Privatization as an International Phenomenon: Kazakhstan

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PRIVATIZATION AS AN INTERNATIONAL PHENOMENON: KAZAKHSTAN

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[T]here is nothing more difficult to carry out, nor more doubtful of success, nor more
dangerous to handle, than to initiate a new order of things.
For the reformer has enemies in all those who profit by the old order, and only
lukewarm defenders in all those who would profit by the new order.¹

INTRODUCTION

All things are constantly changing in the world, and human society
is changing and developing as well. On September 15, 1998, George
Soros testified before the United States House of Representative's
Committee on Banking and Financial Services that all countries are
part of the global capitalist system, characterized as, "a gigantic cir-
culatory system, sucking up capital into the financial markets and in-
itutions at the center and pumping it out to the periphery either di-
rectly in the form of credits and portfolio investments, or indirectly
through multinational corporations."² Mr. Soros stated that up until
1997, financial markets were stable, at which point the situation be-
gan to rapidly change.³ Mr. Soros concluded that the collapse of the
global capitalist system will affect all financial markets and econo-
 mies and could not predict with certainty which economy would fall
next.⁴

In today's unstable economic times, when even some developed
economies are suffering a decline, making assessments is difficult.
Nonetheless, few could deny that historically the private sector often
provides the catalyst for societal growth.⁵ As such, the aim of this es-

¹. See NICCOLO MACHIAVELLI, THE PRINCE AND THE DISCLOSURES, Chap.
VI, at 21 (Luigi Ricci trans., 1950).

². International Economic Turmoil: Hearing Before the House Comm. on
Banking and Fin. Services, 105th Cong. (1998) (statement of George Soros) (vis-
and_Finance.txt>.

³. See id. (commenting on the Asian crisis, which resulted in a reversal of the
flow of capital from the periphery to the center).

⁴. See id. (urging Congress to support international institutions including
authorizing an increase in IMF capital to provide relief to countries already in fi-
nancial crisis).

⁵. See Michele Balfour & Cameron Crise, A Privatization Test: The Czech
Republic, Slovakia, and Poland, 17 FORDHAM INT'L L.J. 84, 85 (1993) (discussing
different privatization schemes and the necessary elements for successful privati-
zation); see also Peter Rutland, Privatization in East Europe: Another Case of
Words that Succeed and Policies that Fail?, 5 TRANSNAT'L L. & CONTEMP.

say is a delineation of common features of privatization worldwide, with an emphasis on the legal framework of privatization in Kazakhstan.

Part I of this essay provides the international substance of privatization, defines "privatization," and determines its forms and methods. Part II surveys the process of privatization in the Czech Republic, Poland, and Russia, with a broader review of Russian privatization legislation, as the experience of those countries has directly affected the Kazakhstani model of privatization. Part III extensively reviews the legal mechanisms of Kazakhstani privatization, as well as the legal provisions for foreign investor participation in the privatization process. The essay concludes by suggesting that the privatization process in Kazakhstan has been successful in overcoming the Soviet legacy and moving the country toward a more prosperous society.

I. PRIVATIZATION AS A WORLD-WIDE PROCESS

The world is currently experiencing a "privatization revolution"—State enterprises in Europe, Asia, Africa, and Latin America are in various stages of privatization. Privatization is an inevitable part of decentralizing a national economy. By reducing a government's role in the management of the country, privatization forces market mechanisms to work. As a result, advisors in countries of economic

PROBS. 1, 4-8 (1995) (discussing the different objectives of privatization, the implementation of privatization programs employed, and the effects of such programs).

6. Lawrence W. Reed, President, Mackinac Center for Public Policy, Adapted from Remarks to The Future of American Business, National Leadership Seminar (visited Mar. 29, 1999) <http://mackinac.org/topics/privatiz/privatiz.htm> (recognizing that improvements in mass communication and transportation have provided for an interdependent world, which lies at the root of today's privatization revolution).

7. See Pace of Privatisation Doubles, PRIVATISATION INT'L, Jan. 1, 1992, available in 1992 WL 2748240, at 1 (commenting that in 1991 profits from the sale of public enterprises to the private sector increased to nearly $50 billion, which was largely the result of privatization in Eastern Europe, Latin America, and Britain); see also Reed, supra note 6, at 3 (discussing privatization experiences in England). While Margaret Thatcher was Prime Minister, the British government sold seven major airports, British Telcom, many State enterprises, and a million units of public housing. See id. As a result, British markets became more competitive saving taxpayers significant sums of money. See id.
transition regard privatization as the primary means to create a market economy and to promote development.  

The necessity of privatization is based on human nature, which can be described in one sentence: "What you own, you take care of; what nobody or everybody owns falls into disrepair." A strong private sector creates more responsible suppliers and allows private citizens to become owners. Owners are likely to closely oversee management as they attempt to maximize profits. This naturally leads to the desire to better serve consumers and quickly respond to consumer demand, which creates competition, "the best governor of markets." Competition among owners distinguishes command economies from market economies, thriving in the latter and withering in the former.

In non-market countries with a centralized economy and a planned distribution of goods, the State is "everything." By substituting private ownership with public ownership, the State produces and distributes all goods and services. This unnatural function places a heavy burden on the State. The cost of the government's immense growth, which is one of the characteristics of a non-market economy,


9. Reed, supra note 6, at 3.


11. See id. (stating that competition "best governs" market economies by creating incentives for maximizing profits, thus insuring lower costs and better quality products/services for consumers).

12. See Reed, supra note 6, at 1 (reporting that although the government was running a budget deficit the bureaucracy still could not efficiently carry out its tasks).
creates a public burden on millions of people. Countries short on revenue are unable to increase taxes because they have already been raised to a critical level—increasing taxes would likely send people, businesses, and investors to "friendlier climates." After reaching this critical point, countries instead choose to transfer State ownership of commercial enterprises to private owners. In other words, State officials, in order to stay in power, are opting to privatize. Some researchers assert that if privatization is done properly and with due care, it will provide for increased market competition, accountability, and incentives, resulting in rapid economic growth. Privatization done poorly, however, can stagnate a country's economy. As such, privatization acts as a catalyst for transforming a national economy, but also requires the creation of legal, institutional, and fiscal mechanisms. The process of creating such mechanisms took developed countries centuries to accomplish, yet former Soviet countries are trying to complete the transformation process within a few years. Some scholars argue that a working market economy cannot be created through revolutionary policies. They assert that governments should allow State enterprises to "wither away slowly," allowing a legal and an institutional framework for new private enterprises to emerge. This essay, however, does not aim to discuss

13. See id. at 1 (noting that for governments of non-market economies, economic security took precedence over personal liberties and freedom of commerce).

14. See id. at 3 (recognizing that State officials also felt pressure to privatize when governments fell behind with technology and advances in production).

15. See RALPH H. FOLSOM ET AL., INTERNATIONAL BUSINESS TRANSACTIONS 892 (3d ed. 1995) (emphasizing that privatization is a long process that must be measured in decades rather than in years even after "the goal is made clear and obstacles removed").

16. See Reed, supra note 6, at 3 (asserting that many State officials resort to privatization as it is "the best or only" alternative they have).

17. See id. at 3 (stating that privatization has led local governments to experience cost savings of as much as 10 to 40 percent).

18. See Gordon, supra note 10, at 518.

19. See George Bogdan, The Economic and Political Logic of Mass Privatization in Czechoslovakia and Poland, 4 CARDOZO J. INT'L COMP. L. 43, 46 (1996) (asserting that market economies are of such a complex nature that market actors must develop the necessary skills and practices).

20. Compare id. (advocating that Eastern European economies should grow "spontaneously" from the private sector already in place), with Andrei A. Baev,
different ways to create a prosperous economy, but rather concentrates on schemes of privatization, which is a method of achieving prosperity.

