01 August 2013

To all our clients and friends

MEMORANDUM
Analyzing Kazakhstan's Competition-Relevant Legislation Amendments

The Law "On Amendments to Certain Legislative Acts of the Republic of Kazakhstan on Competition Issues" (hereinafter, the Law) amending a number of current legislative acts[1] of the Republic of Kazakhstan (hereinafter, the RK or Kazakhstan), including the Competition Law[2], was adopted on 6 March 2013.

This article offers an analysis of those amendments, which we deem to be most important for the business.

1. Law Enactment Date

The Law is put into effect upon expiration of ten calendar days of its first official publication. Experts differ in opinion over the date of the Law enactment – March 24 or March 25.

In our view, the date of the Law enactment is the 25th of March. We proceed from the general provisions of the Civil Code[3] regarding commencement of the running of a term, according to which a term, which is defined by a period of time, commences running on the next day following the calendar date or occurrence an event, which define its commencement (Article 173 of the Civil Code). The Law was first published in the *Kazakhstanskaya Pravda* newspaper No. 93-94 (27367-27368) on 14 March 2013. Hence, if the count starts from March 15, the 10 calendar days end on March 24, i. e., the Law is enacted starting 25 March 2013.

2. Law Objective

The Law is intended to further improve the current Kazakhstan's antimonopoly legislation, strengthen the competition protection and streamline the activities of market entities. Moreover, one of the Law priorities is to harmonize the antimonopoly legislation of the Customs Union member states in the context of formation of the Unified Economic Space (hereinafter, the UES) of Kazakhstan, Russia and Belarus (hereinafter, the UES Member States). A number of amendments were made in order to bring the norms contained in the Competition Law in line

[1] The Law amends the following RK regulatory acts: Civil Code, Criminal Code, Administrative Code, Code on Taxes and Other Mandatory Payments to the Budget (Tax Code), Law on Natural Monopolies and Regulated Markets, Law on Electric Power Industry, Law on Technical Regulation, Law on Licensing, Law on State Regulation of Production and Turnover of Certain Types of Oil Products, Law on Introduction of Amendments into Certain Legislative Acts of the Republic of Kazakhstan on the Issues of Electric Power Industry, Investment Activities of Natural Monopoly Entities and the Regulated Market.

[2] RK Law No. 112-IV "On Competition" dated 25 December 2008, as amended (hereinafter, the Competition Law).

[3] RK Civil Code (General Part) adopted by the RK Supreme Soviet on 27 December 1994, as amended (hereinafter, the Civil Code).

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with the Agreement on the Common Principles and Rules of Competition of 9 December 2010 ratified by Kazakhstan on 8 July 2011, which was aimed at forming the following:

- unified competition policy intended to ensure free movement of goods, services and capital;
- freedom of economic activities;
- efficient functioning of commodity markets in the unified customs territory of the UES Member States;
- harmonization of the UES Member States legislation in the sphere of competition policy and prevention of actions to potentially adversely affect the mutual trade among the UES Member States.

In the framework of the Agreement on the Common Principles and Rules of Competition, the Eurasian Economic Commission adopted a number of resolutions approving: (i) different methodologies in the sphere of competition legislation[4], (ii) procedure for interaction, including informational interaction, between the Eurasian Economic Commission and the authorized agencies of the UES Member States; (iii) criteria for referring a market to cross-border markets; (iv) procedure for the review of cases on competition rules violation; (v) procedure for competition rules violations investigation; (vi) procedure for reviewing the competition rules violation applications (materials).

Many amendments were made pending the adoption of the Model Competition Law for the UES Member States (hereinafter, the Model Law).

3. A Glimpse of the Model Law

The Model Law was expected to have been adopted in June or July 2013, but it has not been adopted so far. The discussion of Model Law provisions took place in 6 different cities, namely, in Moscow, Novosibirsk, Kiev, Minsk, Almaty and Astana.

The key purport of the Model Law is to bring closer the legal regulation of economic relations in the sphere of competition policy, in keeping the political independence of all UES Member States.

The Model Law is expected to be the fundamental document incorporating the common principles and approaches of the UES Member States to the protection of competition, based on which the appropriate amendments are to be introduced into the national antimonopoly laws of such states. Besides, the draft Model Law contains several reference norms, allowing for leaving a number of provisions to the discretion of the UES Member States (for instance, the thresholds for referring economic concentration transactions to those requiring Antimonopoly Agency's prior approval are to be defined by the legislation of the relevant jurisdictions).

