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## 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.<sup>1</sup>

## 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 circulatory system, sucking up capital into the financial markets and institutions at the center and pumping it out to the periphery either directly in the form of credits and portfolio investments, or indirectly through multinational corporations."<sup>2</sup> Mr. Soros stated that up until 1997, financial markets were stable, at which point the situation began to rapidly change.<sup>3</sup> Mr. Soros concluded that the collapse of the global capitalist system will affect all financial markets and economies and could not predict with certainty which economy would fall next.<sup>4</sup>

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.<sup>5</sup> As such, the aim of this es-

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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) (visited Mar. 29, 1999) <[http://www.soros.org/textfiles/speeches/091598\\_Banking\\_and\\_Finance.txt](http://www.soros.org/textfiles/speeches/091598_Banking_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 financial 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 privatization); 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.<sup>7</sup> 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

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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 Telecom, 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.<sup>8</sup>

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."<sup>9</sup> 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."<sup>10</sup> Competition among owners distinguishes command economies from market economies, thriving in the latter and withering in the former.<sup>11</sup>

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.<sup>12</sup> The cost of the government's immense growth, which is one of the characteristics of a non-market economy,

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8. See Philip M. Nichols, *Creating a Market Along the Silk Road: A Comparison of Privatization Techniques*, 29 N.Y.U. J. INT'L L. & POL. 299, 300 (1997) (providing a comparison of the methods of privatization selected by each of the five republics of Central Asia as a means of converting to a market economy); *Privatization in Poland: An Interview with Jeffrey Sachs*, 15 SUFFOLK TRANSNAT'L L.J. 441, 445 (1992) (emphasizing that State ownership should play a minor role in an economy while private ownership is essential to a market economy) [hereinafter *Sachs Interview*]; *Changes in Soviet Balance of Power Boost Market Prospects*, PRIVATISATION INT'L, Sept. 1, 1991, at 1, available in 1991 WL 2715792 (discussing the former Soviet republics and their plans for developing and implementing privatization programs).

9. Reed, *supra* note 6, at 3.

10. David Gordon, *Privatization in Eastern Europe: The Polish Experience*, 25 LAW & POL'Y INT'L BUS. 517, 518 (1994) (describing the efficient market theory).

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.<sup>13</sup> 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.”<sup>14</sup> After reaching this critical point, countries instead choose to transfer State ownership of commercial enterprises to private owners.<sup>15</sup> In other words, State officials, in order to stay in power, are opting to privatize.<sup>16</sup> 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.<sup>17</sup> 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.<sup>18</sup> 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.<sup>19</sup> 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.<sup>20</sup> This essay, however, does not aim to discuss

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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.<sup>21</sup> 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.<sup>22</sup> 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."<sup>23</sup> 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.<sup>24</sup> 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.<sup>25</sup>

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*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").

21. *Privatization*, available in MICROSOFT ENCARTA ENCYCLOPEDIA (1997).

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.<sup>26</sup> 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.<sup>27</sup> 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.<sup>28</sup> 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-

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western aid agencies, such as the World Bank, primarily apply the rapid transformation process).

26. See Reed, *supra* note 6, at 2 (listing the requirements of successful privatization as open, competitive bidding for contracts, use of precise contract terms, and close supervision over the enforcement of contract provisions).

27. See *id.* (asserting that benefits of commercialization to consumers include increased selection of producers and suppliers of goods/services providing for increased consumer choices and lower consumer costs).

28. See Joseph C. Bell, *Privatization in Central and Eastern Europe*, 752 PLI/CORP 385, 389 (1991) (explaining that directors are made primary shareholders of the firm to align their interests with the firm's profit maximizing interests, thereby facilitating the transformation to a market economy).



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.<sup>29</sup> 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.<sup>30</sup> To attract foreign participation, a country would want to enact investment laws that facilitate the movement of capital into and out of the country.<sup>31</sup>

## II. PRIVATIZATION IN FORMER COMMUNIST COUNTRIES

Although calls for privatization began in the 1970s,<sup>32</sup> 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.<sup>33</sup> As a result, States experienced large budget deficits, hyperinflation, a decline in pro-

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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").

33. See *Introduction: Privatization—The Global Scale-Back of Government Involvement in National Economics*, 48 ADMIN. L. REV. 435, 435-36 (1996) (explaining that State-owned producers overproduce unwanted goods and underproduce wanted goods creating shortages of goods in demand, as central planners cannot respond to changes in consumer demand or produce substitute goods).

duction, and reduced living standards.<sup>34</sup> The State monopoly could no longer continue as governments soon realized that a free market system worked, while the socialist system did not.<sup>35</sup> 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.<sup>36</sup> 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.<sup>37</sup> 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.<sup>38</sup>

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

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34. See Paul B. Stephan, III, *Toward a Positive Theory of Privatization – Lessons from Soviet Type Economies*, 16 INT'L REV. L. & ECON. 173, 182 (1996) (providing common economic traits experienced by planned economies in response to stagnant market conditions).