Scholars differ on the precise definition of privatization. Some believe that privatization is "a conversion of businesses from governmental ownership to private," with de-nationalization of industry and freeing of the private sector to provide services that were previously considered governmental. Privatization in its broadest sense is the transfer of assets or services that are supported by public taxes to a market that is supported by entrepreneurial initiative and private competition. One scholar delineates privatization as "the single act of transferring (by the means of buying and selling) the legal title of State property, which was in the possession of State enterprises for restricted purposes of producing certain goods under owner-State control, to individual or associated owners." Although other definitions reflect the essence of privatization, only the last definition embodies the legal perspective of privatization.

Researchers distinguish between different forms of privatization, recognizing that it can be accomplished as either an intermediate or immediate process. Intermediate privatization involves the restructuring of State companies into joint-stock or limited liability companies that remain under State control. Immediate privatization is the rapid transfer of State property to private hands, and is usually accompanied by price liberalization and rapid changes in commercial legislation. As a result, some believe that only immediate privatization can produce real progress.

Civil Law and the Transformation of State Property in Post-Socialist Economies: Alternatives to Privatization, 12 UCLA PAC. BASIN L.J. 131, 137 (1993) (commenting that privatization is a way of "completely abolishing the basis of the whole socialist command system").

22. See Reed, supra note 6, at 1 (asserting that the superiority of a free market economy is now nearly undisputed).
23. Baev, supra note 20, at 150.
24. See FOLSOM, supra note 15, at 896 (stating that the restructured State companies are still State-owned, however, the companies are managed separately from the State budget).
25. See Nichols, supra note 8, at 303 (noting that western advisors generally support rapid transformation of ownership from the public to the private sector and...
Privatization can be accomplished by contracting State property to private citizens, distributing shares in previously owned State businesses, or liquidating unprofitable State enterprises. Theorists emphasize that the most common form of privatization is for the government to contract State property to private firms. This form is exercised through the execution of transparent and competitive contracts between private persons or companies and the State. These contracts usually impose few requirements on the acquiring company. Shares of State enterprises are distributed by auctions, allowing large dispersions of State property into private hands. Shares can be distributed for free, in exchange for vouchers/investment coupons, for money payments, or for future investments. Enterprises in poor financial condition are either liquidated by sale or the assets are transferred to private persons.

Commercialization is another form of privatization. There are different opinions regarding the definition of this process. The first opinion characterizes commercialization as the government’s decision to no longer engage in certain areas of production by simply allowing customers to contract with the provider of their choice. The second opinion, held in most former Communist countries, characterizes commercialization as the first step to privatization, by restructuring State enterprises into joint-stock or limited liability companies with the State appointing the board of directors. Shares of joint-stock companies and membership in limited liability companies can later be sold to private owners.

Researchers also recognize other forms of privatization. Such forms include: giving or selling State property in the form of physi-
cal assets to private entities, distributing vouchers for investment in State property, creating collective investment programs, leasing out the assets of State enterprises, and offering stock to the public. As a rule, countries undergo several forms of privatization on their road to a free market.

To be successful, privatization in countries with centrally-planned economies must attract foreign capital for the modernization of their facilities, adopt foreign management skills in order to capitalize on new technology, and provide sufficient internal financial and production controls. To attract foreign participation, a country would want to enact investment laws that facilitate the movement of capital into and out of the country.

II. PRIVATIZATION IN FORMER COMMUNIST COUNTRIES

Although calls for privatization began in the 1970s, most Communist countries did not begin to privatize State enterprises until the early 1990s. At that time, planned economies operated by producing identical goods in the same quantities, which were purchased on a regular basis, eventually stagnating the market. As a result, States experienced large budget deficits, hyperinflation, a decline in pro-

29. See Baev, supra note 20, at 180-88 (outlining different approaches to the privatization process); Nichols, supra note 8, at 304 (offering examples of mass privatization); Reed, supra note 6, at 3 (listing forms of privatization).

30. See Kenneth Anderson, Three Roles for the Private Equity Market in Foreign Investments, 13 AM. U. INT’L L. REV. 125, 126-27 (1997) (recognizing the difficulty in attracting foreign investors since investors are aware of the illiquidity of such investments and the need for active investment management).

31. See id. at 127 (noting that performing such functions “provides a daunting task in many places throughout the world”).

32. See Reed, supra note 6, at 1 (noting that during the 1970s, State officials and private citizens began to look for new solutions in response to “bloated, overbearing bureaucracies,” “crushing tax burdens,” and “frightening burdens of debts and deficits”).

duction, and reduced living standards. The State monopoly could no longer continue as governments soon realized that a free market system worked, while the socialist system did not. Thus, the decline of the Soviet-era began.

Researchers note that privatization in former Communist countries has several unique features that have not been experienced by capitalist countries. Soviet economics assumed that all means of production were concentrated in State hands. For at least fifty years, the government fixed prices by special edicts and distributed goods in accordance with plans prepared by the Communist Party. Consequently, the scale and features of privatization in post-Soviet countries were different from those of developed nations. First, no other country needed to transfer thousands of enterprises to the private sector. Second, privatization in almost all post-Soviet countries was completed within a short period of time—less than ten years. Third, post-Communist countries used more radical means for transferring State property to private owners. Furthermore, privatization in post-Soviet countries was unparalleled in history because it dealt with a specific collective mentality of people who were accustomed to living in a centralized system of distribution and, consequently, had no concept of the resourcefulness of private property.

The first important steps toward transferring State property in ex-Communist countries were taken in 1989-1990, when almost all ex-Communist countries started price liberalization and declared private property rights. This necessarily predicted privatization and served as


35. See Reed, supra note 6, at *1 (quoting “[w]hat had been ’socialized’ would have to be ‘privatized’”).

36. See Baev, supra note 20, at 133 (explaining that in socialist countries the term “ownership” is given a unique economic meaning such that capital assets are owned by the State and thus the community as a whole).

37. See Bogdan, supra note 19, at 44 (commenting that privatization in Eastern Europe differs from western privatization in that post-Communist countries must virtually create private property and capital markets where they previously did not exist).

38. See id.
grounds for the further development of a legal and institutional framework for a market economy.

A. PRIVATIZATION IN EASTERN EUROPEAN COUNTRIES

1. Privatization in the Czech Republic

The Czech Republic’s economy has been one of the most stable in Eastern Europe. After the break-up of the Soviet system, the Czech government rapidly converted its State-owned economy into a system of private enterprises. Critics found that the Czech Republic had developed a distinct model of mass privatization marked by unique auctions of State enterprises to voucher-holders. The estimated State revenue from privatization of both small and large enterprises was US$130 billion.

Privatization began in the Czech Republic in October 1990 when the country enacted new laws. Privatization was accomplished in two waves. During the first wave, which occurred from 1990 to 1993 in both the Czech Republic and Slovakia, 1492 State enterprises were privatized. During the second wave, which was conducted exclusively in the Czech Republic until 1995, an additional 1300 State companies were privatized.

During the first stage of privatization, legislation gave Czech citizens and legal entities an opportunity to become private owners of

39. See id.
40. See Balfour & Crise, supra note 5, at 93 (describing Czech privatization efforts).
41. See id. at 94 (noting Czechoslovakia’s unique voucher system); Bogdan, supra note 19, at 44 (describing the voucher system).
43. See Czechoslovak Law on Transfers of Some State-Owned Assets to Other Legal Entities or Persons, sec. 3 (1990), available in 1990 WL 488605 [hereinafter Czechoslovak Law on Transfers].
44. See Bogdan, supra note 19, at 51 (noting that the first wave involved Czech, Slovak, and federal firms).
45. See id.
small enterprises. Small enterprises were sold at auctions for money payment. Auctions were conducted in two rounds. If an enterprise was not sold to Czech citizens or Czech legal entities in the first round, then foreign natural and legal persons were entitled to bid in the second round. Small-scale privatization was virtually complete by January of 1993.

