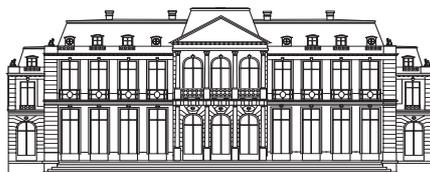


**Organisation for Economic Co-operation and Development**



**Organisation de Coopération et de Développement Économiques**

*in co-operation with*

**the United States Agency for International Development (USAID)**

*and*

**the World Bank**

**Conference on**

**“CORPORATE GOVERNANCE IN RUSSIA”**

***Mr V.Yu. Sinyugin***

*Director for corporate capital of RAO UES of Russia*

**“Case study: Corporate Governance Practices, RAO UES”**

*Moscow*

*31 May - 2 June 1999*

Conference on  
“Corporate Governance in Russia”

**Mr V. Sinyugin<sup>1</sup>**  
**Director for corporate capital of RAO UES of Russia**

1. Objectives of the speech:

- to examine the structure of joint-stock capital and the mechanisms of corporate management and control in RAO “EES Russia” (hereinafter referred to as the Company);
- to present the system of the Company’s relations with its shareholders;
- to make an analysis of the factors promoting and hampering relations with shareholders.

2. Let us begin with a historical reference. The Company has been founded by the RF State Property Committee (Goskomimuschestvo) in accordance with the RF Presidential Decree #923 of 15.08.92 “On Organization of Management of the RF Electric Power Complex in Conditions of Privatization.” The Company charter fund included control packages of stock of the regional electric power engineering enterprises, as well as property complexes (electric power transmission mainlines, substations, hydraulic electric power stations).

This paved the beginning of transformation of state enterprises of the Russian electric power engineering complex from a ministerial entity into a corporation.

At present, the Company is in fact a production and financial holding.

Let us introduce the following main notions:

The Company is RAO “EES Russia” as a legal person, including affiliates and representations;

The Holding is RAO “EES Russia,” as well as subsidiary and subordinate companies of the electric power complex.

3. Let us make a brief characteristic of the production potential of the Holding:

- the installed capacity is 155 million Kwt (78.7% of the total installed capacity in the country);
- the production of electric power is 73.4% of the national aggregate, thermal power – 89.7%;
- the length of system-forming electric power transmission lines is 41.700 thousand kilometers;
- the number of employed personnel is some 700 000 people.

At present, the Holding incorporates in its structure:

- packages of stock of 73 regional energy joint-stock companies (JSC’s);
- packages of stock of 32 electric station JSC’s;
- packages of stock of 59 joint-stock companies – scientific-research, exploration and design institutions;
- packages of stock of 30 joint-stock companies specializing in control and operational management, construction and servicing of the energy complex;
- about 50 packages of stock and shares in non-profile organizations.

Besides that, over 100 packages of stock of organizations of the power construction complex have been handed in the Company’s trusteeship.

4. The Company charter capital totals 21 558 451 684 rubles, which consists of 2 075 149 384 privileged shares and 41 041 753 984 regular shares with the nominal value of 0.5 rubles each.

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<sup>1</sup> The views expressed in this paper are those of the author and do not necessarily reflect those of the OECD

The following categories of owners can be outlined in the structure of the joint-stock capital on the state of 31.01.99:

- state entities – the Russian Federation – 52.5% of the charter capital;
- legal persons – nonresidents of the RF – 33.6%;
- legal persons – residents – 8.3%;
- natural persons – 5.6%.

On the whole, there are some 385 thousand persons among the Company shareholders, the overwhelming majority of which are Russian natural persons (over 350 thousand). More than 330 thousand persons hold packages from 1 to 10 000 shares, whereas about 110 persons hold packages of over 10 000 000 stocks (over 0.02% of the charter fund).

5. The system of corporate management and control consists of the following links:

- The general meeting of the Company shareholders.

The meeting participants are all owners of regular stocks, and in a number of cases – holders of privileged shares.