[4] In particular, the Eurasian Economic Commission's resolutions approve the following methodologies:

- Competition status evaluation methodology;
- Methodology for determining the monopolistically high and monopolistically low prices;
- Methodology for calculation and the procedure for imposing the fines provided for by the Agreement on the Common Principles and Rules of Competition.

The Model Law must reflect the common approach developed by the UES Member States to the provisions dealing with the general principles of state price regulation, state participation in entrepreneurial activities, functions and objectives of antimonopoly agencies and other key issues to be governed by the antimonopoly legislation. According to Mr. B. Kuandykov, the Chairman of RK Competition Protection Agency (hereinafter, the Antimonopoly Agency), "despite the Model Law's recommendatory nature, we believe that brining the national antimonopoly legislation of the Republic of Kazakhstan in line with its [Model Law's. – AEQUITAS] key provisions and the organizational and legal basics of the competition protection will bear a political and image nature"[5].

When discussing the Model Law provisions, taken as a basis were the provisions of Kazakhstan, Russia and Belarus legislations, also taking into account the international experience. Certain existing norms of the Kazakh legislation have been taken into account and included into the draft, for example: the collegiate principle of Antimonopoly Agency management; provisions regarding holding of investigations; grounds for exempting from liability for antimonopoly legislation violations; the right of state monopoly to limit competition in certain spheres of economy in which the sale of goods on a competitive market may adversely affect the constitutional system, etc.

It is also supposed to introduce into the Model Law the norms that are new to Kazakhstan, including:

- use of warning to a market entity in respect of certain violations;
- examination of the territories, premises, documents and items of the person under inspection;
- review of cases over antimonopoly legislation violations by analogy to arbitration proceedings, and other.

4. Amendments to the Competition Law

4.1. Conceptual Apparatus

The conceptual apparatus of the Competition Law underwent certain amendments intended to amplify it and to clarify some of the concepts used therein. For example, the Law now features such new concepts as potential competitor, direct competitor, direct and indirect control and coordination of economic activities.

- Only Article 9 of the Competition Law mentions **potential competitor**[6], this concept evidently being introduced only for the purposes of the Article correct interpretation.
- The concept of "**competitor**" is encountered in many Articles of the Competition Law (mostly in Chapter 3 dedicated to unfair competition). Incorporating the concept of "competitor" into the Competition Law will, in our view, facilitate a better understanding of the Law norms and, in the view of the Antimonopoly Agency, ensure the efficient implementation of the Competition Law regulations.
- Previously, the Kazakh legislation contained no concept of **direct and indirect control**,

[5] *Rynok i Konkurentsiya* magazine, No. 02/2013, p. 13.

[6] Anticompetitive agreements between, or concerted actions by, market entities, which are competitors or *potential competitors* [*emphasis added*. – AEQUITAS] on the same commodity market, shall be deemed horizontal (paragraph 1 of Article 9 of the Competition Law).

which hampered the interpretation of many of its provisions. Only the JSC Law[7] contained a general concept of control, which was understood as a possibility for a person to determine the decisions adopted by a company or another legal entity. Now, for the purposes of the Competition Law, it will use the special definition contained therein, not the one by analogy, as it was before.

- The Law also introduces the concept of **coordination of economic activities**, which is punishable under the Administrative Code[8]. It should be mentioned that so far it is unknown how the persons conducting coordination of economic activities will be identified in practice and how the fact of conducting such coordination will be proved.

As regards the clarified and complemented concepts, the following should be mentioned specifically:

- The definition of **Antimonopoly Agency** has been revised in connection with including into its competence the function of control and regulation of activities in the state monopoly sphere.

- Moreover, the market entities now expressly encompass non-profit organizations conducting entrepreneurial activities in accordance with their charter-defined objectives. In our view, this addition to the market entity concept is not a novelty, because the previous version of the Competition Law, although not expressly referring to non-profit organizations as market entities, suggested, however, by its existing definition that the market entities are all legal entities conducting entrepreneurial activities, i. e., non-profit organizations conducting entrepreneurial activities in accordance with their charter-defined objectives as well.

4.2. Group of Persons

According to the Competition Law version previously in effect, one of the conditions allowing to qualify an aggregate of individuals and/or legal entities as a group of persons was the person's ability to directly or indirectly (via third parties) dispose of more than 25% of the voting shares (charter capital participation interests, unit shares) in a legal entity.

Now, a person will be on a group of persons if it has the right to directly or indirectly (via third parties) dispose of more than 50% of the voting shares (participation interests in the charter capital, unit shares) in a legal entity.

This change testifies to the tendency towards harmonization of the Kazakh legislation with the global antimonopoly practice (for instance, a similar provision is present in the legislations of the Russian Federation and many European Union countries).