Large-scale enterprises had to propose their plans of privatization to the Ministry of Finance, which could approve or disapprove the proposed program. According to legislation, an enterprise could be sold directly to a bidding company, or indirectly to citizens or investment funds. Legislation did not restrict foreigners from the direct purchase of State enterprises, but it did limit foreigners from acquiring State property through investment funds.

The State also tried to protect the rights of its citizens to receive portions of State property. The government distributed investment coupons strictly to Czech citizens. During the first privatization wave, investment coupons had no real price—each coupon booklet equaled 1000 investment points. The coupons enabled the holder to purchase shares of joint-stock companies, or to acquire a participation-interest in investment companies. During the second wave of

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46. See Czechoslovak Law on Transfers, supra note 43, sec. 3.
47. See Andrus, supra note 42, at 615 (demonstrating the characteristics of the Small Scale Privatization Act).
48. See id.
49. See id. at 616 (specifying the characteristics of large-scale privatization enterprises).
50. See id. (noting the two methods of large-scale privatization are the direct sale method and the voucher system).
51. See id. at 619 (describing the Participation Act).
53. See id.
54. See Bogdan, supra note 19, at 50 (explaining the Czech model for citizens to obtain State property).
55. See Czechoslovak Act, supra note 52, art. 25.
privatization, investment coupons had a real money value, which was, however, fairly low.  

Czech legal and natural persons could purchase operational units of small enterprises at auctions. They also had a right to buy shares of larger enterprises either directly at auctions or indirectly by giving their vouchers to private investment companies. Investment companies collected the bulk of coupons. As a result, 432 investment companies controlled 72 percent of all issued coupons in the first wave of privatization, and the nine largest companies controlled up to fifty percent of all issued coupons in the second wave of privatization. By November 1994, the government conducted 11,200 voucher auctions.

In 1998, the Czech Republic continued its privatization efforts in the areas of banking, telecommunications, energy distribution, and financial services. As such, the Czech Republic has privatized almost all State commercial enterprises, mostly among its citizens and legal entities. According to commentators, the privatization effort

56. See Speed the Essence in Eastern Europe Q. Jeffrey Sachs, PRIVATISATION INT’L, Aug. 1, 1992, available in 1992 WL 2748768 (noting that Sachs, an advisor to several governments engaged in privatization, strongly supported the free transfer of ownership through coupons and vouchers). Sachs stated that whether citizens should have to pay for vouchers was relatively insignificant given that thousands of enterprises needed to be privatized. See id. According to Sachs, “[t]here are arguments for and against the kind of charge Czechoslovakia has levied... In Poland they did an opinion survey and the public felt quite strongly that there ought to be some charge... In Russia the intention is to keep the charge very low.” Id.

57. See Czechoslovak Law on Transfers, supra note 43, sec. 4.

58. See Bogdan, supra note 19, at 53 (explaining the investment structure of the voucher system).

59. See Rutland, supra note 5, at 13 (noting the effect of privatization measures in the Czech Republic).

60. See id. at 12.

61. See id. at 15.


63. See id. (noting the success of mass privatization efforts in Central and Eastern Europe).
appears to be an example of genuine democratic process.64 Czech privatization did not offer inducements to insiders of privatized enterprises, nor did it provide favors to workers and managers who participated in privatization on equal footing with non-workers. Moreover, Czech laws only placed reasonable limitations on the investment and acquisition activities of foreigners and legal persons.65 Lastly, during privatization, the Czech Republic entered into treaties with a number of countries.66 These treaties provide investment protection against expropriation, restrictions on private ownership rights, repatriation of earnings, and enforcement of intellectual property rights.67 As a result, the Czech Republic has experienced a rise in domestic business activity, an expansion in trade with the west, and an increase in the amount of foreign investment.68

2. Privatization in Poland

Because Poland is the largest country in Eastern Europe in terms of territory and population, its economy influences every Eastern European country.69 Privatization started rapidly in 1990 when the government lifted price controls, froze salaries, and terminated government subsidies to businesses.70 Polish officials are determined to continue economic reform toward eventual stability.

Poland enacted its first privatization law on July 13, 1990.71 The government also passed laws establishing the Ministry for Ownership Transformation, which promulgated procedures for implement-

64. See id.

65. See Mark Kreisel, Czech Republic: Investment in Freedom and the Future, INT'L DIMENSIONS, Fall 1997, at 6 (noting that the Czech Commercial Code provides foreign investors similar treatment to that of Czech citizens).

66. See id. (describing Czech efforts to protect property and earnings through treaties).

67. See id.

68. See id.

69. See Gordon, supra note 10, at 525 (noting the importance and impact of Poland’s privatization program).

70. See Sachs Interview, supra note 8, at 443 (describing economic “shock therapy” instituted by the Polish government on January 1, 1990).

71. See Polish Privatization Law No. 169 (1990), available in 1990 WL 488624.
ing privatization. State companies were divided into two main categories—the first group comprised 500 large enterprises, and the second group comprised 5500 small- and medium-sized enterprises. In mass privatization, large enterprises were transformed into corporations with further offerings of shares to third persons to ensure large diffusion of ownership, while other enterprises could be transferred to single buyers in whole. Although the citizens of Poland, like the citizens of Czech Republic, were given vouchers, they could not directly participate in auctions, but instead had to give their vouchers to national investment funds. There were approximately twenty investment funds at that time. Arguably, it was easier for the government to protect investors from potential fraud in light of the small number of investment funds.

Frequent changes in the Polish government usually created changes in privatization laws. The first plan of privatization granted enterprise shares in the following manner: ten percent to workers at no cost, thirty percent to all citizens in the form of vouchers, twenty percent to pension funds, ten percent to commercial banks, and thirty percent to Polish and foreign investors. Later, the government privatized State property according to another scheme: thirty-three percent of the company’s stock was granted to a single fund or a “core investor,” thirty percent remained in State possession for future sale or distribution, twenty-seven percent was distributed to investment

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74. See Polish Privatization Law, supra note 71, chs. 1-2.

75. See Bogdan, supra note 19, at 54 (comparing Poland’s privatization program to Czechoslovakia’s program). The government established half of the national investment funds. See id.

76. See Speed the Essence in Eastern Europe Q Jeffrey Sachs, supra note 56. Sachs stated that investment funds in Czechoslovakia were allowed to “spring up,” whereas in Poland great care was taken to license only a small number of firms. See id. According to Sachs, “[s]pontaneity has the advantage that it gets the juices flowing, but it has the disadvantage that people invest their money in completely unknown entities without sufficient legal protection.” Id.

77. See Polish Government Program for Privatization of Polish Economy, supra note 73, art. 2.1 (specifying that any unsold, outstanding shares would return to the Treasury).
groups in three blocks, and the remaining ten percent was given to employees.78

Legislation restricted foreign companies and natural persons from establishing investment funds, but permitted them to buy shares directly at auctions or by obtaining stock options.79 Foreigners could not obtain more than ten percent of a company's stock without a permit from the Foreign Investment Agency.80 Polish citizens, however, could sell their investment fund shares, which they received in exchange for vouchers, on the Stock Exchange. As such, virtually any person, either foreign or Polish, was able to buy shares of investment funds and obtain indirect possession of State enterprises during mass privatization.81

In 1998, upon completing small-scale and mass privatization, the Polish government began privatizing large banks, energy firms, telecommunications companies, insurance companies, and copper mining concerns.82 Privatizing only twenty percent of Polish Telecom's shares resulted in an estimated receipt of US$10 billion.83 While similar to Czech privatization efforts, Poland had its own path. Poland established and maintained control of a small number of investment funds in the process of mass privatization. Each employee of a State enterprise had an opportunity to become an owner of an enterprise.


79. See Bogdan, supra note 19, at 54 (noting that managers of privatizing companies were sometimes compensated with stock options, instead of wages).

