Comments are welcome: please provide comments to cignag@ebrd.com

European Bank
for Reconstruction and Development

Corporate Governance in Transition Economies

Russia Country Report

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With the assistance of:
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The report is based on information available at the end of April 2015.

If you believe that the information has changed or is incorrect, please contact Gian Piero Cigna at cignag@ebrd.com

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This Report – along with all other country reports prepared within this initiative – is available at: http://www.ebrd.com/what-we-do/sectors/legal-reform/corporate-governance/sector-assessment.html

Foreword

As part of its Legal Transition Programme, the European Bank for Reconstruction and Development ("EBRD") has been assessing the state of legal transition in its countries of operations. These assessments provide an analysis of the progress of reform and identify gaps and future reform needs, as well as strengths and opportunities.

In 2012, the Legal Transition team within the EBRD Office of the General Counsel (LTT) developed with the Assistance of Nestor Advisors a methodology for assessing corporate governance frameworks and the governance practices in the EBRD countries of operations. This assessment was implemented in 2014-2015 (the "Assessment").

The Assessment aims at measuring the state of play (status, gaps between local laws/regulations and international standards, effectiveness of implementation) in the area of corporate governance

The Assessment is meant to provide for (i) a comparative analysis of both the quality and effectiveness of national corporate governance legislation (including voluntary codes); (ii) a basis to assess key corporate governance practices of companies against the national legislation; (iii) an understanding whether the legal framework is coupled with proper enforcement mechanisms (e.g., sanctions) and/or with authorities able to ensure proper implementation; (iv) a support to highlight which are the major weaknesses that should be tackled by companies and legislators for improving the national corporate governance framework; and (v) a tool which will enable the EBRD to establish "reference points" enabling comparison across countries.

This country report is part of a series of 34 country reports. A general report synthesising all countries will close the Assessment.

Methodology

This Assessment is based on a methodology designed to measure the quality of legislation in relation to best practices requirements and the effectiveness of its implementation as evidenced by companies' disclosure, also taking into consideration the capacity of the institutional framework (e.g., courts, regulators) to sustain quality governance. The analytical grid developed for assessing the governance framework is based on international recognised best-practice benchmarks (e.g., OECD Corporate Governance Principles, Development Financial Institutions, EBRD, IFC and World Bank ROSC governance methodologies). The methodology is applied identically across all the countries reviewed. The process for gathering, analysing and reporting information is applied identically for each of the countries assessed, which allows comparing countries to each other across a long a set of benchmarking points.

For the purpose of the Assessment, the corporate governance framework and the practices were divided in five key areas: (i) Structure and Functioning of the Board; (ii) Transparency and Disclosure of company information; (iii) Internal Control; (iv) Rights of Shareholders; and (v) Stakeholders and Institutions. Each of these key areas is further divided in sections (for instance, the area "Structure and Functioning of the Board" is divided in five sections: Board composition; Gender diversity at the board; Independent directors; Board effectiveness; and Responsibilities of the board). Each section is further divided in subsections (for instance, the section "Independent Directors" is divided in three subsections: "Requirement to have independent directors"; "Definition of Independence"; and "Disclosed practices").

The assessment started by sending a questionnaire to law firms, audit firms, national regulator(s), ten largest (listed) companies, and stock exchange(s) in each country. Questions were different according to the respondents, which were asked to provide information on the legislation and on how they believe the legislation is implemented.

Responses were assigned to the corresponding subsection(s) and validated by the EBRD corporate governance specialists by looking at the applicable framework and at the disclosure offered by the ten largest (listed) companies in each country. In this respect, the working hypothesis was that the ten largest listed companies are those offering the best disclosure in each country. As such, we presumed that when certain practices were not disclosed by them, they were unlikely to be disclosed by smaller or unlisted companies. The ten largest companies were identified according to their market capitalisation. When a country did not have a stock exchange, there were less than ten listed issuers or there were no data on capitalisation of issuers, the ten largest companies were identified according to their revenues and size of the labour force. In case the largest companies were mostly of one sector (e.g., financial institutions), then the sample of ten companies was corrected to reflect other sectors of the economy.

The validation of responses was undertaken by the corporate governance specialists within the Legal Transition Team through desktop research. This research was conducted both on legislation and on the practices disclosed by the largest (listed) companies (e.g., companies' websites, annual reports, stock exchanges database etc.). In addition, the relevant reports by international financial institutions (e.g., IMF, World Bank, IFC, Transparency International, etc.) were analysed and taken into consideration. Answers received by respondents that were not grounded by specific references to legislation or consistent with the disclosed practices were not taken into consideration.

Following the validation process, each subsection was compiled by adding specific references to legislation and practices. Conclusions were then formulated for each subsection, each rated as per their adherence to international governance standards. The score ranges from 1 (very weak) to 5 (strong). The rating for each section was then calculated by averaging the ratings of the subsections.

Because understanding corporate governance requires a "holistic perspective", where each component needs to have a place in the overall picture – pretty much like a puzzle - in case one of the subsection was rated "weak" or "very weak", the resulting average was decreased by 0.2; in case more than one subsection was rated “weak” or “very weak”, the resulting average was decreased by 0.5. This is because if just one component is not fitting well with the others, then all others are weakened. Similarly, the overall strength diminishes if there are more weak components.

Conversely, in order for the framework to be strong, all components need to be well fitting with each other. Hence, in case all subsections were scored “moderately strong” or “strong”, then the resulting average was increased by 0.5. However, this “positive” adjustment was used with some care as the assessment looked at the top ten largest companies in the country, hence findings tended to be often overly optimistic.