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.<sup>39</sup> After the break-up of the Soviet system, the Czech government rapidly converted its State-owned economy into a system of private enterprises.<sup>40</sup> Critics found that the Czech Republic had developed a distinct model of mass privatization marked by unique auctions of State enterprises to voucher-holders.<sup>41</sup> The estimated State revenue from privatization of both small and large enterprises was US\$130 billion.<sup>42</sup>

Privatization began in the Czech Republic in October 1990 when the country enacted new laws.<sup>43</sup> 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.<sup>44</sup> During the second wave, which was conducted exclusively in the Czech Republic until 1995, an additional 1300 State companies were privatized.<sup>45</sup>

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

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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).

42. *See* Sarah Andrus, *The Czech Republic and Slovakia: Foreign Participation in Changing Economies*, 17 HASTINGS INT'L & COMP. L. REV. 611, 614 (1994) (discussing the evolution of investment legislation in the Czech Republic and Slovakia).

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.<sup>46</sup> 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.<sup>47</sup> Small-scale privatization was virtually complete by January of 1993.<sup>48</sup>

Large-scale enterprises had to propose their plans of privatization to the Ministry of Finance, which could approve or disapprove the proposed program.<sup>49</sup> According to legislation, an enterprise could be sold directly to a bidding company, or indirectly to citizens or investment funds.<sup>50</sup> Legislation did not restrict foreigners from the direct purchase of State enterprises, but it did limit foreigners from acquiring State property through investment funds.<sup>51</sup>

The State also tried to protect the rights of its citizens to receive portions of State property.<sup>52</sup> The government distributed investment coupons strictly to Czech citizens.<sup>53</sup> During the first privatization wave, investment coupons had no real price—each coupon booklet equaled 1000 investment points.<sup>54</sup> The coupons enabled the holder to purchase shares of joint-stock companies, or to acquire a participation-interest in investment companies.<sup>55</sup> 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).

52. See Czechoslovak Act of Feb. 26, 1991 on Conditions of Transfer of State Property to Other Persons (Large Privatization Law) arts. 22-26 (1991), available in 1991 WL 501310 [hereinafter Czechoslovak 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.<sup>56</sup>

Czech legal and natural persons could purchase operational units of small enterprises at auctions.<sup>57</sup> 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.<sup>58</sup> Investment companies collected the bulk of coupons.<sup>59</sup> 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.<sup>60</sup> By November 1994, the government conducted 11,200 voucher auctions.<sup>61</sup>

In 1998, the Czech Republic continued its privatization efforts in the areas of banking, telecommunications, energy distribution, and financial services.<sup>62</sup> As such, the Czech Republic has privatized almost all State commercial enterprises, mostly among its citizens and legal entities.<sup>63</sup> According to commentators, the privatization effort

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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.

62. See Henry Gibbon, *Pressing Ahead with Structural Reforms (Privatization of Telecommunication Companies in Central and Eastern Europe)*, PRIVATIZATION INT'L, June 1, 1998, at 16, available in 1998 WL 18957823 (highlighting the expansion of privatization in the telecom sector).

63. See *id.* (noting the success of mass privatization efforts in Central and Eastern Europe).

appears to be an example of genuine democratic process.<sup>64</sup> 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.<sup>65</sup> Lastly, during privatization, the Czech Republic entered into treaties with a number of countries.<sup>66</sup> These treaties provide investment protection against expropriation, restrictions on private ownership rights, repatriation of earnings, and enforcement of intellectual property rights.<sup>67</sup> 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.<sup>68</sup>

## 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.<sup>69</sup> Privatization started rapidly in 1990 when the government lifted price controls, froze salaries, and terminated government subsidies to businesses.<sup>70</sup> Polish officials are determined to continue economic reform toward eventual stability.

Poland enacted its first privatization law on July 13, 1990.<sup>71</sup> The government also passed laws establishing the Ministry for Ownership Transformation, which promulgated procedures for implement-

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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.<sup>72</sup> 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.<sup>73</sup> 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.<sup>74</sup> 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.<sup>75</sup> There were approximately twenty investment funds at that time.<sup>76</sup> 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.<sup>77</sup> 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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72. See Polish Law Establishing Office of Minister for Ownership Transformation Act of July 13, 1990, art. 1, *available in* 1990 WL 488624.