80. See Polish Privatization Law, supra note 71, art. 19.2.

81. See generally id. arts. 19.2-19.3

82. See Gibbon, supra note 62, at 16 (describing the expansion of privatization to telecom companies).

83. See id. (noting that the sale of up to twenty percent of Polish telecom is the country's largest equity offering to date).
B. PRIVATIZATION IN RUSSIA

Privatization made its first steps in Russia in 1991. By that time, however, the government liberalized prices and declared private property rights. The Law on Privatization of State and Municipal Enterprises of 1991 declared the State's intention to privatize State-owned enterprises. Furthermore, it created the State Committee for State Property, responsible for enforcement of the privatization process.

During 1992-1993, the government privatized small retail and wholesale companies, food services, State agricultural enterprises and related repair and machine locations, unused facilities and incomplete construction projects, and road repair facilities. The government, however, prohibited privatizing major enterprises, those employing over 10,000 workers, and enterprises of national significance, such as military and defense, mining and natural resources, chemical, fuel and energy, air transportation, nuclear facilities, public transportation, higher education, medical facilities, and alcohol and tobacco production. Before privatizing, State enterprises converted to joint-stock companies with a future plan of distributing shares to the public.

In 1992, Boris Yeltsin, the President of the Russian Federation, introduced a program of voucher privatization called "mass privatization." This privatization program tried to create wealthy citizens who in turn would create a wealthy State. As much as forty to fifty

86. See id. at 6.
87. See id.
88. See Rutland, supra note 5, at 13 (describing Russia's 1992 privatization program).
89. See Moors, supra note 85, at 17-30 (analyzing the State program and describing the effects of the program).
90. See id. at 30; see also Raftopol, supra note 84, at 450 (describing how the
percent of State property was intended for privatization through vouchers. Voucher privatization was touted as a democratic process that would create millions of private owners. Many believed that removing the managerial function from the State, and putting it into the hands of individuals with a proprietary interest would create an incentive to make the enterprise efficient and profitable. The government provided each citizen with one voucher worth 10,000 Rubles. Although vouchers were intended as a means of payment for the purchase of either assets of State companies or shares of registered investment funds, they could also be traded in the market. Many citizens did not expect to receive benefits from the investment of vouchers since Russian citizens typically have low expectations of their government. Therefore, instead of participating in privatization, citizens chose to simply sell their vouchers, giving others the opportunity to obtain larger shares of the enterprises. Although the mass selling of vouchers led to their rapid devaluation, this program was claimed a success in terms of its scale: from the issuance of 150 million vouchers, the government collected 94 million vouchers and 40 million Russians became shareholders.

Legislation created favorable conditions for employees of privatizing enterprises. Employees were offered a buy-out program with three different options. The first option granted the employee a one-time opportunity to acquire up to twenty-five percent of the enter-

State program was intended to change the outlook of the Russian citizens by encouraging a sense of self-determination and individual accumulation of wealth).

93. See Raftopol, supra note 84, at 455 (describing the design, security protections and value of the vouchers that were distributed to all eligible citizens in October 1992).
94. See id. (explaining the options available to the voucher holder).
95. See id. at 450 (describing the nature of Russian citizens' attitude toward government).
prise's stock in the form of privileged shares at no cost, and granted the employee an option to purchase an additional ten percent of the enterprise's stock in the form of ordinary shares at a thirty percent discount from its nominal rate. The second option provided for the acquisition of fifty-one percent of the shares at their nominal value. The third option combined the previous two. Thus, if the workers obtained a maximum of fifty-one percent of the company's stock, and twenty percent of the stock went to the State, only twenty-nine percent of the shares remained. These shares were sold at auction, not for money, but rather for vouchers.

Besides citizens, there were other participants in the privatization process. A right to participate in privatization and obtain title to portions of State property went to investment funds and foreign investors. Investment funds acted as financial intermediaries in Russian privatization, balancing citizens' vouchers on one side, and shares of privatizing State enterprises on the other. For regulatory purposes, the Russian government required investment funds to register with the State Committee on State Property. Within a very short time, there were 300 investment funds with 700 branches throughout Russia. Despite a regulatory framework, some investment funds exploited people's trust by collecting large amounts of money and vouchers, only to disappear without a trace.

Foreigners could participate in the privatization process, but their role in mass privatization was limited by vague legislation. First, legislation provided that a foreigner could not participate directly in the privatization of medium-sized enterprises. This program was carried out exclusively by vouchers. Vouchers, however, were freely traded, which gave foreign investors an opportunity to purchase them. This enabled some foreign companies, as well as Russian citi-

97. See Moors, supra note 85, at 28.
98. See id. at 29.
99. See Rutland, supra note 5, at 14 (analyzing the success of the Russian privatization program).
100. See Raftopol, supra note 84, at 464 (describing the rapid expansion of investment funds in Russia in 1992).
101. See id. at 464-65 (illustrating investment fund embezzlement).
zens, to acquire stock.\textsuperscript{103} Foreign investors played relatively minor roles in the privatization of large enterprises.\textsuperscript{104}

The scale of mass privatization in Russia was astounding. Approximately 85,000 small enterprises and around 14,000 medium and large enterprises have been transferred to private hands. Close to 650 private investment funds collected nearly 94 million vouchers.\textsuperscript{105} The government held an estimated 11,200 voucher auctions.\textsuperscript{106} In 1997-1998, privatization continued with the sale of seventy large enterprises, some of which included oil, energy, and telecommunications companies.\textsuperscript{107}

Privatization in Russia had many positive points. It broke State monopolies and created an enormous number of private companies. Yet there have been problems associated with the policies. First, privatization legislation created the “loans-for-shares” scheme. This scheme privatized State companies by allowing private entities to finance their purchase.\textsuperscript{108} Second, the creation of large State holding companies in oil, gas, energy, and pipelines was problematic. Some of these interests still remain in State possession, undermining the development of the Russian economy.\textsuperscript{109} Third, rampant corruption emerged and now dominates the Russian economy.\textsuperscript{110} Fourth, privati-

\begin{enumerate}
\item See Raftopol, supra note 84, at 462 (citing as an example of foreign participation in mass privatization, a French company buying twenty percent of the Prem concrete plant).
\item “Influential outside investors with a substantial amount of shares relative to insider ownership are absent in Russia . . . .” Katharina Pistor, Privatization and Corporate Governance in Russia: An Empirical Study, in PRIVATIZATION, CONVERSION, AND ENTERPRISE REFORM IN RUSSIA 69 (Michael McFaul & Tova Perlmutter eds., 1995) (finding that outside investors, including both foreign and Russian investors other than employees and former employees of the enterprise, acquired a mean of 19 percent of the total stock).
\item See Creating Private Enterprises and Efficient Markets, supra note 96.
\item See Rutland, supra note 5, at 14.
\item See Gibbon, supra note 62, at 16.
\item See Moors, supra note 85, at 46 (describing the re-alignment of Russian oil interests into 10 organizations, each of which is substantially owned and controlled by the government).
\item See Daniel McGrory, Economic, Legal, and Political Dilemmas of Privati-
\end{enumerate}
zation was not transparent, as former factory managers, nomenclatura, and organized crime figures were able to concentrate a considerable amount of State property. A few "red directors" acquired State enterprises by appropriating company funds to buy a controlling number of shares, or forcing workers to give up their shares. This appropriation was supported in significant part by the so-called "Russian shadow," or informal economy. Researchers assert that these adverse features caused the Russian economy to crash during the summer of 1998.

