need of reform in all elements examined, the only exception being “Accounting”, because of the 1996 Law “on Accounting in Turkmenistan”. In order to understand how securities market legislation works in practice, in the same year the EBRD undertook a Legal Indicator Survey asking practitioners in the region to comment on a hypothetical case study. The Survey concentrated on effectiveness of prospectus disclosure requirements, private and public enforcement mechanisms and authority of the market regulator. Effectiveness of securities markets legislation is perceived as very low as the country lacks a functioning stock exchange and an IPO has yet to be launched. There is no disclosure practice based on prospectus and financial reporting is made in accordance with national standards, which are not compliant with international standards. The functions of the Ministry of Economy and Finance as securities markets regulator extends beyond mere supervision, with the Ministry empowered to enquire into the merits of an issue in certain cases. This form of control is too tight to allow a market to develop effectively.

Going forward, commencing constructive dialogue with the private sector and building up consensus for constructive reform, improving legislation in line with international standards, should be a priority action of the government.

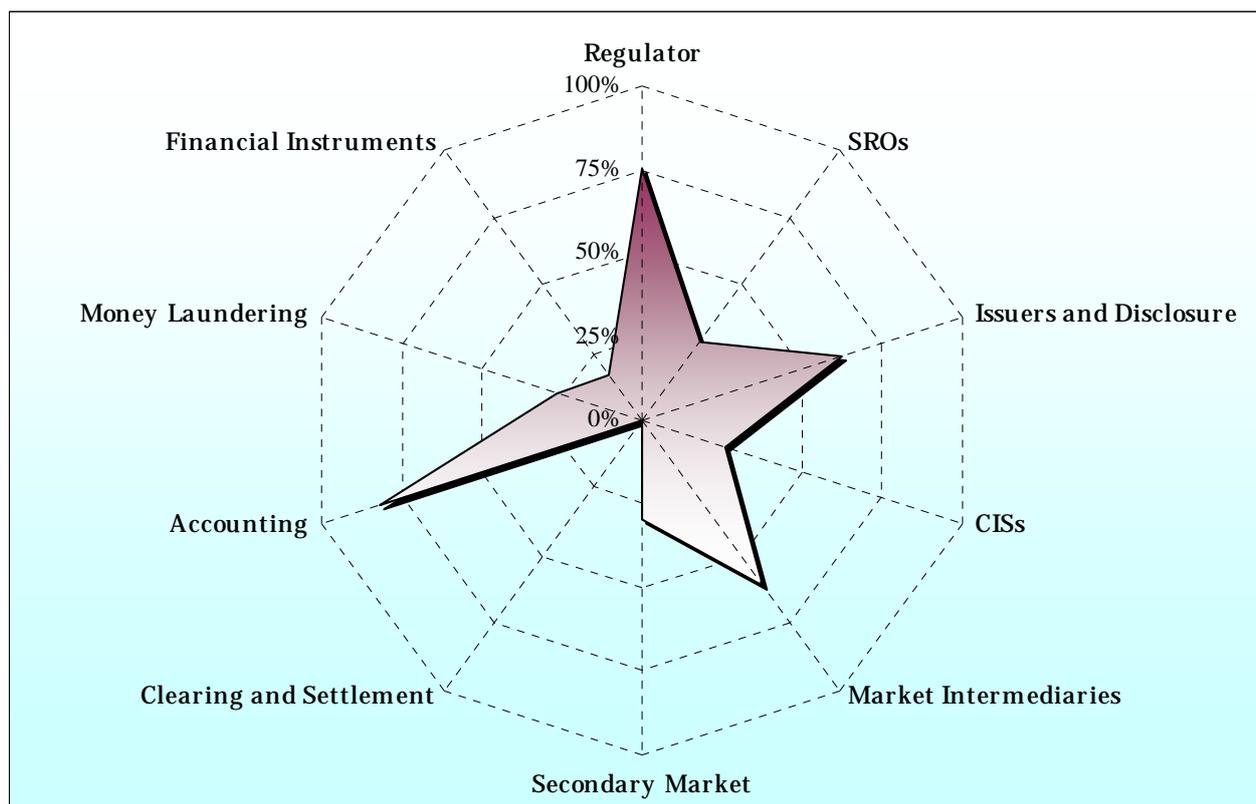
**Chart 9 – Quality of securities market legislation in the EBRD countries of operations**



**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 Turkmenistna ranks.

**Source:** Securities markets legislation assessment 2007

**Chart 10 - Quality of securities markets legislation in Turkmenistan (2007)**



*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 securities markets laws approximate these standards.