This change is also positive for large companies, because shrinking the circle of persons included in a group reduces the scope of information to be submitted when applying for the Antimonopoly Agency's consent to economic concentration. On the other hand, this change means that certain market entities will not be recognized as a group of persons, which will entail an increase of the number of transactions requiring the Antimonopoly Agency's prior consent.

[7] RK Law No. 415-II "On Joint Stock Companies" dated 13 May 2003, as amended (hereinafter, the JSC Law).

[8] RK Code No. 155-II "On Administrative Violations" dated 30 January 2001, as amended (hereinafter, the Administrative Code).

4.3. Anticompetitive Agreements

The Law introduces provisions banning vertical and horizontal agreements, subject to the possible or actual occurrence of consequences described below.

Prohibited are **horizontal agreements**[9] between market entities that infringe on customers' legitimate rights and/or lead or may lead to:

"1) establishment or maintaining of prices (tariffs), discounts, extra charges (surcharges) and markups;

2) increasing, decreasing or maintaining prices at auctions;

3) division of a commodity market according to the territorial principle, volume of sale or purchase of goods, assortment of goods being sold or the composition of sellers or buyers (customers);

4) reduction or cessation of goods production;

5) refusal from entering into contracts with certain sellers or buyers (customers)" (subparagraphs 1-5 of paragraph 1 of Article 10 of the Competition Law).

One of the positive aspects of the above innovations is the fact that now the territory-based division of a commodity market is only prohibited in case of horizontal agreements and is allowed in case of such commonly encountered types of vertical agreements as distributor agreements and other similar agreements.

Prohibited are **vertical agreements**[10] between market entities, if:

"1) the agreements lead or may lead to the establishment of goods resale price, except where the seller establishes for the buyer a maximum goods resale price;

2) the agreement provides for the buyer's obligation not to sell the goods of a market entity, which is the seller's competitor. This prohibition shall not cover the agreements on buyer's organization of the sale of goods under a trademark or another means of individualization of the seller or manufacturer" (subparagraphs 1 and 2 of paragraph 2 of Article 10 of the Competition Law).

Thus, the revised Competition Law expressly prohibits including the so-called "exclusivity provision" into vertical agreements, unless these are agreements on buyer's organization of the sale of goods under a trademark or another means of individualization of the seller or manufacturer.

4.4. Dominant or Monopolistic Position

The Law introduces amendments stating that the dominant position of market entities will be determined based on a special document setting out the procedure for competition status evaluation, calculation formulas, etc. It should be mentioned that previously the legislation did not contain such a provision.

[9] Horizontal agreements – agreements entered into between market entities that are competitors or potential competitors on the same commodity market.

[10] Vertical agreements – agreements entered into by non-competing market entities one of which is acquiring goods or is a potential acquirer thereof and the other is providing the goods or is a potential seller (supplier) thereof.

According to the amendments, a market entity's dominant position is to be established based on the Competition Status Evaluation Methodology approved by the Eurasian Economic Commission[11] and proceeding from the analysis of quite a number of circumstances, for example, the market entity's share on the market and how it correlates with the shares of competitors and buyers; the market entity's ability to unilaterally determine the goods price level and to decisively affect the general goods sale conditions on a relevant commodity market; presence of restrictions on access to the commodity market, etc.

Besides, the list of prohibited actions of market entities holding a dominant or monopolistic position, which have led or are leading to the restriction of access to the relevant commodity market, or prevention, restriction and elimination of competition and/or which infringe on the legitimate rights of consumers or other persons, was expanded.

Now, the prohibited actions include as well as follows:

- withdrawal of goods from circulation, if such withdrawal resulted in the increase of the goods price;
- imposing on the counterparty economically or technologically unjustified contract terms unrelated to the subject of contract;
- impeding access to, or exit from, the commodity market for other market entities;
- economically, technologically or otherwise unjustified setting of different prices (tariffs) for the same goods, or creation of discriminatory conditions.

4.5. Unfair Competition

The list of actions referred to unfair competition has been expanded. In addition to the previously established, the list now comes to include such actions as:

- sale of goods in providing to the consumer unreliable information regarding the nature, method and place of manufacture, consumer properties, quality and quantity of the goods and/or their manufacturers;
- market entity's inappropriate comparison of the goods produced and/or sold by it with goods produced and/or sold by other market entities.

The Law also qualifies as unfair competition the acquisition of tie-in goods (in addition to the previously stipulated sale of tie-in goods).