73. See Polish Government Program for Privatization of Polish Economy, Feb. 12, 1990, at 1, *available in* 1990 WL 488633.

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.<sup>78</sup>

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.<sup>79</sup> Foreigners could not obtain more than ten percent of a company's stock without a permit from the Foreign Investment Agency.<sup>80</sup> 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.<sup>81</sup>

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.<sup>82</sup> Privatizing only twenty percent of Polish Telecom's shares resulted in an estimated receipt of US\$10 billion.<sup>83</sup> 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.

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78. See Bogdan, *supra* note 19, at 54 (explaining the role of investment funds in the mass privatization plan). See generally Lawrence S. Michel & Brian Ngo, *Case Study: Privatization in Poland* (visited Apr. 4, 1999) <<http://www.worldbank.org/html/edi/cases/poland.html#briefing>>.

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.<sup>84</sup> 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.<sup>85</sup>

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.<sup>86</sup> 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.<sup>87</sup> Before privatizing, State enterprises converted to joint-stock companies with a future plan of distributing shares to the public.<sup>88</sup>

In 1992, Boris Yeltsin, the President of the Russian Federation, introduced a program of voucher privatization called "mass privatization."<sup>89</sup> This privatization program tried to create wealthy citizens who in turn would create a wealthy State.<sup>90</sup> As much as forty to fifty

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84. See Anthony V. Raftopol, *Russian Roulette: A Theoretical Analysis of Voucher Privatization in Russia*, 11 B.U. INT'L L.J. 435, 451 (1993) (reviewing Russia's post-1991 economic plan).

85. See Kent F. Moors, *The Failure of Russian Privatization 1992-1994: How the Industrial Nomenclatura Prevented Genuine Reform*, 3 J. INT'L LEGAL STUD. 1, 2 (1997) (describing the influence of the bureaucracy on the privatization process in Russia).

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.<sup>91</sup> 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.<sup>92</sup> The government provided each citizen with one voucher worth 10,000 Rubles.<sup>93</sup> 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.<sup>94</sup> Many citizens did not expect to receive benefits from the investment of vouchers since Russian citizens typically have low expectations of their government.<sup>95</sup> 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.<sup>96</sup>

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-

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

91. See *Privatization Programme Implemented*, ITAR-TASS, July 21, 1992, available in LEXIS, Nexis Library, TASS File.

92. See Fred Hiatt, *Russia Starts Large-Scale Privatization: Eight Volgograd Factories Put on the Auction Block*, WASH. POST, Feb. 9, 1993, at A12 (summarizing the goals of the State Program for Privatization of State and Municipal Enterprises in the Russian Federation for 1992).

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).

96. See *Creating Private Enterprises and Efficient Markets*, RUSSIA REFORM MONITOR, Jan. 1995 (visited Apr. 7, 1999) <[http://www.wired.com/collections/multimedia/6.01\\_st\\_petersburg8.htm](http://www.wired.com/collections/multimedia/6.01_st_petersburg8.htm)>.

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.<sup>97</sup> 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.<sup>98</sup> 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.<sup>99</sup>

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.<sup>100</sup> 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.<sup>101</sup>

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.<sup>102</sup> Vouchers, however, were freely traded, which gave foreign investors an opportunity to purchase them. This enabled some foreign companies, as well as Russian citi-

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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).

102. See Changes in Soviet Balance of Power Boost Market Prospects, PRIVATIZATION INT'L, Sept. 1, 1991, available in 1991 WL 2715792.

zens, to acquire stock.<sup>103</sup> Foreign investors played relatively minor roles in the privatization of large enterprises.<sup>104</sup>

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.<sup>105</sup> The government held an estimated 11,200 voucher auctions.<sup>106</sup> In 1997-1998, privatization continued with the sale of seventy large enterprises, some of which included oil, energy, and telecommunications companies.<sup>107</sup>

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.<sup>108</sup> 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.<sup>109</sup> Third, rampant corruption emerged and now dominates the Russian economy.<sup>110</sup> Fourth, privati-

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103. 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).

104. "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).

105. See *Creating Private Enterprises and Efficient Markets*, *supra* note 96.

106. See Rutland, *supra* note 5, at 14.

107. See Gibbon, *supra* note 62, at 16.

108. See Bruce Sterling, *Art and Corruption*, (visited Apr. 7, 1999) <[http://www.wired.com/collections/multimedia/6.01\\_st\\_petersbutg5.htm](http://www.wired.com/collections/multimedia/6.01_st_petersbutg5.htm)>.

109. 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).