It is noteworthy that while over 50% of stocks are in property of the Russian Federation, 33% of the votes on these stocks on a shareholders' meeting (i.e. approximately 17% of the charter capital) are passed over to the RF member entities in proportion to the volumes of electric power consumption. Therefore, the holder of a control package of stock is actually absent from the shareholders' meeting, although, according to the shareholders' register, the Russian Federation is not recognized as such.

- The Company Board of Directors.

The Board of Directors, consisting of 15 members, is elected by cumulative vote of the shareholders' meeting. At present, seven members of the Board represent the RF and another two members represent the RF entities. Therefore, the majority of votes on the Board of Directors belong to representatives of state organizations.

An important feature of the managerial structure of the Board is the creation of a collegium of state representatives in the Company, consisting of eight representatives of the federal authorities. As a rule, the collegium holds its sessions simultaneously with sessions of the Board of Directors. The collegium decisions are mandatory during the vote of RF representatives on the Board of Directors. Thus, the collegium, being a superstructure over the Board of Directors, actually predetermines its decisions.

- The Company Executive Board.

The Executive Board is the Company's collegial executive body.

The Executive Board consists of 13 members appointed by the Board of Directors for a period of 5 years.

- Chairman of the Company Board.

The Chairman is the Company's singular executive body appointed by the Board of Directors also for a five-year period.

- The Company's Auditing Commission.

The Auditing Commission is a body of shareholders' control over the Company's financial and economic activity. The Company's Auditing Commission is elected by the shareholders' meeting in the amount of five persons for a period of three years.

6. Objectives of the Company management's work with shareholders:

- strengthening shareholders' and potential investors' trust in the Company, among other things, to prepare future attraction of capital on the securities market;
- creating conditions for raising the liquidity of the Company stock;
- preparation and coordination of justified and mutually acceptable decisions of the Company shareholders' meetings.

7. The main corporate events within the system of relations with shareholders in the Company are:

- election of the Board of Directors, appointment of the Chairman and members of the Executive Board;
- sessions of the Company managerial bodies (primarily the shareholders' meeting and the Board of Directors);

- approval of the Company's annual report, distribution of profit and loss, as well as payment of dividends to shareholders;
- amendment of the Charter and internal documents of the Company;
- disclosure of information to shareholders (compulsory and additional);
- inspection of the Company's activity on assignment of shareholders (by the Auditing Commission and the auditor of the Company).

8. Due to strategic importance of the Company, the RF normative acts have instituted a number of particularities with respect of it:

- the share of the state in the Company is to be not less than 50% in the course of three years as of the moment of founding (later, the Federal Law #74-FZ has raised this share to 51% without a fixed term);
- the share of nonresidents in the Company's charter capital is not to exceed 25%;
- representatives of the state on the Board of Directors and its general director (president) were appointed by the RF Government (in our opinion, this restriction has lost force after the adoption of the Federal Law "On Joint-Stock Companies");
- before the moment of the sale of over 50% of the Company stock by the state, the withdrawal of packages of stock from the Company charter capital shall be carried out on the basis of proposals of the Company upon decision of the RF Government.

9. The system of the Company's relations with shareholders includes:

A) Fulfillment of obligations before shareholders, fixed by the RF normative acts and the Company Charter, in particular:

- granting the right to participate in shareholders' meetings;
- presenting information compulsory for disclosure (including quarterly reports on securities and notifications about significant events and facts in the Company's activity);
- payment of dividends on privileged stock (in case of existence of profit);
- consideration of shareholders' appeals;

B) Additional actions with respect to shareholders:

- holding regular meetings of the Chairman of the Company Board with representatives of major shareholders for presenting intermediary results of the Company's activity and plans for the future;
- organization of operative conference-calls for the shareholders with participation of the Company's supreme management in connection with new events in the Company's activity;
- opening the Company's Internet site in Russian and English;
- holding special meetings in connection with preparation for the annual shareholders' meeting in large financial centers of the world (New York, London, etc.);
- presenting to shareholders a consolidated accounting balance sheet based on international financial accounting standards, prepared by PriceWaterHouseCoopers;
- setting up a department in the Company's executive staff, responsible for relations with shareholders (the Department of Joint-Stock Capital);
- organization of thematic meetings with members of the Board and heads of divisions of the executive apparatus on shareholders' request;
- forming a methodology of relations of shareholders and the leadership of affiliated and subordinate companies, resolution of conflicts and discriminating provisions of their statutory documents;
- interaction with associations of the securities market participants and investors (NAUFOR, PARTAD, OPIAK).