4.6. Antimonopoly Agency's Scope of Competence

The Law introduces certain innovations with respect to the Antimonopoly Agency's scope of competence, for example: propaganda of fair competition; ensuring informational transparency of the pursued competition policy (including quarterly publication of information on the Antimonopoly Agency's activities in mass media and on the Antimonopoly Agency's official website); expert review of the prices for goods produced and sold by a state monopoly entity.

The Law also sets forth that certain Antimonopoly Agency's actions, for instance, approval of certain methodologies (for the analysis and evaluation of the status of competitive environment on a commodity market in defining the criteria for the goods interchangeability and affordability,

[11] Competition Status Evaluation Methodology approved by the Council of the Eurasian Economic Commission, dated 25 December 2012, No. 299.

and the commodity market boundaries; for identifying the monopolistically high (low) and monopsonically low prices) and submission of proposals to the Government to refer the commodity market to the regulated markets, are to be approved by the state authority, coordinating, on inter-sectoral and interregional level, the development of key guidelines for the state social-and-economic policy.

4.7. Antimonopoly Agency's Interaction with Regulatory, Law-Enforcement and Antimonopoly Agencies of Other States

The version of the Competition Law previously in effect contained norms providing for the Antimonopoly Agency's interaction only with regulatory and law-enforcement authorities of the RK. Now, given the UES framework, the Law sets out the norm to regulate the interaction of the Customs Union member states' antimonopoly agencies, which involves, among other things, the submission of notifications and requests for information, holding consultations and informing about investigations.

Beside this, in the framework of participation in international organizations, the Antimonopoly Agency may send enquiries to antimonopoly agencies of other states and provide information upon their requests.

4.8. Economic Concentration

The Law changes and supplements the provisions relating to economic concentration. The previously effective version of the Competition Law provided for the possibility to enter into transactions recognized as economic concentration, on condition of obtaining the Antimonopoly Agency's prior consent.

The Law introduces notification procedure in respect of two out of five types of transactions recognized as economic concentration. Pursuant to the revised Competition Law, when entering into certain types of transactions[12], market entities are to notify the Antimonopoly Agency of the transaction within 45 calendar days of the date of the transaction execution.

In view of such amendments, the Competition Law is added with provisions setting out the procedure for notifying about the performed economic concentration and the deadlines for the notification review by the Antimonopoly Agency.

The Law mentions the following consequences of notifying the Antimonopoly Agency:

- in the event the Antimonopoly Agency, upon expiration of 45 calendar days after receiving the performed economic concentration notification, does not send a written response to the notification sender stating the need to cancel the transaction, the economic concentration is deemed to have been implemented;

- in the event the Antimonopoly Agency establishes, in the course of reviewing the performed economic concentration notification, that its performance has led or may lead to competition restriction or elimination, including through the arising or strengthening of a

[12] Transactions requiring the Antimonopoly Agency notification include:

- acquisition by a market entity of the rights (including based on a trust management agreement, joint operating agreement or agency agreement) allowing to issue binding instructions to another market entity in its conduct of entrepreneurial activities, or to perform the functions of its executive body;

- participation of the same individuals in the executive bodies, boards of directors, supervisory boards or other management bodies of two or more market entities, provided that the said individuals determine in such entities the conditions of the latters' entrepreneurial activities.

market entity's dominant position, the Antimonopoly Agency issues an ordinance[13], which must be fulfilled within 30 calendar days;

- in the event of failure to fulfill the ordinance, the Antimonopoly Agency goes to court claiming to force the market entity to fulfill the Antimonopoly Agency's ordinance.

The analysis of the above provisions suggests a conclusion that the notification procedure is actually a post-approval of the performed transactions, because in case the Antimonopoly Agency finds that the transaction consummation has led or may lead to competition restriction or elimination, the market entities may face such negative implications as transaction cancellation or an ordinance issued by the Antimonopoly Agency, as provided for by the Competition Law.

Pursuant to the Law, market entities still retain the right to file applications for the Antimonopoly Agency's consent to economic concentration with respect to transactions falling within the notification procedure. We deem that in a number of instances, in order to avoid the risk of transaction cancellation or issuance of the Antimonopoly Agency's ordinance, it would be advisable to obtain the Antimonopoly Agency's prior consent to economic concentration, even if such transactions fall within the notification procedure.

One of significant changes worth mentioning is the increase of threshold of the acquirer's (group of persons) and the target company's aggregate book value of assets and aggregate goods sales volume for the past financial year, which, once reached, entails necessity to either obtain the Antimonopoly Agency's consent, or to notify it. This index was increased from 2,000,000 monthly calculation indices (hereinafter, the MCI[14]) to 10,000,000 MCI. In monetary terms, previously this amount approximately made 23,080,000 USD, and now, subject to the amendments, it makes 115,400,000 USD. Hence, given the adopted amendments, it is expected that the number of transactions requiring the Antimonopoly Agency's prior consent or notification will dwindle.