Key areas were then rated according to the same criteria.

The ratings are presented through the colours detailed in the box below and they demonstrate the adequacy or need of reform in respect to each governance area and section.

Rating:

“Strong to very strong” (DARK GREEN) - The corporate governance framework / related practices of companies are fit-for-purpose and consistent with best practice.

“Moderately strong” (LIGHT GREEN) - Most of the corporate governance framework / related practices of companies are fit-for-purpose but further reform is needed on some aspects.

“Fair” (YELLOW) - The corporate governance framework / related practices of companies present some elements of good practice, but there are a few critical issues suggesting that overall the system should be assessed with a view of reform.

“Weak” (ORANGE) - The corporate governance framework / related practices of companies may present few elements of good practice, but overall the system is in need of reform.

“Very weak” (RED) - The corporate governance framework / related practices of companies present significant risks and the system is in need of significant reform.

We believe corporate governance cannot be captured and measured simply by numerical values. Hence, alongside the “quantitative” assessment obtained according to the methodology described above, a “qualitative” assessment was also undertaken, by classifying our findings for each section as “strengths” and “weaknesses”. Because understanding corporate governance requires a “holistic perspective”, when the “quantitative” assessment was finalised, the assessment team compared it with the “qualitative” assessment, and when any inconsistency (i.e. material weaknesses or strengths) was noticed, the average scores of the sections were adjusted by up to ±0.5.

A preliminary version of the Assessment was made public for consultation. The comments and corrections received during the process were analysed by the corporate governance specialists. When confirmed, the corrections were reflected in the final ratings and in this Assessment.

Overview

Legislative framework

The primary sources of corporate governance legislation in Russia are the Law on Joint Stock Companies, the Law on the Securities Market, the Law on Countering the Illegal Use of Insider Information and Market Manipulation, the Regulation on Information Disclosure by Issuers of Securities and the Law on Banks and Banking Activity. In 2001, a Corporate Governance Code was adopted to be implemented pursuant to the so-called "*comply or explain*" approach. The Code was revised in 2013 and a new Code was enacted in 2014. So far, there has been little or no monitoring on how companies comply with the Code, but the Central Bank of Russia has committed to actively oversee the implementation of the new Code. Results of these efforts are yet to be reported.

Structure and functioning of the board

Joint stock companies (JSC) in Russia are organised under a one-tier system, where the role of CEO and chair of the board must be separate. Most of the board of the largest listed companies appears to be well sized, but in a few cases the board appears to be very large. Evidence has shown that smaller board tend to perform better. Legal entities cannot be board members. The law does not clearly assign to the board all key functions; specifically, the law is silent on board's strategic role in balancing risk and reward, and on oversight of management. Further, the board does not have authority by law to appoint and remove executives, unless so provided by the Articles. Companies are required to have independent directors on their board, and most of the ten largest listed companies appear to have them on board. The Corporate Governance Code includes a definition of independence; however, there are other definitions provided in different laws, which does not help clarity. All ten largest listed companies have created an audit committee, which in most cases is made by a majority of independent directors. Eight companies also have a remuneration and a nomination committee. Boards seem to have a diversified mix of skills, however the qualifications of audit committee members are often not appropriate for the functions of the committee. Gender diversity at the board appears limited.

Transparency and disclosure

The law requires companies to prepare annual reports including financial and non-financial information and all ten largest listed companies published comprehensive annual reports with information on governance and ownership structures. However, only five of them provided a *comply or explain* statement. Overall, disclosure is very formalistic in nature: listed companies appear to disclose the contents of their internal documents, but not the corporate governance practices in place. Very often, explanations are minimal and not convincing. Most of the largest listed companies disclose having independent directors on their boards but only in very few cases there are some (limited) explanations on the ground upon which these directors are considered independent. In most cases, it is impossible to understand if they are really independent. Companies are required to disclose financial information in line with IFRS, and all ten largest listed companies appear to comply with this requirement. The law requires companies to disclose price sensitive events, as well as the initiation of any insolvency or restructuring proceedings. Breach of disclosure obligations is subject to sanctions.

Internal Control

Joint stock companies are required to appoint an independent external auditor; listed companies are also required to publish the auditor's name and report on their website, and all ten largest listed companies appear to comply with this requirement. Auditors are allowed to provide non-auditing services. This should be carefully monitored as it might compromise the auditors' independence. Unfortunately, disclosure on this matter is very limited. Listed companies and banks are required to set up internal audit departments, and the majority of the largest companies appear to comply. Banks are not required to establish a standalone compliance function. As mentioned above, listed companies are required to set up an audit committee, made up of – at least - a majority of independent members, and a revision commission, which is responsible for the oversight of the company's financial and business activities. We have doubts about the effectiveness of the revision commission. In practice, the large majority of companies in our sample have established both an audit committee and a revision commission, but only in two cases the audit committee is entirely made up of independent board members. The large majority of the top ten largest companies have adopted a code of ethics, however only in one case it is clearly disclosed who the officer in charge of monitoring compliance is. This is a key issue as the value of the code is in its implementation. There is no comprehensive legislation protecting whistle-blowers. Regulation on related party transactions appears to be limited, and not fully aligned with best practices. The regulation on conflict of interests also appears to be limited.