110. See Daniel McGrory, *Economic, Legal, and Political Dilemmas of Privati-*

zation was not transparent, as former factory managers, nomenclatura, and organized crime figures were able to concentrate a considerable amount of State property.<sup>111</sup> 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.<sup>112</sup> This appropriation was supported in significant part by the so-called "Russian shadow," or informal economy.<sup>113</sup> Researchers assert that these adverse features caused the Russian economy to crash during the summer of 1998.<sup>114</sup>

### 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<sup>115</sup>

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

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*zation in Russia: Civilizing the Russian Underground Economy and Prospects for Establishing a Civil Economy in Russia*, 5 TRANSNAT'L L. & CONTEMP. PROBS. 65 (1995) (tracing the link between the underground economy under the Soviet regime and corruption in privatization efforts).

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).

114. See Merton J. Peck, *Russian Privatization: What Basics Does it Provide for a Market Economy*, 5 TRANSNAT'L L. & CONTEMP. PROBS. 21, 27-31, 36-37 (1996).

115. Nursultan Nazarbaev, Speech on the Situation in the Country and Major Directions of Domestic and Foreign Policy: Democratization, Economic and Political Reform for the New Century (Sept. 30, 1998) (visited Apr. 7, 1999) <<http://www.president.kz/main/mainframe.asp?Eng=en>>.

Independent States ("CIS").<sup>116</sup> Its population is 16,672,000 people.<sup>117</sup> Kazakhstan is rich in natural resources,<sup>118</sup> which, according to the Constitution,<sup>119</sup> 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<sup>120</sup> 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.<sup>121</sup> This edict divided all State property into three groups: property of the USSR, property of the Kazakh SSR, and municipal property.<sup>122</sup> 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").<sup>123</sup>

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116. See GENERAL INFORMATION ABOUT KAZAKHSTAN (visited Apr. 7, 1999) <<http://www.president.kz/main/mainframe.asp?Eng=en>>.

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 fauna, 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).

121. See Postanovlenie Verhovnogo Soveta Kazakhskoi SSR, Ob osnovnih napravleniakh razgosudarstvleniia i privatizatsii gosudarstvennoi sobsovennosti v Kazakhskoi SSR [Resolution of the Supreme Soviet of the Kazakh SSR, on the General Directions of Transformation and Privatization of State Property in Kazakh SSR, Feb. 16, 1991], available in Kazakhstani Legislation database [hereinafter Resolution on the General Directions of Privatization] (on file with *American University International Law Review*).

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.<sup>124</sup>

In December 1991, the presidents of the eleven republics of the former Soviet Union established the CIS and terminated the existence of the USSR.<sup>125</sup> The USSR property located on the territories of sovereign republics became the property of those republics.<sup>126</sup> This agreement recognized a transfer of the property of the USSR, as well as finances, enterprises, institutions, and subsidiaries, to the independent States.<sup>127</sup> 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.<sup>128</sup> The legislature issued many laws and regulations during the first year of privatization. Among the most important were the Law on Destatization and Privatization<sup>129</sup> and the Program of Destatization and Privatization for 1991-1992.<sup>130</sup> The legislation defined the main principles of

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124. See *id.* secs. 5, 8.

125. See Letter dated 27 December 1991 from the Permanent Representative of Belarus to the United Nations addressed to the Secretary-General, U.N. GAOR, 47th Sess., U.N. Doc. A/47/60 (1991) (reporting the Alma Ata agreements that established the Commonwealth of Independent States).

126. See, e.g., KAZAKHSTAN CONST. art. II, sec. 2, available in CONSTITUTIONS OF THE COUNTRIES OF THE WORLD 11 (Gisbert H. Flanz ed., 1996) ("The sovereignty of the Republic of Kazakhstan extends over its entire territory. The State ensures integrity, inviolability and inalienability of its territory.").

127. See *id.*

128. See FOLSOM, *supra* note 15, at 893.

129. See Zakon Kazakhskoi SSR "O pazgosudarstvlenii i privatizacii" ot 22 iynia 1991 goda [The Law on Destatization and Privatization, June 22, 1991], available in Kazakhstani Legislation database [hereinafter Law on Privatization] (on file with American University International Law Review).

130. See O Programme razgosudarstvleniya i privatizacii gosudarstvennoi sobstvennosti v Kazakhskoi SSR na 1991-1992 god (I etap) [On the Program of Destatization and Privatization of State Property in Kazakh SSR in 1991-1992 (First stage)], available in Kazakhstani Legislation database [hereinafter Program

privatization as the following: publicity, competition, legal succession, the responsibility of the State officials to carry out privatization by transparent methods, and availability of information concerning the property for sale to the Kazakhstani population.<sup>131</sup>

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.<sup>132</sup> 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.<sup>133</sup>

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.<sup>134</sup> In the second stage, in addition to small-scale privatization, the State began mass privatization of medium-sized enterprises, including privatization of agricultural entities.<sup>135</sup> Finally, in the third stage, case-by-case privatization began.<sup>136</sup> Presumably, when privati-

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of Privatization I Stage] (on file with *American University International Law Review*).