4.9. Other Amendments

Beside the key changes described above, there are other changes, in particular, as follows:

- The Law secures the procedures for forming and maintaining the State Register of market entities holding a dominant or monopolistic position (hereinafter, the Register). It should be mentioned that, due to the constantly changing situation on the commodity market, the Register cannot objectively and timely register all actual dominant entities, because in order to do so the Register would need to be updated on a daily basis. However, it does not seem possible to update the Register that often due to a number of reasons, such as the Antimonopoly Agency's lack of sufficient resources for daily inspections, etc. Therefore, in the opinion of the Antimonopoly Agency and some antimonopoly law experts, such Register must be abolished.

[13] Pursuant to the Competition Law, the Antimonopoly Agency may issue ordinances to:

- stop the Competition Law violations and/or eliminate their consequences;
- restore the previously existing state of affairs;
- terminate or amend the agreements contradicting the Competition Law;
- enter into agreement with another market entity, if the violation here is an unreasonable refusal or evasion from agreement with certain sellers (suppliers) or buyers;
- prevent (refrain from) violations of the Competition Law.

[14] In 2013, the MCI is set at 1,731 KZT (approximately 11.5 USD).

- The provisions governing the state assistance issues are deleted from the Law, in connection with an insignificant number of the relevant applications submitted.

- The institute of preliminary investigation has been eliminated, because, as shown by practice, the violations identification procedure was time-consuming.

- The Law sets forth additional grounds to trigger investigation of antimonopoly legislation violations, which now include information contained in mass media.

4.10. Amendments Regarding Liability for Competition Legislation Violations

4.10.1. Administrative Liability

The Law introduces amendments into the Administrative Code pursuant to which fines on monopolistic activities are to be assessed not on the total income, as established before, but on income derived as a result of the antimonopoly legislation violation. On the one hand, this change plays into the hands of violators, but on the other hand, the practitioners are of opinion that it might be difficult to calculate the fines because, in some cases, it is fairly problematic to determine the exact amount of income obtained as a result of legislation violation (for example, in case of eliminating other market entities from the commodity market, as a result of which the violator increases its income from sales of own products) and, in some cases, such income may not arise (for example, in case of refusing to enter into contracts with certain sellers or buyers).

The following violations of antimonopoly legislation entail administrative liability:

- entering into anticompetitive agreements;

- performing anticompetitive concerted actions;

- abuse of dominant position;

- coordination of market entities' economic activities;

- performing economic concentration without Antimonopoly Agency's consent;

- failure to submit or untimely submission of the performed economic concentration notification to the Antimonopoly Agency;

- failure to fulfill Antimonopoly Agency's ordinances;

- anticompetitive actions of governmental agencies or local executive authorities.

It should be mentioned that the violations mentioned in p.p. 4) and 6) above fall under administrative liability for the first time. Previously, the legislation did not regard such acts as administrative violations, hence, envisaged no liability therefor.

If committing acts described in p.p. 1) – 3) above, one is liable to a fine in the amount of from 5% to 10% of the income derived as a result of monopolistic activities, with confiscation of monopolistic income[15]. In case of committing other acts, the fine amount ranges from 200 to 2,000 MCI.

[15] A market entity can derive monopolistic income as a result of: (1) anticompetitive agreement between, or concerted actions by, market entities; (2) the market entity's abuse of its dominant or monopolistic position.

4.10.2. Criminal Liability

Criminal liability is imposable in case of "market entities' establishing and/or maintaining monopolistically high (low) or concerted prices; establishing limitations on resale of goods (work, services) purchased from a market entity holding a dominant or monopolistic position based on territorial principle, circle of buyers, purchase conditions, quantity or price; dividing commodity markets based on territorial principle, assortment of goods (work, services) and volume of their sales or purchase, circle of sellers or buyers; and other acts aimed at competition restriction, if these have caused large damage to an individual, organization or the state or are associated with derivation of large income by the market entity" (paragraph 1 of Article 196 of the Criminal Code[16]).

The Law defines the large damage as damage caused to an individual for the amount exceeding 1,000 MCI or damage caused to an organization or the state for the amount exceeding 10,000 MCI, as established by the RK legislation as of the moment of the crime commission (paragraph 2 of Comments on Article 196 of the Criminal Code).

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[16] RK Criminal Code No. 167-I, dated 16 July 1997, as amended (hereinafter, the Criminal Code).