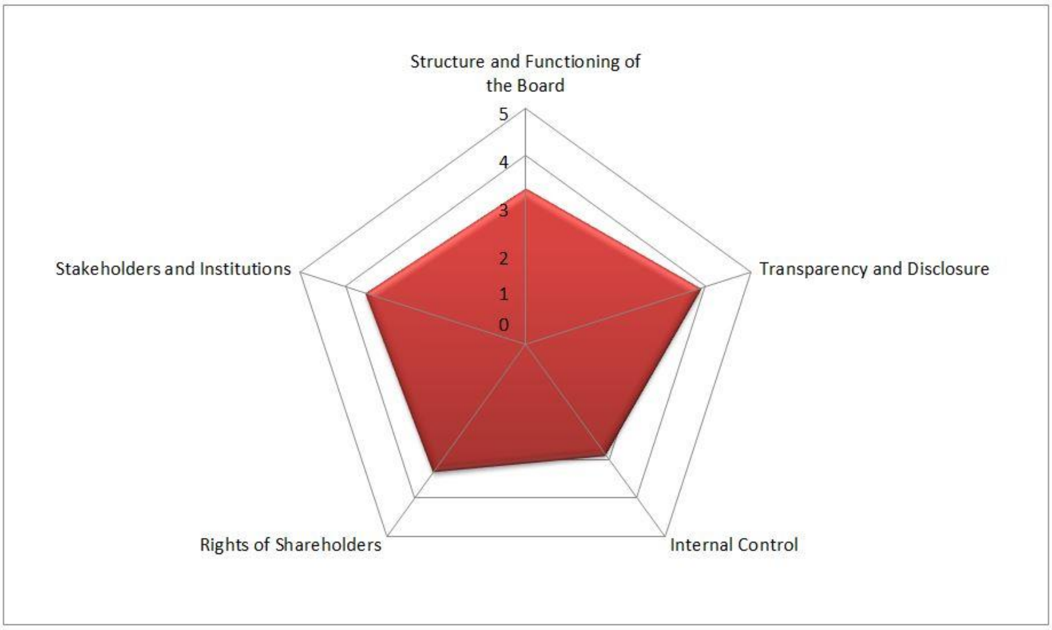
Right of shareholders

Minority shareholders are entitled to call a general shareholders' meeting (GSM) and put additional items on the GSM's agenda. However, it is not clear if shareholders have the right to ask questions at the GSM. Pre-emptive rights are provided by law in case of capital increase, but no supermajority is required for waiving them. Cumulative voting is provided by law. Two-thirds qualified majority vote is required to amend the articles of association and to approve other key decisions such as mergers, reorganisations or winding up procedures. Insider trading is prohibited by law, and violations of these provisions can lead to fines or imprisonment. Shareholders can file derivative suits on behalf of companies; however, there is limited (if any) case law on this matter, which may indicate that enforcement is difficult in practice. The law regulates registration of shareholding and shareholder agreements, which are considered enforceable Joint stock companies with more than fifty shareholders are required to maintain their share register with an external licenced registrar.

Institutional Framework

The Moscow Exchange is highly capitalised and very liquid. Trading is divided in five segments with different corporate governance requirements. To be listed in the First or Second Tier, companies must establish audit, nomination and remuneration committees, as well as prepare their financial statements in accordance with the IFRS. The website of the Moscow Exchange contains a comprehensive database of companies' financial and non-financial information, and the Exchange appears to be very active in promoting good corporate governance. The Russian Corporate Governance Code was developed in 2001 and was revised in 2014. All joint stock companies are recommended to implement the code's provisions, and all listed companies are required to include a "comply or explain" section in their annual reports. However, only five of the ten largest listed companies have disclosed a "comply or explain" statement. Most of the explanations provided are excessively formalistic, and make no significant reference to companies' current state of corporate governance practices. Indicators by international organisations point out that corruption remain a perceived concern.

Corporate Governance Legislation and Practices in Russia



Source: EBRD, Corporate Governance Assessment 2016

Note: The extremity of each axis represents an ideal score, i.e., corresponding to the standards set forth in best practices and international standards (e.g., OECD Corporate Governance Principles). The fuller the 'web', the closer the corporate governance legislation and practices of the country approximates best practices.

Key: Very weak: 1 / Weak: 2 / Fair: 3 / Moderately Strong: 4 / Strong to very strong: 5