*Source:* EBRD securities markets sector assessment 2007

### 3.6 Telecommunications

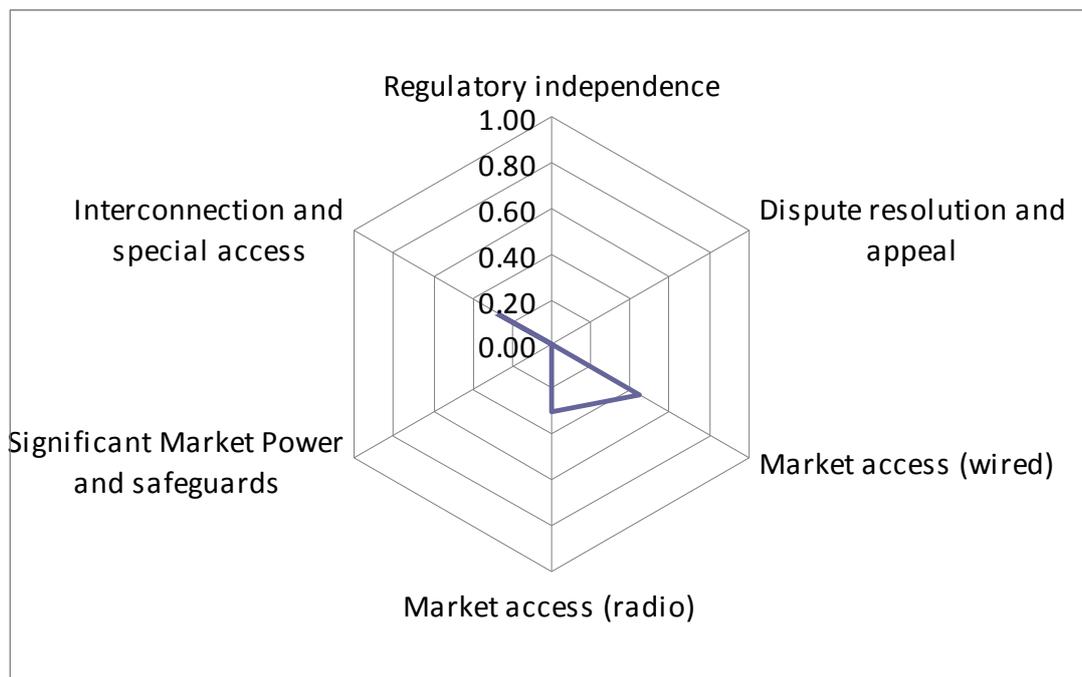
The Ministry of Communications (the ‘Ministry’) is the central authority in the communications sector in Turkmenistan, being regulator and operator, controlling eight State Enterprises in the post and communications sector. Law is made by the Cabinet of Ministers and the Deputy Chairman of the Cabinet of Ministers (Deputy Prime Minister) has overall responsibility for the sector. The President and the Cabinet of Ministers defines policy for the sector and the Ministry is tasked with its implementation. Under the 2000 Law on Communications, the Ministry provides proposals for the development of the sector and is the regulatory body that regulates the co-operation between operators. It also receives applications for, and issues, licences (under the “Law on Regulation of Licences”), carries out spectrum management (under “Law on Frequency Management”) and establishes tariffs caps for residential line rentals and local calls. The General Director of Turkmen Telecom reports to the Cabinet of Ministers, as does the Minister for Communications. Thus there is no real concept of separation of powers as understood under modern regulatory practices and political interference is inevitable under the vertical structure of Ministry, Regulator and State owned operator.