131. See Decree Having Authority of Law of the President of the Republic of Kazakhstan on Privatization, art. 4., Dec. 23, 1995 (visited Apr. 7, 1999) <<http://www.kazecon.kz/law/law-eng/PRIV-ENG.HTM>> [hereinafter Decree on Privatization].

132. See Program of Privatization I Stage, *supra* note 130, sec. 1 (outlining the three privatization categories).

133. See Nacional'naya programma razgosudarstvleniya i privatizatsii v Respublike Kazakhstan na 1993-1995 godi (II etap), adobrena Ukazom Prezidenta Respubliki Kazakhstan ot 5 marta 1993 goda [National Program of Destatization and Privatization in the Republic of Kazakhstan in 1993-1995 (II stage), approved by the President of the Republic of Kazakhstan, Mar. 5, 1993], available in Kazakhstani Legislation database [hereinafter Program of Privatization II Stage] (on file with *American University International Law Review*).

134. See Program of Privatization I Stage, *supra* note 130, sec. 1.

135. See Program of Privatization II Stage, *supra* note 133, sec. 1.

136. See Programma privatizatsii i restrukturizatsii gosudarstvennoi sobstvennoi v Respubliki Kazakhstan na 1996-1998 godi (III etap), odobrena Postanovleniem Pravitel'stva Respubliki Kazakhstan ot 27 fevralia, 1996 goda 246 [The Program of Privatization and Restructuring of State Property in the Republic of Kazakhstan in Feb. 27, 1997, No. 246], available in Kazakhstani Legislation database [hereinafter Program of Privatization III Stage] (on file with *American University Inter-*



zation is complete, the private sector will dominate the Kazakhstani economy.<sup>137</sup>

### *1. First Stage of Privatization*

In the first stage of privatization, the legislation distinguished the term "destatization" from the term "privatization."<sup>138</sup> Destatization means the transformation of State enterprises, including management and corresponding functions, to private enterprises.<sup>139</sup> 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.<sup>140</sup>

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.<sup>141</sup> 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.<sup>142</sup>

Small enterprises were sold at auctions, which were carried out according to specific procedures.<sup>143</sup> Auctions were, as a rule, closed.

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*national Law Review*).

137. See *id.* at introduction.

138. See Law on Privatization, *supra* note 129, art. 1.

139. See *id.*

140. See *id.*

141. See *id.* arts. 5, 6.

142. See *Izmeneniia 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*).

143. See *Polozhenie ob organizatsii aukcionov, kommercheskih konkursov po priobreteniiu ob'ektov gosudarstvennoi sobstvennosti v ramkakh maloi privatizatsii*,

This essentially meant that participants sent their bids to the authorized body that later decided whose bid won.<sup>144</sup> 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.<sup>145</sup> 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.<sup>146</sup>

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.<sup>147</sup> 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.<sup>148</sup>

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.<sup>149</sup> 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.<sup>150</sup> Possession of these coupons enabled

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Postanovlenie Gosudaerstvennogo Komiteta Po Upravleniyu Gosimuschestvom Respubliki Kazakhstan ot 4 aprelya 1993 goda [On Organization of Auctions, and Tenders for Acquisition of State Property in Small Privatization, Apr. 4, 1993], available in Kazakhstani Legislation database (on file with *American University International Law Review*).

144. See Program of Privatization I Stage, *supra* note 130, sec. 2.

145. See *id.*

146. See *id.* sec. 3.

147. See *id.* sec. 7.

148. See *id.* sec. 8.

149. See *id.* sec. 6.

150. See Polozhenie o kuponnom mehanizme privatizatsii gosudarstvennoi sobsovennosti v Kazakhskoi SSR, odobreno Postanovleniem Prezidenta 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.<sup>151</sup> One could assign his or her coupons only to direct relatives as a gift or bequest.<sup>152</sup> Presumably, the amount of coupons given to each working citizen was approximately enough for privatizing an ordinary one-bedroom apartment or a house. If a coupon-holder did not have enough coupons, he could pay the rest of the price in cash.<sup>153</sup> Case-by-case privatization at that time was moving slowly, due to lengthy preparation of detailed evaluations and plans for each item. Privatization in the agricultural sector was limited to selling, leasing, or transferring assets of agricultural enterprises, while agricultural land was barred from privatization.<sup>154</sup>