<table>
<tr><th>Key Areas and Rating</th><th>Strengths and Weaknesses</th></tr>
<tr><td>1. Structure and Functioning of the Board
Fair</td><td>Joint stock companies in Russia are organised under a one-tier system, where the role of CEO and chair of the board must be separate. Most of the board of the largest listed companies appears to be well sized, but in a few cases the board appears to be very large. Evidence has shown that smaller board tend to perform better.
Legal entities cannot be board members.
The law does not clearly assign to the board all key functions; specifically, the law is silent on board's strategic role in balancing risk and reward, and on oversight of management. The board does not have authority by law to appoint and remove executives, unless so provided by the Articles.
Companies are required to have independent directors on their board, and most of the companies appear to have them on board. The Corporate Governance Code includes a definition of independence; however, there are other definitions provided in different laws, which does not help clarity. In practice, only in very few cases there are some (limited) explanations on the ground upon which directors are considered independent. In most cases, companies just name a director as independent without providing any explanation.
All ten largest listed companies have created an audit committee, which in most cases is made by a majority of independent directors. Eight companies have also created a remuneration and a nomination committee. Boards seem to have a diversified mix of skills, however the qualifications of audit committee's members are often not appropriate for the functions of the committee.
Gender diversity at the board of the ten largest listed companies appears to be limited.
Directors' fiduciary duties, liability of board members; conflict of interest and related party transactions are regulated by law.</td></tr>
<tr><td>1.1. Board Composition
Fair</td><td>Strengths:
The law requires the roles of the CEO and Chairman to be split.
Legal entities cannot serve as board members.
The boards of the ten largest companies appear to be well sized (9 to 13 members – average: 10.8 members). Note that one bank among the ten largest listed companies has 17 board members, which seems excessive.
The Corporate Governance Code recommends the board to be comprised of highly skilled individuals with experience relevant to the company's business and good reputation. In general, boards seem to have a diversified mix of skills,
An Order of the regulator requires companies listed at the highest (first) tier at stock exchange to establish at least three committees (i.e., nomination committee; remuneration committee; and audit committee). All ten largest listed companies have created an audit committee, and eight of them also have remuneration and nomination committees.
The same Order requires committees to be composed entirely of independent directors unless objective reasons advocate otherwise. In that case, at least the majority of members should be independent. In practice, it appears that the majority of the audit committees in our sample are made by a majority of independent directors (in two cases the audit committee is made entirely of independent directors).
The same Order requires that at least 1/5 - but no less than three members of the board - should be independent. The Corporate Governance Code recommends companies to have at least 1/3 of independent directors. Nine out of the ten largest listed companies disclose having independent directors on their boards (average in these boards: 42.34%). In at least two cases the independent directors are less than 1/3 of the board and in one case, independent directors are less than three.
Weaknesses:
The law does not foresee any specific qualifications for board members, chairman or committee members. Only the banking law requires boards of directors to have a high level of 'business reputation'.
The law does not give boards the authority to appoint executives. This authority stays with the general shareholders' meeting, unless differently provided by the Articles of Association.
Most of the largest listed companies disclose having independent directors on their boards but only in very few cases there are some (limited) explanations on the ground upon which these directors are considered independent. In most cases, it is impossible to understand if they are really independent.</td></tr>
<tr><td>1.2. Gender Diversity at the Board (6.76%)
Very weak</td><td>Strengths:
All ten largest listed companies disclose the composition of their boards.
It appears that there are 8 women on four boards: two in two companies, and one in the other four companies. The average of female representation on these boards is 11.26%.
In total, there are 8 women among the 108 board members of the top ten largest companies.
Overall, when counting all the ten companies in our sample, the average female representation falls to 6.76%.</td></tr>
</table>

Key Areas and Rating	Strengths and Weaknesses
1.3. Independent Directors *Moderately strong*	***Strengths:*** • *By Order of the regulator, in listed companies at least 1/5 of the board - but no less than three board members - should be independent. The Corporate Governance Code recommends all companies that at least 1/3 of board directors should be independent. Nine out of the ten largest listed companies disclose having independent directors on their boards: seven companies disclose that at least 1/3 of their board members are independent and two companies disclose having less than 1/3 of independent members. The average of independent directors in these boards is 42.34%. In at least one case, independent directors are less than three. One company does not disclose any information on this matter.* • *The Corporate Governance Code provides for a definition of independence that also includes positive criteria (i.e., what it is expected in practice from independent directors). This is a step in the right direction.* • *The majority of the audit committees in our sample are made by a majority of independent directors (in two cases the audit committee is made entirely of independent directors). In three cases, independent directors are a minority of the audit committee.* ***Weaknesses:*** • *Different definitions of independence can be found in several legal sources; this does not help clarity and makes it difficult for companies to report compliance.* • *Most of the largest listed companies disclose having independent directors on their boards but only in very few cases there are some (limited) explanations on the ground upon which these directors are considered independent. In most cases, it is impossible to understand if they are really independent.*
1.4. Board Effectiveness *Fair*	***Strengths:*** • *The law provides that the board should determine "the priority directions of the company's activities", which can be interpreted as strategic guidance.* • *As mentioned above, companies seeking to be listed at the stock exchange's first tier are required to establish at least three board committees: nomination, remuneration and audit. The Corporate Governance Code recommends all companies to establish these committees. All ten largest listed companies have created an audit committee, and eight of them also have remuneration and nomination committees.* • *The Corporate Governance Code recommends companies to have a corporate secretary. Eight out of the ten largest companies in the country disclose having a corporate secretary in place.* • *Our respondents believe that about half of the boards' discussion time is dedicated to strategic issues, whereas the other half is dedicated to operational issues.* ***Weaknesses:*** • *There is no consolidated practice of board evaluation. Only three among the ten largest companies disclosed having performed them, and this was likely influenced by their double listing at the London Stock Exchange.* • *The law includes a detailed list of board functions, but there is no clear reference to the role of the board in balancing the amount of risk the company is prepared to face in relation to its strategy (risk profile or appetite), or to the oversight of management.* • *The frequency of board meetings in person per year varies from 7 to 12, while the number of board meetings in absentia varies from 5 to 75. It is concerning that large listed companies reported 3, 6, or even 7 times more meetings in absentia than in person. Further, the high number of meetings can be an indication that the board is involved in operational matters. It is generally accepted that boards of directors that are suffering from 'information overload' regarding operational matters will find it harder to concentrate on major strategic issues.*
1.5. Responsibilities of the Board *Fair*	***Strengths:*** • *As mentioned above, the law stipulates that the board should perform a strategic guidance function. It is, however, silent on role of the board in balancing risk and reward in relation to strategy, and the oversight of management.* • *Seven among the ten largest listed companies disclosed in their annual reports that their boards are in charge of strategic planning.* • *The legal framework on directors' duties is well developed. Directors are obliged to act in the interest of the company and shareholders, exercising their rights and performing their duties reasonably and in good faith. Case law exemplifies instances when the duty of a director to act reasonably and in good faith is breached.* • *By law, company officers are responsible to the company and its shareholders for any harm inflicted by their actions.* ***Weaknesses:*** • *When the company has no more than 1,000 shareholders, the law allows boards to approve related party transactions with a simple majority. Board members holding an interest in these transactions must refrain from voting. If the number of shareholders exceeds 1,000, then the decision should be approved by a majority of independent directors with no interest in the transaction. Here, the definition of independence provided by law is quite narrow. Further, directors are not required to recuse themselves from participating in the deliberations on a particular agenda item when they have a conflict of interest. If the value of the transaction is more than 2% of the book value of the company's assets, the law foresees that the decision shall be taken by a simple majority of not-interested shareholders at the general shareholders' meeting.* • *It is not clear why the audit committee (which is required for most listed companies) is not assigned with competence over related party transactions.*