There is a tight system of control in the sector in Turkmenistan, right through from licence application to market operation. Each licence is for a fixed term of three years. There are currently understood to be 32 different types of licence in the sector, issued by the Ministry, though there appear to be efforts to revise the number of licences required to take account of new technologies and new services. There are no exclusive rights explicitly defined and where there is only one licence holder this is understood to be because no other operator has applied for a licence.

State-owned TurkmenTelecom runs fixed line services nationally, except in the capital, which is operated by another state company, Ashgabat City Network. Technically speaking anyone is supposedly allowed to offer Internet services provided they have a licence, but at present there is only one licence holder, TurkmenTelecom. There are two mobile operators, Altyn Asyr (100% government controlled) is understood to have around 200,000 subscribers and MTS (100% privately owned) has just in excess of 1 million subscribers.

Tariffs are set by the operators themselves. However, before a licence is issued, the Ministry examines the tariff proposals, to see that certain tariffs are not exceeded. If a private operator wants to change retail tariffs or interconnection charges, they are understood to need to consult the Ministry. Tariff rebalancing has been discussed but not implemented.

**Chart 11 - Quality of telecommunications regulatory framework in Turkmenistan (2008)**



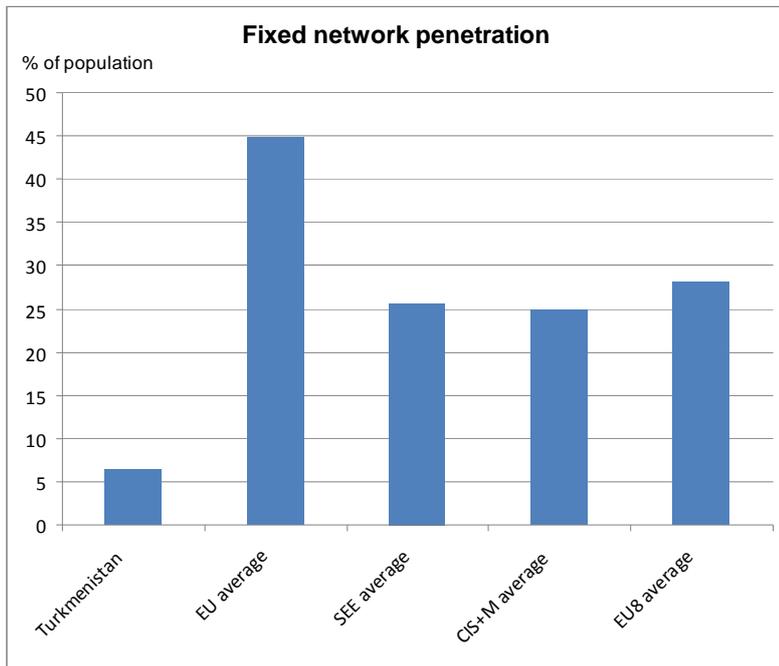
*Note:* The diagram shows the combined quality of institutional framework, market access and operational environment when benchmarked against international standards issued by the WTO and the European Union. The extremity of each axis represents an ideal score of 100 per cent, that is, full compliance with international standards. The fuller the “web”, the closer the overall telecommunications regulatory framework of the country approximates these standards.

In a 2008 Communications Sector Assessment undertaken by EBRD, Turkmenistan was assessed as having “Low compliance” when measured against benchmarks of international best practice, scoring low in all categories assessed (see charts above).