III. LEGAL ASPECTS OF PRIVATIZATION IN KAZAKHSTAN

A. PRIVATIZATION LEGISLATION

"The affair can't be completed. Without difficulties nothing gets done, without striving the goal can not be reached." Kazakh proverb

The Republic of Kazakhstan is one of the Central Asian republics of the former Soviet Union ("USSR"). With a territory of 1,049,150 square miles, it is the second largest among the Commonwealth of

111. See J. Michael Waller, Author's Rebuttal to the Department of State, 5 DEMOKRATIZATSIYA: J. POST-SOVIET DEMOCRATIZATION pg. unavail. online (1997) (on file with American University International Law Review).

112. See Raftopol, supra note 84, at 467; Rutland, supra note 5, at 14 (providing an example where a director of one of the biggest Russian auto factories bought thirty percent of the company's shares through fifteen fictional companies using credits he obtained from banks).

113. See McGrory, supra note 110, at 71 (estimating that as much as forty percent of Russians personal income is derived from illegal sources).


Independent States ("CIS"). Its population is 16,672,000 people. Kazakhstan is rich in natural resources, which, according to the Constitution, belong to the Republic of Kazakhstan as a foundation of its sovereignty and independence. Also, Kazakhstan’s rich natural resources play an important role in the success of its privatization efforts by attracting both internal and external investors.

In early 1991, the Supreme Soviet of the Kazakh SSR—an authorized body of the State at that time—issued an edict, "On Main Directions of Destatization and Privatization of State Property in Kazakh SSR." The Supreme Soviet declared destatization and privatization to be the most important condition for the transition of the Kazakhstani economy to a free market system, strengthening the diversification of property rights, and developing entrepreneurial activity. This edict divided all State property into three groups: property of the USSR, property of the Kazakh SSR, and municipal property. Additionally, it established a State body for management of privatization—the State Committee of the Kazakh Soviet Socialist Republic on Management of State Property ("State Committee").


117. See id.

118. See id. Kazakhstani fields of chromium, vanadium, bismuth, phosphorite, and fluorine are known as the second largest in the world. See id. There are 160 known deposits of oil and gas, which contain approximately 20 billion barrels of oil and seven hundred million tons of natural gas. See id.

119. See KAZAKHSTAN CONST. art. VI, sec. 3, available in CONSTITUTIONS OF THE COUNTRIES OF THE WORLD 14 (Gisbert H. Flanz ed., 1996) ("The land and underground resources, waters, flora, and failure, other natural resources shall be owned by the state.")

120. See infra notes 138-40 and accompanying text (defining these terms at the various stages of privatization).


122. See id. sec. 4.1.

123. See id. sec. 4.
The State Committee determined financial sources for privatization and ascertained preferences to employees of the privatizing enterprises.\textsuperscript{124}

In December 1991, the presidents of the eleven republics of the former Soviet Union established the CIS and terminated the existence of the USSR.\textsuperscript{125} The USSR property located on the territories of sovereign republics became the property of those republics.\textsuperscript{126} This agreement recognized a transfer of the property of the USSR, as well as finances, enterprises, institutions, and subsidiaries, to the independent States.\textsuperscript{127} Thus, Kazakhstan acquired many resources of the USSR, including mills, plants, military bases, and even nuclear arms.

The process of privatization was not easy for the Republic of Kazakhstan. In addition to privatization, it had to declare private property rights, create legislation for the operation of private enterprises, establish methods for transferring State property to private parties, regulate bankruptcy procedures, and address other important questions necessary for the functioning of a market economy.\textsuperscript{128} The legislature issued many laws and regulations during the first year of privatization. Among the most important were the Law on Destatization and Privatization\textsuperscript{129} and the Program of Destatization and Privatization for 1991-1992.\textsuperscript{130} The legislation defined the main principles of

\begin{enumerate}
\item[124.] \textit{See id.} secs. 5, 8.
\item[127.] \textit{See id.}
\item[128.] \textit{See FOLSOM, supra note 15, at 893.}
Privatization was divided into three categories depending on the number of employees: small-scale privatization, mass privatization of medium-sized enterprises, and case-by-case privatization of large-scale enterprises. Enterprises with not more than two hundred employees were called "small," those with not more than five thousand employees were called "medium-sized," and large enterprises were those that had more than five thousand employees.

The process of privatization was divided into three stages. In the first stage, the State focused its efforts on the privatization of small enterprises, such as retail stores, wholesale companies, and service facilities. In the second stage, in addition to small-scale privatization, the State began mass privatization of medium-sized enterprises, including privatization of agricultural entities. Finally, in the third stage, case-by-case privatization began. Presumably, when privati-
zation is complete, the private sector will dominate the Kazakhstani economy.\textsuperscript{137}

1. First Stage of Privatization

In the first stage of privatization, the legislation distinguished the term "destatization" from the term "privatization."\textsuperscript{138} Destatization means the transformation of State enterprises, including management and corresponding functions, to private enterprises.\textsuperscript{139} Enterprises were transformed into joint-stock and limited liability companies with State ownership. This process was similar to the transformation of State property in other former Soviet countries. The definition of "privatization" means the acquisition of State property or shares of State companies by private persons and legal entities.\textsuperscript{140}

Many entrepreneurs privatized State property at the beginning of this period. The State Committee, its local branches, and municipal bodies authorized the sale of State enterprises and property.\textsuperscript{141} The distribution of power among the State and municipal bodies negatively affected privatization as a whole because the municipalities pursued independent decisions that were more profitable for their regions, while less profitable for the State as a whole. To counteract this problem, the government passed amendments in 1993 that transferred privatization authority to the State Committee. To further strengthen the power of the State Committee, its Chairman was nominated Deputy Prime Minister of the Republic.\textsuperscript{142}

Small enterprises were sold at auctions, which were carried out according to specific procedures.\textsuperscript{143} Auctions were, as a rule, closed.

\textsuperscript{137} See id. at introduction.

\textsuperscript{138} See Law on Privatization, supra note 129, art. 1.

\textsuperscript{139} See id.

\textsuperscript{140} See id.

\textsuperscript{141} See id. arts. 5, 6.

\textsuperscript{142} See Izmenenia v Zakon Kazakhskoi SSR "O pazgosudarstvlenii i privatizatsii" ot 22 maya 1993 goda [The Amendments to the Law on Destatization and Privatization May, 22, 1993], art. 10, available in Kazakhstani Legislation database (on file with American University International Law Review).

\textsuperscript{143} See Polozenie ob organizatcii auksionov, kommercheskih konkursov po priobreteniy ob'ektov gosudarstvenoi sobstvennosti v ramkah maloi privatizacii,
This essentially meant that participants sent their bids to the authorized body that later decided whose bid won.\textsuperscript{144} Citizens who resided in Kazakhstan for at least five years and legal entities of the Republic of Kazakhstan had an opportunity to participate in the first stage of privatization.\textsuperscript{145} Employees of small enterprises had some advantages, collectively they could obtain possession, a lease, or management rights to the State enterprise in the process of destatization and receive ten percent of the shares of the privatizing enterprise at no cost.\textsuperscript{146}

Although almost all State property was subject to privatization, unprofitable enterprises had to be sold first. Objects of exceptional State property, including land, natural resources, security and military interests, and other enterprises as determined by the Council of Ministries, could not be privatized.\textsuperscript{147} Enterprises within the Ministries of Education, Public Health, Communications, Energy, Geology, Mass-Media, and Aviation, and companies that produced poisonous or toxic materials could not be privatized in the first stage.\textsuperscript{145}

In addition to small-scale privatization and destatization of middle-size enterprises, the State sold its housing fund. Kazakhstani citizens were converted into owners of their homes and apartments through the privatization of the State housing fund.\textsuperscript{149} Privatization of the State housing fund was achieved by using investment coupons, which were given to citizens who permanently resided and worked in the Republic of Kazakhstan.\textsuperscript{150} Possession of these coupons enabled

\begin{itemize}
  \item 144. See Program of Privatization I Stage, supra note 130, sec. 2.
  \item 145. See id.
  \item 146. See id. sec. 3.
  \item 147. See id. sec. 7.
  \item 148. See id. sec. 8.
  \item 149. See id. sec. 6.
  \item 150. See Polozenie o kuponnom mehanizme privatizacii gosudarstvenoi sobsovennosti v Kazakhskoi SSR, odobreno Postanovleniem Presidentsa Kazakhskoi SSR ot 13 sentiabria 1991 goda 444 [On the Regulation of Coupon Mechanism of Privatization of State Property in Kazakh SSR, approved by the Edict of the Presi-
the holders to privatize State houses, as well as assets of agricultural enterprises. The State determined that the main purpose of privatization in the second stage would be to transfer medium-sized enterprises into private hands, through so-called "mass privatization." At least fifty-one percent of the ordinary shares of middle-size companies were offered to Privatization Investment Funds ("PIFs"), ten percent of privileged shares were given at no cost to employees, and thirty-nine percent of the enterprise's shares remained in State possession.