Key Areas and Rating	Strengths and Weaknesses
2. Transparency and Disclosure *Fair/Moderately strong*	*The law requires companies to prepare annual reports including financial and non-financial information and all ten largest listed companies published comprehensive annual reports with information on governance and ownership structures. However, only five of them provided a comply or explain statement. Overall, disclosure is very formalistic in nature: listed companies appear to disclose the contents of its internal documents but not the corporate governance practices in place. Very often, explanations are minimal and not convincing.* *Most of the largest listed companies disclose having independent directors on their boards but only in very few cases there are some (limited) explanations on the ground upon which these directors are considered independent. In most cases, it is impossible to understand if they are really independent.* *Companies are required to disclose financial information in line with IFRS, and all ten largest listed companies appear to comply with this requirement.* *The law requires companies to disclose price sensitive events, as well as the initiation of any insolvency or restructuring proceedings.* *Breach of disclosure obligations is subject to sanctions.* *Joint stock companies are required to appoint an independent external auditor. Listed companies are required to publish the auditor's name and report on their website, and all ten largest listed companies comply with this requirement. Auditors are allowed to provide non-auditing services. This practice should be carefully monitored as it might compromise the auditors' independence. Disclosure on this matter is very limited.*
2.1. Non-Financial Information Disclosure *Fair/Moderately strong*	***Strengths:*** • *All ten largest listed companies included forward-looking strategic statements in their annual reports.* • *The law requires companies to provide detailed disclosures in their annual reports. Similarly, they must publish this report on their websites and submit them to the regulator.* • *All ten largest companies appear to keep their websites up-to-date.* • *Decree 454 requires companies with exchange-traded equity to disclose their compliance with the Corporate Governance Code in a section of their statutory annual reports. The board must also include a statement informing on the company's compliance with the Code. This statement should specifically mention those principles with which the issuer does not fully comply and briefly describe deviations. The compliance report should also explain the reasons for deviation and explain how alternative governance arrangements respect the spirit of the Code.* • *All ten listed companies declare their compliance with the Corporate Governance Code and have adopted their own corporate governance codes, but only five include a "comply or explain" statement.* • *By law, issuers are required to disclose the names of their board members. Additionally, the Corporate Governance Code recommends companies to disclose their qualifications. All ten largest companies disclose the names of their board members. Eight companies disclose the qualifications of their board members, however in several cases information is limited to education and work experience and does not allow to understand if the qualifications of the board members are fit for purpose and are adding value to the work of the board.* • *Seven of the ten largest companies disclose the activities of their board. Nine among the ten largest companies disclose the number of board meetings per year.* • *All ten largest listed companies disclose having an audit committee. Eight among the ten largest listed companies also declared having nomination and remuneration committees. Seven disclose the number of committees' meetings. Disclosure on committee's activities is however limited and is often a copy and paste from the company's documentation and does not relate to the activities actually undertaken by the committees.* • *Companies disclose their beneficial ownership and provide updated information on their capital and number of shares.* • *The Corporate Governance Code calls for the adoption of a code of ethics, and nine out of ten companies adopted one.* • *All ten largest companies disclose the names of shareholders owning at least 5% of shares.* ***Weaknesses:*** • *Companies are only required to disclose their board members' qualifications in the general shareholders' meeting's materials sent to shareholders prior to the election of directors.* • *Only half of the companies in our sample provided a "comply or explain" statement with the Corporate Governance Code. Overall, disclosure is very formalistic in nature: listed companies appear to disclose the contents of its internal documents regulating the activities of their bodies, but not the corporate governance practices in place. Very often, explanations are minimal and not entirely convincing.* • *Though there are some provisions regulating audit committee disclosures, requirement to report other board committees' meetings and activities appears to be limited.* • *Most of the largest listed companies disclose having independent directors on their boards but only in very few cases there are some (limited) explanations on the ground upon which these directors are considered independent. In most cases, it is impossible to understand if they are really independent.* • *Companies are not required to make the minutes of the general shareholders' meeting publicly available.* • *Only one company discloses transactions of company shares.*