## 2. Second Stage of Privatization

Starting in 1993, the second stage of privatization ensued with legislation providing for the complete privatization of small enterprises and the housing fund, as well as a continuation of the case-by-case and agricultural complex privatization.<sup>155</sup> 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.<sup>156</sup>

Kazakhstan issued a different type of privatization investment coupon for the acquisition of State enterprises during mass privatization.<sup>157</sup> Unlike the coupons distributed in the first stage of privatiza-

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dent of the Republic of Kazakhstan, Sept. 13, 1991, No. 444] sec. 1, para. 1, *available in* Kazakhstani Legislation database (on file with *American University International Law Review*).

151. *See id.* para. 4.

152. *See id.* (noting that citizens were prohibited from selling their coupons).

153. *See id.* para. 11.

154. *See* Program of Privatization I Stage, *supra* note 130, sec. 7.

155. *See* Program of Privatization II Stage, *supra* note 133, at introduction.

156. *See Twin-track Approach in Kazakhstan*, PRIVATIZATION INT'L, Mar. 1, 1994, *available in* 1994 WL 2547365.

157. *See* Program of Privatization II Stage, *supra* note 133, art. 3.

tion, private investment coupons ("PICs") were allocated among all citizens of the Republic of Kazakhstan in equal amounts during the second stage of privatization.<sup>158</sup> PICs could not be exchanged for money and were deposited in special accounts in State banks.<sup>159</sup> 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.<sup>160</sup> PIF accumulation of PICs served to protect the shares of State enterprises from widespread dilution and also reduced investment risks for each citizen.<sup>161</sup> 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.<sup>162</sup> Although the government licensed two hundred PIFs to participate in mass privatization, the twenty largest PIFs collected sixty percent of the issued coupons.<sup>163</sup> Coupon privatization was complete in 1996, with the sale of 1700 State enterprises.<sup>164</sup> 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.<sup>165</sup>

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").<sup>166</sup> The Decree re-evaluated the definition of privatization and

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158. *See id.*

159. *See id.*

160. *See id.*

161. *See id.*

162. *See id.*

163. *See Nichols, supra* note 8, at 313.

164. *See* Program of Privatization III Stage, *supra* note 136, at introduction.

165. Zakon Respubliki Kazakhstan "Ob investitsionnih fondah" ot 6 marta 1997 goda. [Law of the Republic of Kazakhstan on Investment Funds, Mar. 6, 1997] art. 1, available in Kazakhstani Legislation database (on file with *American University International Law Review*).

166. Decree on Privatization, *supra* note 131. This Decree was issued when the

nullified the term "destatization," since destatization was complete.<sup>167</sup> 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.<sup>168</sup> 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.<sup>169</sup> 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.<sup>170</sup> There are also restrictions on purchases by joint-stock companies.<sup>171</sup>

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.<sup>172</sup> In turn, the buyer can examine the environmental condition of the property.<sup>173</sup> 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.<sup>174</sup> Although the State assumes liability for

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Parliament of the Republic of Kazakhstan was dissolved, and the President, according to Article 1 of the law of the Republic of Kazakhstan "Concerning the Temporary Delegation of Additional Authorities to the President of the Republic of Kazakhstan and the Heads of Local Administrations," dated December 10, 1993, received additional authority. *See id.* preamble. The President was therefore able to issue decrees, which have the authority of law.

167. *See id.* art. 1.

168. *See id.*

169. *See id.* art. 5.

170. *See id.* art. 2.

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).

172. *See* Decree on Privatization, *supra* note 131, art. 18.

173. *See id.*

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.<sup>175</sup> 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.<sup>176</sup> 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.<sup>177</sup> This provision, however, is only enforceable against buyers within three years from the date of the conclusion of their privatization agreements.<sup>178</sup> 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.<sup>179</sup>

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,<sup>180</sup> drug stores, and a number of gasoline stations.<sup>181</sup> Thousands of companies were transferred to employees.<sup>182</sup> The program of mass privatization is com-

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175. *See id.*

176. *See id.* art. 25.

177. *See id.*

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.*

179. *See id.* art. 26.

180. *See* Program of Privatization III Stage, *supra* note 136, at introduction.

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](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).

182. *See* Nichols, *supra* note 8, at 312 (stating that it was usually small enter-

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.<sup>183</sup>

### 3. Third Stage of Privatization

The third stage of privatization began in 1996,<sup>184</sup> with the goal of selling approximately 200 to 250 large enterprises and 1000 strategic enterprises.<sup>185</sup> 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.<sup>186</sup> 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.<sup>187</sup>

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

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prises that were transferred to their employees and declaring that more than 4,800 enterprises were transferred).