C) Perspective activities with respect to shareholders:

- forming a data base on interaction with the Company shareholders;
- elaboration and adoption of the Code of the Company's relations with shareholders;
- preparation and delivery of the regular information bulletin for the Company's shareholders;
- preliminary notification about the forthcoming significant events and facts in the Company's activity.

10. Factors promoting relations with shareholders:

- existence of RF legislation on compulsory disclosure of information, fixing the format and terms of disclosure;
- introduction of compulsory annual audits of public joint-stock companies;
- existence of the special federal Law "On Protection Investors' Rights and Legal Interests";
- creation of a single printed edition for disclosure of information on significant facts and events in the activity of open joint-stock companies ("Supplement to the Herald of the Federal Commission for the Securities Market);
- formation of a system of information disclosure on the basis of Internet resources, on the initiative of the federal Commission for the Securities Market.

11. Factors hampering relations with shareholders:

- adoption of RF normative acts infringing shareholders' rights.

The Federal Law "On Specifics of Disposal of the Stock of the Russian Joint-Stock Power and Electrification Company "Russian Single Energy System" and Shares of Other Joint-Stock Power Engineering Companies, Constituting State Property" of 07.05.98 has imposed restrictions on the ownership of more than 25% of RAO "EES Russia" stocks by nonresidents, whereas on the date of its adoption they held about 30% of the Company shares. At present, the above morn of the Law is not being observed, as there is no mechanism of its implementation, which was to be elaborated by the RF Government. To all appearances, a civilized mechanism of implementation of the Law can hardly be found in the near future.

The adoption of the aforementioned Federal Law has made an exceptionally negative impact on the rate of the Company's shares, as well as on the entire Russian stock market (see diagram).

Besides that, the RF State Duma is considering a draft Federal Law "On Approval of the List of Joint-Stock Companies Manufacturing Produce (Goods, Works, Services) of Strategic Importance for State Security and Specifics of Disposal of their Shares." This draft envisages the approval of a list of more than 1,000 joint-stock companies, and the introduction of a restrictive mechanism for nonresidents' participation in the management of the above joint-stock companies (a package of shares not exceeding 25% of the charter capital);

- collisions of the RF privatization and joint-stock legislation, including difficulties of applying the specifics of creation and legal status of joint-stock companies during the privatization of state and municipal enterprises (on the Company's example);
- lack of standard requirements during the preparation and publishing of the annual report of the joint-stock company;
- lack of effective mechanisms preventing the "washing away" of the shareholders' share, as the canceling of privileged right to the purchase of new emission stocks is carried out in accordance with the Federal Law "On Joint-Stock Companies" by a majority of votes;
- introduction of provisions in the joint-stock companies' statutory documents, discriminating the rights of minorities of shareholders (on the example of provisions of charters of affiliated companies, envisaging the need to acquire preliminary consent of the Board of Directors to the purchase of over 1% of voting shares);
- lack of operative methodic recommendations of the Federal Commission for the Securities Market concerning the practice of employment of the RF legislation on securities.

12. Additional problems in activity of joint-stock companies in the sphere of corporate policy:

- the problem of conflict of interests (on example of the main shareholder of the Company – the state, which is also one of the principal consumers of the Holding service and a regulator of the market of electric power engineering services);
- lack of explicit legislative mechanisms of distribution of profit and procedures of budgeting of joint-stock companies' activity;

Shareholders of the majority of Russian companies, gathered for their annual meeting, are compelled to accept the distribution of profits and losses proposed by the companies' management.

- lack of special procedures of holding corporate events for large joint-stock companies; The RF legislation does not describe explicitly enough the possibilities of notification of shareholders of meetings via mass media (in case of existence of a relevant provision in the charter).
- problem of unrealistic time frames of information disclosure (on example of the requirement to publish reports on significant facts in the activity of joint-stock companies within five days from emergence of such facts; the approval of quarterly reports on securities of large joint-stock companies by the Board of Directors within 30 days after the termination of the quarter is also problematic).