<table>
<tr><th>Key Areas and Rating</th><th>Strengths and Weaknesses</th></tr>
<tr><td>2.2. Financial Information Disclosure
Strong</td><td>Strengths:
• All ten largest companies prepared their financial statements in line with the IFRS and disclosed them on their websites.</td></tr>
<tr><td>2.3. Reporting to the Market and to Shareholders
Fair</td><td>Strengths:
• The law requires companies to disclose annual reports on their websites, which should include financial and non-financial information. All ten largest companies published comprehensive annual reports.
• The law requires companies to disclose price sensitive events and the start of insolvency and restructuring proceedings.
• The law sanctions the non-disclosure of annual reports, and the regulator confirms that several companies have been sanctioned for reporting breaches in the past.
Weaknesses:
• The law does not require companies to make the minutes of the general shareholders' meeting publicly available, but only to provide them to shareholders upon request.
• Overall, disclosure is very formalistic in nature: listed companies appear to disclose the contents of its internal documents regulating the activities of their bodies, but not the corporate governance practices in place. Very often, explanations are minimal and not convincing.</td></tr>
<tr><td>2.4. Disclosure on the External Audit
Fair</td><td>Strengths:
• Joint stock companies are required to appoint an independent external auditor.
• The authority to appoint the auditor belongs to the general shareholders' meeting.
• The law requires the external auditor to be independent. The audit committee oversees the external auditor's independence and objectivity, as well as the quality of the auditing process.
• Listed companies are required to publish the auditor's name and report on their website, and all ten largest listed companies comply with this requirement.
Weaknesses:
• Audit firms are not forbidden from providing non-audit services to their clients, which can undermine their independence. No company discloses having in place a policy of non-auditing services provided by its external auditor. Further, disclosure on non-auditing services provided by the external auditor is limited.</td></tr>
</table>

<table>
<tr><th>Key Areas and Rating</th><th>Strengths and Weaknesses</th></tr>
<tr><td>3. Internal Control
Fair</td><td>Listed companies and banks are required to set up internal audit departments, and the majority of the largest companies appear to comply with this requirement. It appears that banks are not required to establish a standalone compliance function.
Listed companies are required to set up an audit committee, made up of – at least - a majority of independent members, and a revision commission, which is responsible for the oversight of the company's financial and business activities. We have doubts about the effectiveness of the revision commission.
In practice, it appears that the large majority of companies in our sample have established both an audit committee and a revision commission, but only in two cases the audit committee is entirely made up of independent board members.
Joint stock companies are required to appoint an independent external auditor. Auditors are allowed to provide non-auditing services. There is no auditors' rotation requirement.
The large majority of the top ten largest companies have adopted a code of ethics, however only in one case it is clearly disclosed who the officer in charge of monitoring compliance is. This is a key issue as the value of the code is in its implementation.
There is no comprehensive legislation protecting whistle-blowers in Russia. Regulation on related party transactions appears to be limited, and not fully aligned with best practices. The regulation on conflict of interests also appears to be limited.</td></tr>
<tr><td>3.1. Quality of the Internal Control Framework
Fair</td><td>Strengths:
• Listed companies and banks are required to set up internal audit departments, and nine out of the ten largest listed companies appear to comply with this requirement. The internal audit function is functionally subordinated to the board and administratively to the executive body.
• Listed companies are required to set up an audit committee, composed of non-executives and at least in its majority of independent directors. All ten largest companies disclosed having set up an audit committee. The majority of audit committees are made up of a majority of independent directors.
• Joint stock companies are required to set up a revision commission, whose members are appointed by the general shareholders' meeting. The revision commission is responsible for the oversight of the company's financial and business activities. Nine out of the ten largest listed companies set up a revision commission.
• The Corporate Governance Code calls for the adoption of a code of ethics. Nine companies in our sample disclose having a code of ethics, however only in one case it is clearly disclosed who the officer in charge of monitoring compliance is. This is a key issue as the value of the code is in its implementation.
Weaknesses:
• According to the report by Transparency International entitled "Protection of corruption whistle-blowers", there is virtually no legal protection for whistle-blowers in Russia.
• It appears that banks are not required to establish a standalone compliance function.
• We have doubts about the effectiveness of the revision commission. This is a body appointed by and reporting to the general shareholders' meeting. It is often confused with the audit committee, but there are substantial differences, as the revision commission is not a board committee and is not involved in the direction of the company.
• In at least two companies in our sample, independent directors are only a minority of the audit committee. Further, it appears that in most cases, the qualifications of the audit committee's members are not appropriate for the functions and responsibilities of the committee.</td></tr>
<tr><td>3.2. Quality of Internal and External Audit
Fair</td><td>Strengths:
• Listed companies and banks are required to be set up internal audit departments.
• Joint stock companies are required to appoint an independent external auditor.
• An Order of the regulator requires audit committees to oversee external auditor's independence and objectivity, as well as the quality of the audit conducted.
• Nine out of the ten largest listed companies are being audited by international auditing firms.
• The Russian Institute of Internal Auditors (http://www.iia-ru.ru) cooperates with the Institute of Internal Auditors and represents the latter in Russia by virtue of a partnership agreement.
Weaknesses:
• There is no prohibition for audit firms to provide non-auditing services to their clients. No company discloses having in place a policy of non-auditing services provided by its external auditor. Further, disclosure of non-auditing services provided is very limited.
• There is no requirement to rotate audit firms. Only three companies disclosed information on the rotation of their auditors.</td></tr>
<tr><td>3.3. Functioning and Independence of the Audit Committee
Fair</td><td>Strengths:
• Listed companies are required to set up an audit committee, composed of non-executive and at least in its majority of independent directors. All ten largest listed companies disclosed having set up an audit committee.
• Seven of the ten largest listed companies disclosed the frequency of audit committee meetings.</td></tr>
</table>