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)*, Prilozhenie 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.<sup>191</sup> As many as forty of the large enterprises particularly attractive to investors were privatized through management contracts.<sup>192</sup> 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.<sup>193</sup> Legislation also permits cancellation of management contracts if management fails to meet performance expectations.<sup>194</sup> The Kazakhstani government terminated contracts with several managers complaining that they failed to make the necessary investments and improvements while managing the companies.<sup>195</sup>

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.<sup>196</sup> All

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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.<sup>197</sup> 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.<sup>198</sup> Auctions were conducted according to the English method of bidding—with price increases—and the Dutch method—with price reductions.<sup>199</sup> The price of the privatizing enterprise, however, could not be more than ten percent below a price determined by the government.<sup>200</sup>

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.<sup>201</sup> 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.<sup>202</sup> 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.<sup>203</sup> There has

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197. *See id.* art. 12.

198. *See* Regulation of the State Privatization Committee of the Republic of Kazakhstan on the Procedure for the Sale of State Shares at Auctions, Feb. 7, 1996 (visited Apr. 20, 1999) <<http://www.kazecon.kz/law/law-eng/amendm.htm>> (outlining the information required to be published in the announcement). Additionally, the announcement must be published in the press of the "oblast" where the joint-stock company is located and where the auction will be held. *See id.*

199. *See id.* arts. 1.1.7, 1.1.8, 2.2, 3.3 (defining and describing the English and Dutch auction processes).

200. *See id.* at amend. 1.

201. *See* Law on Privatization, *supra* note 129, art. 13.

202. *See* Nurdin Damitov, "Blue Chip" Program of the Republic of Kazakhstan (visited Apr. 20, 1999) <<http://www.kazecon.kz/English/bluechip.htm>>.

203. *See id.* (stating that agreements for the tender of Kazakhstan's first four

been criticism, however, that the government gives unfair advantages to these foreign investors.<sup>204</sup> 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.<sup>205</sup> 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.<sup>206</sup> Subsequent legislation authorized the President of the Republic of Kazakhstan to determine where the money would go.<sup>207</sup> 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.<sup>208</sup> 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.<sup>209</sup> The State also plans to foster

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"blue chip" companies were concluded by April 17, 1998).

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).

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.*

206. See Resolution on the General Directions of Privatization, *supra* note 121, para. 9.

207. See Law on Privatization, *supra* note 129, art. 23.

208. See Decree on Privatization, *supra* note 131, art. 20.

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.<sup>210</sup>

#### 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.<sup>211</sup> Generally, foreign direct investment plays "key roles in stimulating economies of developing states" and is seen as an "engine of growth."<sup>212</sup> 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.<sup>213</sup>

In Kazakhstan, the President has repeatedly emphasized that foreign investment and strong foreign relations are essential for the effective development of Kazakhstani natural resources.<sup>214</sup> 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.<sup>215</sup> 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.<sup>216</sup> As such, for-

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210. See *id.* sec. 5.

211. See Anderson, *supra* note 30, at 126.

212. Cheryl W. Gray & William W. Jarosz, *Law and Regulation of Foreign Direct Investment: The Experience from Central and Eastern Europe*, 33 COLUM. J. TRANSNAT'L L. 1, 3 (1995).

213. See *id.* at 10-14 (outlining different incentives for investors to invest abroad).

214. See State: Foreign Policy Pursued by Kazakhstan: Extract from President Nursultan Nazarbaev's Speech on Foreign Policy Issues, Feb. 15, 1995 (visited Apr. 20, 1999) <<http://www.president.kz/main/mainframe.asp?Eng=en>>.

215. See *id.*

216. See *Twin-track Approach in Kazakhstan*, *supra* note 156 (citing findings by

eign direct investment in Kazakhstan had already reached US\$1.2 billion by 1996.<sup>217</sup> 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.<sup>218</sup>

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.<sup>219</sup> 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.<sup>220</sup> 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.<sup>221</sup> Foreign participation in mass privatization of middle-size enterprises, however, was still lim-

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the accounting firm KPMG's Policy Economics Group).