Kazakhstan issued a different type of privatization investment coupon for the acquisition of State enterprises during mass privatization. Unlike the coupons distributed in the first stage of privatization...
tion, private investment coupons ("PICs") were allocated among all citizens of the Republic of Kazakhstan in equal amounts during the second stage of privatization.\textsuperscript{158} PICs could not be exchanged for money and were deposited in special accounts in State banks.\textsuperscript{159} Legislation prohibited coupon-holders from investing coupons directly into a particular enterprise. The only way to use the coupons was to give them to authorized PIFs, which could participate at auctions and buy shares of State enterprises.\textsuperscript{160} PIF accumulation of PICs served to protect the shares of State enterprises from widespread dilution and also reduced investment risks for each citizen.\textsuperscript{161} The government subjected PIFs to regulatory controls by limiting their activities to securities investment. In addition, PIFs could not own more than twenty percent of any enterprise or invest in affiliated companies. PIFs could not issue bonds or possess more than five percent of all issued PICs.\textsuperscript{162} Although the government licensed two hundred PIFs to participate in mass privatization, the twenty largest PIFs collected sixty percent of the issued coupons.\textsuperscript{163} Coupon privatization was complete in 1996, with the sale of 1700 State enterprises.\textsuperscript{164} During the third stage of privatization, PIFs were transformed into mutual fund and investment companies, and were thereby authorized to issue securities and make diversified investments.\textsuperscript{165}

At the end of the second stage of privatization, existing legislation became outdated. As a result, the President of the Republic of Kazakhstan issued the Decree Having Authority of Law of the President of the Republic of Kazakhstan Concerning Privatization ("Decree").\textsuperscript{166} The Decree re-evaluated the definition of privatization and

\textsuperscript{158} See id.
\textsuperscript{159} See id.
\textsuperscript{160} See id.
\textsuperscript{161} See id.
\textsuperscript{162} See id.
\textsuperscript{163} See id.
\textsuperscript{164} See Nichols, supra note 8, at 313.
\textsuperscript{165} See Program of Privatization III Stage, supra note 136, at introduction.
\textsuperscript{166} Decree on Privatization, supra note 131. This Decree was issued when the
nullified the term “destatization,” since destatization was complete.\textsuperscript{167} It defined privatization as the sale of State property to natural persons and private and foreign legal entities by the State owner pursuant to special procedures.\textsuperscript{168} The subjects of privatization were State-owned enterprises and institutions. The government could sell all or part of the assets of an enterprise; subdivisions of an enterprise, and stock or shares in charter funds of economic partnerships.\textsuperscript{169} The definition of the term “buyer” also changed. Legal entities, including individuals, may be buyers, with the exception of those who (i) have State ownership of more than twenty percent, or (ii) have no right to participate in privatization according to the legislation of the Republic of Kazakhstan.\textsuperscript{170} There are also restrictions on purchases by joint-stock companies.\textsuperscript{171}

The Decree was novel in that it introduced two important environmental provisions. Article 18 requires the seller in case-by-case privatizations to disclose information about the ecological condition of the property to a buyer.\textsuperscript{172} In turn, the buyer can examine the environmental condition of the property.\textsuperscript{173} This provision is valid only for case-by-case privatizations; therefore, hundreds of buyers of smaller enterprises have no right to prove that assets of their company were polluted prior to purchase. They are, however, still liable for damages to the environment and to the public health caused by their purchased enterprise.\textsuperscript{174} Although the State assumes liability for

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\textsuperscript{167} See id. art. 1.

\textsuperscript{168} See id.

\textsuperscript{169} See id. art. 5.

\textsuperscript{170} See id. art. 2.

\textsuperscript{171} See id. (stating that a joint-stock company buyer may not purchase more than twenty-five percent of shares in another joint-stock company which holds some of the buyer’s stock).

\textsuperscript{172} See Decree on Privatization, supra note 131, art. 18.

\textsuperscript{173} See id.

\textsuperscript{174} See id. art. 23.
damage caused prior to privatization, it is almost impossible to determine when damage occurred if the environmental evaluation was not prepared during privatization of the enterprise.\textsuperscript{175} Thus, this provision has created disparity among buyers, giving preference to buyers of larger companies.

The Decree also provides that the sales agreement of an enterprise could be declared invalid by the courts.\textsuperscript{176} Such nullification of the sales contract can occur if: (i) the buyer had no right to participate in privatization, (ii) the buyer was granted illegal privileges and advantages, (iii) the selling procedure was violated, and (iv) any other reasons decided by the legislature within the Republic of Kazakhstan.\textsuperscript{177} This provision, however, is only enforceable against buyers within three years from the date of the conclusion of their privatization agreements.\textsuperscript{178} Dissolution of the agreement is also possible, and it must be conducted under the procedures specified in the Civil Code of the Republic of Kazakhstan. Parties must return everything acquired under the dissolved agreement, and the culpable party must reimburse the other party for its losses.\textsuperscript{179}

The second stage of privatization was successful in terms of its scale. The government sold hundreds of enterprises, including retail stores, public catering and service companies,\textsuperscript{180} drug stores, and a number of gasoline stations.\textsuperscript{181} Thousands of companies were transferred to employees.\textsuperscript{182} The program of mass privatization is com-

\begin{itemize}
\item \textsuperscript{175} See id.
\item \textsuperscript{176} See id. art. 25.
\item \textsuperscript{177} See id.
\item \textsuperscript{178} See Decree on Privatization, supra note 131, art. 25. Actions to invalidate an agreement may be brought by an interested entity or the Attorney General. See id. A further restriction on the statute of limitations is that the action must be brought within six months of the date the plaintiff knew, or should have known, of the grounds for invalidation. See id.
\item \textsuperscript{179} See id. art. 26.
\item \textsuperscript{180} See Program of Privatization III Stage, supra note 136, at introduction.
\item \textsuperscript{181} See Privatization in Kazakhstan, in A BULLETIN ISSUED IN BEHALF OF THE GKP-GKI IN KAZAKHSTAN, Jan./Feb. 1997 (visited Apr. 23, 1999) <http://www.kazecon.kz/survey/CCF/Feb_e.htm> (noting that there were small-scale privatization successes, including twenty-seven drug stores and twenty petroleum stations).
\item \textsuperscript{182} See Nichols, supra note 8, at 312 (stating that it was usually small enter-
\end{itemize}
plete as exemplified in the following situations: in case-by-case privatization, five enterprises were sold, forty-four enterprises were transferred to management, and 93 percent of all agricultural enterprises were sold as well. 183

3. Third Stage of Privatization

The third stage of privatization began in 1996, 184 with the goal of selling approximately 200 to 250 large enterprises and 1000 strategic enterprises. 185 Entities prohibited from sale in previous stages, such as oil, gas, refining, power, mining, transport, communications, metallurgy, health care, public education, science, and cultural enterprises, were all subject to privatization in the third stage. 186 Since these enterprises and institutions were the biggest and most important for the growth of the Republic of Kazakhstan, the government required a thorough analysis of the “buyers” bids by all the relevant ministries, State committees, and other central and local executive bodies. 187