Key Areas and Rating	***Strengths and Weaknesses***
	Weaknesses: • *Only two of the ten largest listed companies have the audit committee made up entirely of independent board members. However, in most cases, independent directors are a majority of the committee.* • *In most cases, the qualifications of the audit committee's members are not appropriate for the functions and responsibilities of the committee.*
3.4. Control over Related Party Transactions and Conflict of Interest *Weak*	***Strengths:*** • *All ten largest listed companies disclose information on related party transactions.* ***Weaknesses:*** • *The definition of a related party is limited to a board director, an executive, a 20% shareholder, any person who is able to give company instructions which are binding, and their affiliates, who either directly participate in the transaction, hold board or management positions, or are 20 % shareholders in the company on the other side of the transaction. This is too restrictive and fails to include parties that would usually be considered as related parties.* • *The regulation on related party transactions appears to be limited, and not fully aligned with best practices. The law provides that a decision on entering into a related party transaction shall be taken by a simple majority of board directors, excluding those with interest in the transaction, when the company does not have more than 1,000 shareholders. If the number of shareholders exceeds 1,000, then the decision should be approved by the majority of independent directors with no interest in the transaction. Here the definition of independent director – which is different from the one provided by the Corporate Governance Code - is relatively narrow.* • *Directors are not required or encouraged to abstain from participating in the deliberations on a particular agenda item when they any conflicts of interest.* • *It is not clear why the audit committee (which is required for most listed companies) is not assigned with competence over related party transactions.*

Comments are welcome: please provide comments to cignag@ebrd.com

Key Areas and Rating	Strengths and Weaknesses
4. Rights of Shareholders *Fair*	*Minority shareholders are entitled to call a general shareholders' meeting (GSM) and put additional items on the GSM's agenda. However, the law is not explicit about granting shareholders the right to ask questions at the GSM.* *Pre-emptive rights are provided by law in case of capital increase, but no supermajority is required in case of waivers. Cumulative voting is provided by law.* *Two-thirds qualified majority vote is required to amend the Articles of Association and to approve other key decisions such as mergers, reorganisations or winding up procedures.* *Insider trading is prohibited by law, and violations of these provisions can lead to fines or imprisonment.* *The law requires companies to disclose financial and non-financial information in their annual reports, and it appears that annual reports are generally available.* *Shareholders can file derivative suits on behalf of companies; however, there is no evidence of derivative suit cases, which may indicate that enforcement is difficult in practice.* *The law regulates registration of shareholding and shareholder agreements.* *Joint stock companies with more than fifty shareholders are required to maintain their share register with an external licenced registrar.*
4.1. General Shareholders' Meeting (GSM) *Fair*	***Strengths:*** • *Shareholders owning at least 10% of the company's shares can call a GSM.* • *The law requires joint stock companies to send the GSM agenda to shareholders at least 20 calendar days before the meeting. Nevertheless, the law does not require companies to post this information on their websites, though this is recommended by the new Corporate Governance Code.* • *The law enables shareholders owning at least 2% of company's voting shares to put additional items on the agenda of the GSM.* • *Voting shareholders holding at least 2% of shares can nominate candidates for election to the board.* ***Weaknesses:*** • *The Corporate Governance Code recommends the GSM to provide reasonably equal opportunities to all shareholders to express their opinions and ask questions to board directors and members of the executive body. However, the law does not explicitly grant shareholders the right to ask questions at the GSM.* • *According to the OECD Russia 'Corporate Governance Roundtable - Background Paper' (2013), shareholders of Russian companies "are not able to obtain high-quality materials for shareholders' meetings in the most appropriate form and within timeframes to suit the shareholders". This research also shows that shareholders, especially foreign investors, are in fact stripped of the possibility of exercising their voting right at general shareholders' meetings in terms of being able to scrutinise all of the materials and reach a reasoned decision on items on the agenda. The timeframes for providing the materials (including 20 days) do not allow foreign investors with an impressive chain of depositaries (international, regional and local), each of which also have their own internal voting timeframes, to participate in votes by correspondence having adopted a well-founded position regarding each point on the agenda.* • *None of the ten largest listed companies provide information on their voting rights.*
4.2. Protection against Insider Trading and Self-dealing *Weak*	***Strengths****:* • *Insider trading is forbidden by law. Violation of this prohibition may lead to fines or imprisonment.* ***Weaknesses****:* • *There is no information or evidence of any investigated insider trading cases being brought to court.* • *Board members and managers must disclose share trading in the annual report. Only one of the ten largest listed companies discloses such information.*
4.3. Minority Shareholders Protection and Shareholders' Access to Information *Weak*	***Strengths:*** • *The law requires joint stock companies to disclose on their website annual reports which should include information on non-financial disclosures. All ten largest listed companies published comprehensive annual reports with information that provides substantial data on governance and ownership structures, and five of them submitted "comply or explain" sections with their reports. This is likely to be an influence of their double listing at the London Stock Exchange.* • *Two-thirds qualified majority vote is required to amend the articles of association and approve other key decisions such as mergers, reorganisations or winding up procedures (the blocking minority is 33%+1).* • *The law provides for cumulative voting.* • *Shares grant to shareholders the same rights. Shares with multiple voting rights are not allowed by law and hence voting at the GSM is carried out in line with the "one-share, one-vote" principle.* • *Derivative claims are permitted by law.* ***Weaknesses:*** • *Shareholders are entitled to pre-emptive rights in public offerings, but the law does not require any supermajority to waive pre-emptive rights.* • *According to the OECD Russia 'Corporate Governance Roundtable - Background Paper' (2013), shareholders of Russian companies "are not able to obtain high-quality materials for shareholders' meetings in the most appropriate form and within timeframes to suit the shareholders."*