13. The prospects of the Company's relationships with shareholders are presently considered in the "Program of Development of the Stock Market of the Company and Affiliated Companies," being developed upon decision of the Board of Directors.

We would be grateful for proposals of all interested persons concerning the quest of new forms of relations with shareholders.

In conclusion, let me thank the organizers of the conference for the invitation and express the hope that this conference will become an important step towards understanding and improvement of the system of corporate policy in Russia.

## **SLIDES**

Relations with Shareholders as an element of Corporate Management

Department of joint-stock capital of RAO "EES Russia"  
V.Yu.Sinugin

### **Characteristics of the Company's Volume**

RAO "EES Russia" is a unique electric power engineering company

- Installed capacity – 155 million Kwt (78.68% of the national level)
- Percent of nationwide production is:
  - Electric power – 73.43%
  - Thermal power – 89.69%
- Number of employees – over 700 thousand people

Share in the total RF volume (%)

Production of thermal power

Production of electric power

Installed capacity

Share

### **Scope of Activity**

- The Company services RF territory occupying 17 074.4 thousand km<sup>2</sup>

- The incorporates in its structure some 200 joint-stock companies (JSC), including
  - 73 energy JSC's
  - 32 station JSC's
- Length of system-forming power transmission lines – 41.7 thousand km, including:
  - 330 Kwt – 7.09 thousand km
  - 400-500 Kwt – 30.48 thousand km
  - 750 Kwt and more – 3019 thousand km

### **Structure of Joint-Stock Capital**

- Charter capital – 21.6 billion rubles
- Regular shares
- Privileged shares
- Nominal 0.5 rubles
- In RTS and MMVB listing

State

Russian legal persons

Russian natural persons

Foreign shareholders (legal and natural persons)

### **System of Corporate Management**

Shareholders' meeting

Collegium of state representatives

Board of Directors

Company Executive Board

Chairman of the Board

### **Objectives of Management's Work and Main Corporate Events**

- Strengthening shareholders' and potential investors' trust
- Preparation and coordination of justified and mutually acceptable decisions by the shareholders' meeting
- Corporate events – within the system of relationships with shareholders
  - Election of the Board of Directors, appointment of Chairman and members of the Executive Board
  - Approval of the annual report, distribution of profit
  - Introduction of amendments into the Charter
  - Disclosure of information

Legislative Regulation

- Federal legislation
  - Federal Law 74-FZ
  - Federal Law “On Joint-Stock Companies”
  - Federal Law “On Protection of Investors’ Rights and Legal Interests”
- Particularities and contradictions in the legislation

### **Dynamics of the Price of RAO “EES Russia” Shares in 1998**

Dynamics of the price of RAO “EES Russia” shares (Russian trade system)

- Privileged shares
- Regular shares

\$ US

### **System of Relations with Shareholders**

- Fulfillment of obligations before shareholders, fixed by the RF normative acts and the Company Charter
  - Providing information compulsory for disclosure
  - Consideration of shareholders; appeals
- Additional actions with respect to shareholders
  - Holding regular meetings with the Company leadership
  - Forming a methodology of shareholders’ relations with the Company leadership
  - Interaction with associations of participants of the securities market and investors
- Perspective activities
  - Formation of a data base on interaction with shareholders
  - Elaboration and adoption of the Code of the Company relations with shareholders

Factors Promoting the Company’s Relations with Shareholders

- Existence of the RF legislation on compulsory disclosure of information
- Introduction of annual audits
- Special federal Law “On Protection of Investors’ Rights and Legal Interests”
- Formation of a system of information disclosure on initiative of the Federal Commission for Securities

### **Problems in Activity of Joint-Stock Companies**

Conflict of interests

- The state is the main shareholder, consumer of electric and thermal power, as well as the regulator of the market of electric power engineering services
- Lack of explicit legislative mechanisms of profit distribution and budgeting procedures
- Lack of special procedures of holding corporate events for major shareholders
- Problem of unrealistic time frames of information disclosure