Privatization continued through a sale of State enterprises at auctions or by the direct sale of an enterprise to the managing company. 188 The government conducted direct sales for large enterprises, which in the preliminary phase were leased or given to management with a buyout option. 189 An enterprise was given to management when privatization of the enterprise was not expedient. 190 Managers

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183. See Program of Privatization III Stage, supra note 136, at introduction.
184. See id.
185. See Emil Bukhman, The Cart Before the Horse: Anticipatory Securities Regulation in Kazakhstan, 22 BROOKLYN J. INT’L L. 535, 542 (1997) (stating that these companies will be subject to case-by-case privatization because each has financial or regulatory uniqueness).
186. See Program of Privatization III Stage, supra note 136, sec. 2.
187. See id. sec. 3.
188. See id. sec. 1.
189. See id.
190. See Polozenie o konkurse po zaklucheniyu kontrakta na upravlenie predpriyatiem (ob’ektom), Prilozenie k Postanovleniyu Kabineta Ministrov Respubliki Kazakhstan ot 20 iyulia 1993 goda 633 [On Tender For the Right to Manage an Enterprise (Object), the Second Appendix to Resolution of Cabinet of Ministers of the Republic of Kazakhstan, July 20, 1993, No. 633] sec. 3, available in Ka-
of State enterprises, through incentive contracts, could buy an enterprise if it fulfilled performance obligations. As many as forty of the large enterprises particularly attractive to investors were privatized through management contracts. The world's largest steel mill, Karmet, as well as major copper, chrome and aluminum mills, and oil and gas companies were sold to several foreign investors through management contracts. Legislation also permits cancellation of management contracts if management fails to meet performance expectations. The Kazakhstani government terminated contracts with several managers complaining that they failed to make the necessary investments and improvements while managing the companies.

Besides the direct sale of enterprises to managers, privatization proceeded using auctions and tenders. In auctions, the winner is the person who bids the highest price for the enterprise; in tenders, the winner is the person who offers the best conditions for investment into the enterprise, best management program, and so forth. All

zakhstani Legislation database (on file with American University International Law Review).

191. See id.

192. See Grigori A. Marchenko, The Development of the Corporate Securities Market in Kazakhstan, June 1997, para. 12 (visited Apr. 20, 1999) <http://www.kazecon.kz/English/tender3.htm>. Mr. Marchenko was the Chairman of the National Securities Commission in Kazakhstan. See id. He describes "management contracts" as a form of de facto privatization, whereby an enterprise is managed by an outside investor in return for a share in the enterprise's profits. See id. Typically, the investor makes contributions of working capital, employees, and other investments for the enterprise. See id. This arrangement is also called a "management trust," and the investor typically prepares the company for privatization. See Nichols, supra note 8, at 315. Although the investor receives a share of the company's profits, if any, the real benefit it accrues is the ability to have the first opportunity to acquire the company once it is offered for sale. See id.

193. See Marchenko, supra note 192, para. 12 (stating that Karmet is fully-owned by the British group, Ispat International, and that many other industrial enterprises are majority-owned by foreign investors).

194. See Nichols, supra note 8, at 316 (describing the Kazakhstani government's dismissal of the first two managers of the Karmet steel mill).

195. See id. The first two Karmet management contracts were terminated due to the failure of the managing company to make necessary investments to improve the operation and productivity of the mill. See id. Once the current owner, Ispat International, took over, productivity of the mill increased by 250 percent. See id.

196. See Decree on Privatization, supra note 131, art. 13.
natural persons, private legal entities, and even foreign legal entities that are registered for participation in an auction are allowed to bid. Auctions in the last stage of privatization, unlike the first stage, were open and transparent. Regulations required the authorized State Committee to publish information on the enterprises to be privatized in the official newspaper at least thirty days before the auction date. Auctions were conducted according to the English method of bidding—with price increases—and the Dutch method—with price reductions. The price of the privatizing enterprise, however, could not be more than ten percent below a price determined by the government.

Unlike privatization by auction, privatization through tenders was not always transparent. Tenders were conducted by a group of officials without publication of alternative proposals. As a result, the public did not know what particular criteria influenced the buyer’s choice. The tender winner was required to fulfill specific obligations, such as replace obsolete equipment, make determined investments, maintain a certain number of workers, or produce a specific kind of good. For example, in 1997, the Kazakhstani government asked investment companies interested in “blue chip” enterprises in the oil, gas, and telecommunications sectors to prepare their bid proposals. A variety of investment banks and funds, among them ABN AMRO, ING Barings, Salomon Brothers, Global Securities, Lazard Freres, Peregrine, Regent Pacific, BZW Barclays, and HSBC, sent their proposals from which the government chose the winners.
been criticism, however, that the government gives unfair advantages to these foreign investors.\textsuperscript{204} For example, the chrome supplier, Kazchrome, which had a 1995 annual profit of over $145 million, was sold to a foreign investor for $36.8 million through a tender.\textsuperscript{205} Such practices have given rise to concern among privatization participants about its transparency and fairness.

The State uses privatization proceeds differently depending on the circumstances. During the early stages of privatization, money was distributed among the State Reserve Fund, the State Fund on Economic Stabilization, and the Special Fund of the Kazakh SSR on Management of State Property.\textsuperscript{206} Subsequent legislation authorized the President of the Republic of Kazakhstan to determine where the money would go.\textsuperscript{207} Presently, the Decree on Privatization specifies that funds received from the sale of State property are to be included in the State’s revenues of the State budget, and are to be spent according to the Law on the State Budget of the Republic of Kazakhstan.\textsuperscript{208} Thus, privatization money, which was formerly distributed to a large number of institutions, is now concentrated in the budget and is allocated according to budgetary needs.

Privatization in Kazakhstan is almost complete. The program of privatization in the third stage provides for some post-privatization measures. Those measures, which can be taken by the government, include: (i) State guarantees for privatized enterprises in all forms of economic support and technical assistance, and (ii) State training programs for managers and specialists of privatized enterprises on how to operate in a market economy.\textsuperscript{209} The State also plans to foster

\textsuperscript{204} See Nichols, supra note 8, at 319 (describing potential problems and advantages which foreign investors may face when attempting to enter the Kazakhstan market).

\textsuperscript{205} See id. The author notes, however, that the low purchase price may be a result of external factors such as the investing company’s assumption of debt or the Kazakhstan government’s eagerness to privatize the company quickly. See id.

\textsuperscript{206} See Resolution on the General Directions of Privatization, supra note 121, para. 9.

\textsuperscript{207} See Law on Privatization, supra note 129, art. 23.

\textsuperscript{208} See Decree on Privatization, supra note 131, art. 20.