Key Areas and Rating	Strengths and Weaknesses
	• *There is no evidence of derivative claims being pursued in Russia. This implies that enforcement might be difficult in practice.* • *The law allows companies to establish caps to the number of votes that a shareholder can exercise in its articles of association.*
4.4. Registration of Shareholdings *Fair*	***Strengths:*** • *The Law on the Securities Market states that the free transferability of shares cannot be restricted.* • *Shareholders can enter into shareholder agreements which, if established in compliance with Russian law, are fully enforceable. Nevertheless, in case the foreign law applies, only the part of the agreement which does not contradict Russian law is enforceable.* • *Since 2014, joint stock companies with more than fifty shareholders are required to maintain their share register with an external licenced registrar.* ***Weaknesses:*** • *As mentioned in the 2013 World Bank ROSC, there has been a bad practice of share dilution and other abuses related to share registration in Russia.*

Key Areas and Rating	Strengths and Weaknesses
5. Stakeholders and Institutions *Moderately strong/Fair*	*The Moscow Exchange is highly capitalised and very liquid. Trading is divided in five segments with different corporate governance requirements. To be listed in the First or Second Tier, companies must establish audit, nomination and remuneration committees, as well as prepare their financial statements in accordance with the IFRS.* *The website of the Moscow Exchange contains a comprehensive database of companies' financial and non-financial information, and the Exchange appears to be very active in promoting good corporate governance.* *The Russian Corporate Governance Code was developed in 2001 with the assistance of the EBRD, and was revised in 2014. All joint stock companies are recommended to implement the Code's provisions, and all listed companies are required to present a "comply or explain" section in their annual reports. Despite this request, only five of the ten largest listed companies have disclosed a "comply or explain" statement. Most of the explanations provided are excessively formalistic, and make no significant reference to companies' current state of corporate governance practices. The Central Bank of Russia has committed to actively oversee the implementation of the new Code. Results of these efforts are yet to be reported.* *Indicators by international organisations point out that corruption remain a perceived concern.*
5.1. Corporate Governance Structure and Institutions *Moderately Strong*	***Strengths:*** • *In December 2011, the Moscow Securities Exchange (MSE) was formed as a result of a merger between the MICEX Group, Russia's main operator of securities, foreign exchange and money markets, and the RTS Group, the operator of Russia's leading derivatives market. Its market capitalisation is around 42.9% of the GDP, and it seems that the volume of trades is relatively high.* • *There are five main listing markets at the MSE. Companies forming part of the First or Second Tier listings are required to comply with higher corporate governance standards. To be listed in these two Tiers, companies must establish audit, nomination and remuneration committees, as well as prepare their financial statements in accordance with IFRS. In case of non-compliance, companies can be relocated to a lower tier, or be delisted.* • *The MSE supervises compliance with its listing rules.* • *The MSE's website provides a comprehensive list of regulatory submissions by listed companies, including financial and non-financial reports.* • *Rulings of the regulatory agencies are documented, publicly available and easily accessible. Rulings issued by the National Bank of Russia are regularly published on the Bank's website.* • *International audit and law firms have a material presence in the country.* • *International ratings agencies are active within the country; all ten surveyed companies have been rated by international ratings agencies.* • *There are several organisations actively promoting corporate governance in the country, such as the Russian Institute of Directors (RID), the Independent Director Association (IDA) and the Investor Protection Association (IPA). These organisations provide training for directors, as well as research and consulting services which support promotion of good corporate governance practices.*
5.2. Corporate Governance Code *Moderately strong*	***Strengths:*** • *The Russian Corporate Governance Code was developed in 2001. The Code was recently revised in 2013 and a new Corporate Governance Code was adopted in 2014.* • *The Code is based upon OECD's Principles of Corporate Governance.* • *The Code is divided in two main sections: (i) the Principles of Corporate Governance (the code itself); and (ii) the Recommendations on the Principles of Corporate Governance, for the practical implementation of the Code's Principles.* • *All joint stock companies are recommended to implement the Code's provisions, and all listed companies are required to present a "comply or explain" statement in their annual reports.* • *Though the implementation of the previous Corporate Governance Code was not actively monitored, the Central Bank of Russia has committed to oversee the implementation of the new Code. The Bank of Russia kept its commitment and following the Code's entry into force and a publication of a Manual for Issuers in February 2016 - to provide guidance ahead of preparation of their annual reports - the Bank of Russia issued the first ever monitoring report in April 2017. We believe this is a significant step in the right direction.* ***Weaknesses:*** • *Despite being required to present a "comply or explain" statement in their annual report, only five of the ten largest listed companies have disclosed their corporate governance practices. Furthermore, most of the explanations provided are excessively formalistic, and make no significant reference to companies' current state of corporate governance practices.* • *There is no case law specifically referring to the Corporate Governance Code.*

Key Areas and Rating	***Strengths and Weaknesses***
5.3. Institutional Environment *Fair*	***Strengths:*** • *The MSE and the Bank of Russia seem to be active in the promotion of corporate governance.* • *According to the 2015 EBRD Assessment on Accessibility of Court Decisions, it seems that case law is fairly easily accessible to parties and the public, with the lack of prompt publication of decisions being highlighted as the only major issue.* ***Weaknesses:*** • *A few significant inconsistencies were found in laws, regulations and the corporate governance codes. For example, there is not a clear and consistent definition of independent director.* • *International indicators rank Russia moderately well in terms of investor protection (Doing Business Index 2014) and competitiveness (World Economic Forum's Global Competitiveness 2013-2014), but relatively poorly in terms of corruption perception (CPI).*