217. See *Privatization in Kazakhstan*, *supra* note 181.

218. See NATIONAL STATISTICAL AGENCY OF THE REP. OF KAZAKHSTAN, STATISTICAL BULLETIN NO. 3, at 84 (1998).

219. See Law on Privatization, *supra* note 129, art. 8.

220. See "Ob uchastii inostrannykh investorov v processe privatizatsii gosudarstvennoi sobstvennosti v Respublike Kazakhstan", prilozhenie No7 k Postanovleniyu Kabineta Ministrov Respubliki Kazakhstan ot 20.07.93 goda 633 [On Participation of Foreign Investors in the Process of Privatization of State Property in the Republic of Kazakhstan, appendix to the Edict of Cabinet of Ministers of the Republic of Kazakhstan, July 20, 1993, No. 633], available in Kazakhstani Legislation database [hereinafter Foreign Investors in the Process of Privatization] (on file with *American University International Law Review*).

221. See Polozhenie o poriadke uchastiya inostrannykh investorov v processe privatizatsii ob'ektov gosudarstvennoi sobstvennosti v ramkakh maloi privatizatsii, postanovlenie Gosudarstvennogo Komiteta Respubliki Kazakhstan po Gosudarstvennomu Imuschestvu ot 24 yanvaria 1995 [On Participation of Foreign Investors in a Process of Small-scale Privatization in the Republic of Kazakhstan, approved by the Ordinance of the State Committee for State Property, Jan. 24, 1995], available in Kazakhstani legislation database (on file with *American University International Law Review*).

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.<sup>222</sup> 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.<sup>223</sup>

Kazakhstani legislation guarantees foreigners the freedom of entrepreneurial activities by prohibiting the illegal interference of entrepreneurial activity by State officials who have supervisory functions.<sup>224</sup> 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.<sup>225</sup>

The Law on State Support of Direct Investments in the Republic of Kazakhstan fostered a favorable climate for foreign direct investment.<sup>226</sup> 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.<sup>227</sup> 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.<sup>228</sup> The State guarantees the security of investment ac-

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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.

224. See Ukaz Prezidenta Respubliki Kazakhstan "O dopolnitel'nyh merah po realizacii gosudarstvennih garantii cvobodii predprinimatel'skoi deiatel'nosti" 14 iunia 1996 goda [Decree of the President of the Republic of Kazakhstan on Additional Measures for Implementation of the State Guarantees of the Freedom of Entrepreneurial Activities, June 14, 1996], available in Kazakhstani Legislation database (on file with *American University International Law Review*).

225. See *id.* sec. 1.

226. See Zakon "O gosudarstvennoi podderzke priamyh investicii v Respubliki Kazakhstan" ot 28 fevralia 1997 goda, [Law on State Support of Direct Investments in the Republic of Kazakhstan, Feb. 28, 1997], available in Kazakhstani Legislation database [hereinafter Law on State Support of Direct Investments] (on file with *American University International Law Review*).

227. See *id.* art. 5.

228. See *id.* art. 2.

tivities,<sup>229</sup> 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.<sup>230</sup> 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.<sup>231</sup> 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.<sup>232</sup>

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.<sup>233</sup> 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,<sup>234</sup> some foreign investors purchased large enterprises in Kazakhstan for a fraction of their real value.<sup>235</sup> Second, bribery of State

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229. *See id.* art. 4.

230. *See id.* art. 8.

231. *See id.* arts. 8-9.

232. *See* State Committee of the Republic of Kazakhstan on Investments, Resolution on the approval of The Regulations on the Procedure of Admittance of Applications from Investors for Obtaining Privileges and Preferences for the Investment Project Implementation and Application for Obtaining Privileges and Preferences for the Investment Project Implementation (visited Apr. 23, 1999) <<http://www.kazecon.kz/law/law-eng/3.html>> (listing the Kazakhstani government's preferential areas for foreign direct investment).

233. *See* Law on State Support of Direct Investments, *supra* note 226, art. 12.

234. *See id.* art. 10.

235. *See supra* notes 204-05 and accompanying text (detailing the purchase of a Kazakhstani business by foreign investors for a fraction of its worth).

officials is still a potential problem, although it may be better prevented with increased enforcement of the new Law on Fight with Corruption, enacted July 1998.

## 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 include small-scale, mass, and large-scale privatization, governed by the central State bodies with payment by cash or by investment coupons. 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 emphasized mass privatization of medium-size enterprises that were sold at auctions with payment by investment coupons. The government 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 participants 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 national economy. It was an engine of institutional, legislative, organizational, 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.<sup>236</sup> 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.<sup>237</sup> 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.<sup>238</sup>

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.<sup>239</sup> He pledged that Kazakhstani citizens would gather the fruits of the State reforms soon.<sup>240</sup>

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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).

239. See *Innaguratsionnaya Rech: Prezidenta Respubliki Kazakhstan* [The Speech of the President of the Republic of Kazakhstan in the Inauguration Ceremony], KAZAKHSTANSKAYA PRAVDA, Jan. 21, 1999, at 1.

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.