\textsuperscript{209} See Program of Privatization III Stage, supra note 136, sec. 4.
the growth of the securities market by creating a network of professional market participants, and improving the efficiency of stock exchange operations.210

B. PARTICIPATION OF FOREIGN INVESTORS IN THE PRIVATIZATION IN KAZAKHSTAN

In many post-Communist countries, privatization could not be successful without attracting foreign capital and foreign management. Foreign participation helps to introduce new technology and establish adequate systems of management and quality control.211 Generally, foreign direct investment plays "key roles in stimulating economies of developing states" and is seen as an "engine of growth."212 Governments attract foreign investors by providing different advantages, such as location of the enterprise, favorable tax rates and regulatory regimes, as well as political and economic stability of the particular country.213

In Kazakhstan, the President has repeatedly emphasized that foreign investment and strong foreign relations are essential for the effective development of Kazakhstani natural resources.214 He also stated that the foreign policy of the Republic of Kazakhstan aims to create and maintain strong external connections to achieve a successful realization of economic objectives, social and political stability, and peaceful relations.215 Since Kazakhstani policy is to attract foreign investors, legislation is intended to create a favorable investment climate. Researchers note that compared to other CIS republics, investment in Kazakhstan carries relatively low risk.216 As such, for-
eign direct investment in Kazakhstan had already reached US$1.2 billion by 1996.217 In 1998, the Kazakhstani State Budget alone received US$17.6 million in contributions from foreign investors, while the total amount of foreign direct investment reached US$184.9 million.218

Foreigners participated in Kazakhstan's privatization process since its inception. The Law on Destatization and Privatization allowed citizens of foreign States and foreign legal entities with offices in Kazakhstan to purchase assets or stock of privatizing enterprises, but excluded them from acquiring small enterprises in the first stage of privatization.219 Later, the government enacted special legislation that eliminated restrictions on foreign participation in small-scale privatization and reinforced foreign participation in case-by-case privatization on the basis of open competition with local investors.220 The 1995 Edict of the State Committee for State Property reflects unprecedented Kazakhstani efforts to create a favorable climate for foreign participation in small-scale privatization. The Edict provided foreign investors with an opportunity to participate in special auctions held exclusively for foreign investors.221 Foreign participation in mass privatization of middle-size enterprises, however, was still lim-
ited for the sake of the Kazakhstani population. Foreigners could not establish PIFs, purchase more than thirty percent of the shares of PIFs, or control more than a thirty-five percent market share of certain goods. Nonetheless, once the PICs were allocated to the PIFs and once trading of securities by PIFs began, foreigners were able to purchase shares and assets of former State companies.

Kazakhstani legislation guarantees foreigners the freedom of entrepreneurial activities by prohibiting the illegal interference of entrepreneurial activity by State officials who have supervisory functions. State officials who commit illegal acts are subject to dismissal from the State service and imposition of penalties in accordance with the administrative and criminal legislation of the Republic of Kazakhstan.

The Law on State Support of Direct Investments in the Republic of Kazakhstan fostered a favorable climate for foreign direct investment. The goal of this law was to accelerate the development of the production of goods, works, and services in the cardinal sectors of the economy. The law broadly defines foreign direct investment, but excludes those investments involving sovereign guarantees of the Republic of Kazakhstan, or those given as an official technical support or grant. The State guarantees the security of investment ac-

222. See Foreign Investors in the Process of Privatization, supra note 220, sec. 2.2.
223. See Twin-track Approach in Kazakhstan, supra note 156.
225. See id. sec. 1.
227. See id. art. 5.
228. See id. art. 2.
Privatization in Kazakhstan protects investors assets from repatriation and expropriation, safeguards investors from unscrupulous State officials, allows free transfer of capital and convertibility of currency, and includes choice of law provisions to insulate investors from amendments and additions to Kazakhstani laws. Kazakhstan also established a system of economic privileges for investors, including tax relief during the first five years and a reduction of taxes up to fifty percent in the following five years. The law also provides full or partial relief from tariffs on imported equipment and materials necessary for the development of the investment. Although Kazakhstani legislation has opened its economy for investment, some sectors, such as telecommunications, electrical infrastructure, oil and gas, agricultural, livestock and fertilizers, and investment in the new Kazakhstani capital, Astana, have an even more favorable regulatory regime.

The aforementioned privileges for foreign investors, however, are applicable only to those investors who conclude investment contracts with the authorized State Committee. Parties to a contract stipulate all grants and privileges to be given to a particular investor. Legislation specifies the terms and conditions required for the conclusion of the investment contract. As such, despite Kazakhstan's attractive investment incentives, investors are concerned about some issues. First, although legislation requires transparency in investment contracts and full disclosure of all documents related to planned investment, some foreign investors purchased large enterprises in Kazakhstan for a fraction of their real value. Second, bribery of State...
officials is still a potential problem, although it may be better pre-
vented with increased enforcement of the new Law on Fight with 

CONCLUSION

Kazakhstan has experienced both immediate and intermediate 
forms of privatization. In terms of the amount of property involved 
and the diversity of forms and methods, Kazakhstani privatization is 
comparable only with the Russian programs.

Kazakhstan employed a variety of privatization methods. They in-
clude small-scale, mass, and large-scale privatization, governed by 
the central State bodies with payment by cash or by investment cou-
pons. State property was transferred to its new owners by auctions, 
tenders, or directly to employees at no cost, or for a nominal charge. 
Legislation shaped privatization into three distinct stages. In the first 
stage of privatization, the Kazakhstani laws emphasized the sale of 
small enterprises, frequently to their workers, and the sale of State 
houses to current tenants. In the second stage, the government em-
phasized mass privatization of medium-size enterprises that were 
sold at auctions with payment by investment coupons. The govern-
ment expects privatization to be complete in the third and final stage 
with the sale of large and strategic enterprises. Foreign companies 
and natural persons have been encouraged to participate in this stage. 
Legislation has provided equal treatment of local and foreign partici-
pants in privatization. It has also guaranteed a favorable regime for 
foreign investors, free convertibility of currency, free transfer of 
capital, permanent legislation for investors, and the free exercise of 
property rights.

Finally, privatization in Kazakhstan changed the system of the na-
tional economy. It was an engine of institutional, legislative, organ-
izational, and social change. It is, therefore, appropriate to say that at 
the end of privatization, Kazakhstan has developed completely new 
legislation and created new institutions. Its legislation now reflects 
the world’s experience and provides for continuing changes in the 
Kazakhstani economy toward a free market with private property.

Scholars have differing opinions concerning what constitutes a 
successful privatization effort. Some scholars consider privatization 
to be successful depending upon how State property is allocated to
private hands, while others regard privatization success depending upon the amount of property privatized in the process. Consequently, some researchers, pointing out such negative features as corruption in the process of privatization, non-transparency, and allocation of State property in the hands of a shadow economy, assert that the whole privatization process has failed.\(^2^{36}\) Others, however, believe privatization has succeeded if almost all State property has been privatized, despite some negative features, and has failed if many enterprises still remain in a State’s possession.\(^2^{37}\) Accordingly, the latter argue that the task of privatization is simply to convert State enterprises into private companies using a variety of market mechanisms that make the economy more efficient.\(^2^{38}\)

Considering privatization in Kazakhstan from both points of view, it can be inferred that Kazakhstani privatization is a success. There is little evidence of unfairness and non-transparency, almost all State property was privatized, new legislation for support of market mechanisms was enacted, and new institutions were created. Furthermore, Kazakhstani State institutions and currency are stable. Moreover, the President of the Republic of Kazakhstan declared his adherence to the principles of building a democracy with a market economy by means of stable exterior and interior policies.\(^2^{39}\) He pledged that Kazakhstani citizens would gather the fruits of the State reforms soon.\(^2^{40}\)

\(^{236}\) See, e.g., Moors, supra note 85, at 51-52; Raftopol, supra note 84, at 467; Sterling, supra note 108.

\(^{237}\) See, e.g., William C. Philbrick, The Task of Regulating Investment Funds in the Formerly Centrally Planned Economies, 8 EMORY INT’L L. REV. 539, 552-57 (1994) (describing the successes and failures of privatization in Hungary, the Czech Republic and Russia); Sachs Interview, supra note 8, at 456-57 (proposing a system where companies are partially privatized immediately by the government giving up to fifty percent of the company’s shares to its employees and the general public).

\(^{238}\) See Sachs Interview, supra note 8, at 454-58 (expressing concern that traditional privatization by public offering is time consuming and may result in corporate waste while the ownership of the company is in transition).


\(^{240}\) See id.
In conclusion, the results of Kazakhstan’s enormous privatization effort will be clearer in time. Privatization has been one of the most important steps for the Republic of Kazakhstan in order to extinguish its Soviet legacy. Today, the private sector dominates the Kazakhstani economy and, consequently, the country achieved one of the steps toward its goal of building a prosperous future.