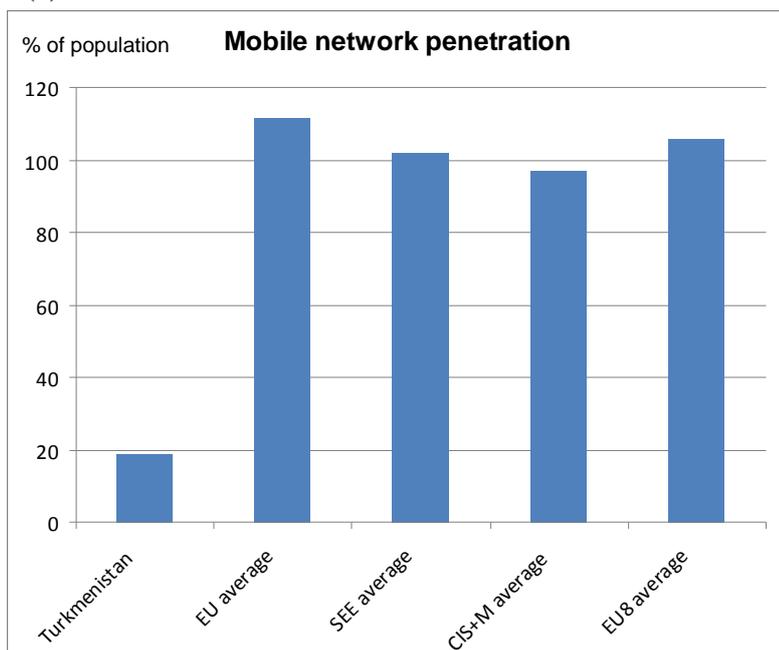
Going forward significant legal, regulatory and institutional reform will be necessary in the sector for Turkmenistan to exploit the potential the sector has to benefit the economy and its citizens. The relative success of private operations in the mobile sector should encourage the government to grant a third mobile licence (to a private investor) and/or move the state-owned mobile operator towards privatisation or a strategic partnership. On both the fixed and wireless side, a firm strategy for the exploitation of broadband technology based on liberalisation should be developed and implemented without delay. Tariff rebalancing on the fixed side and general overhaul of the licensing regime is critical to opening up the sector to appropriate levels of investment and the government should make their implementation a priority.

**Chart 12. Key indicators for Turkmenistan telecommunications market (2008)**

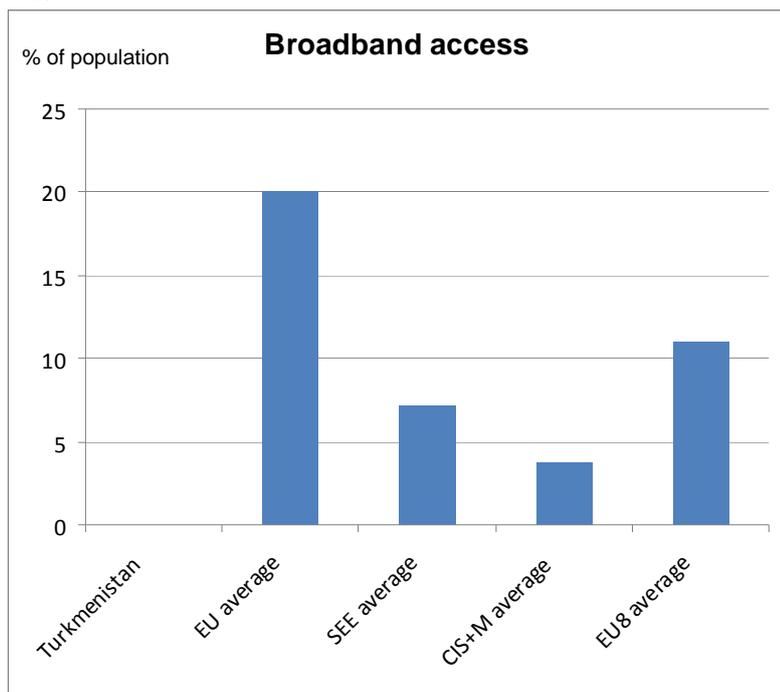
**10(a) Fixed Network Penetration**



**10(b) Mobile Network Penetration**



### 10(c) Broadband Network Penetration



*Note:* Key indicators for Turkmenistan provide the fixed network penetration defined as active subscriber lines as a percentage of population, mobile network penetration defined as active pre- and post-paid subscribers as a percentage of population and the broadband network penetration defined as the number of access subscribers with speeds of 144k/bits or more as a percentage of population (broadband Network Penetration less than 1% is not shown on this chart).

*Source:* EBRD Telecommunications Regulatory Assessment, 2008