

Client Alert on Azerbaijani Securities Regulations

July 28, 2015

Securities Markets Law

New categories of professional participants in securities markets

Professional participants in securities markets are defined to include investment companies, stock exchanges, clearing houses, investment fund depositaries and a central depository. They are to be created in the form of joint stock companies and will be subject to licensing.

An investment company is defined as a joint stock company having a license to engage in the activities of an investment company and the sole activity of which consists of rendering primary and auxiliary investment services. Investment companies will be issued a single license for a range of activities, including those of a broker, dealer and underwriter, subject to the limitations set forth in the terms of the license.

Certain licenses will be issued for an unlimited period of time

Unlike current requirements, according to which a license is issued for five years, the activities of stock exchanges, clearing houses and depositaries will be licensed for an indefinite period of time.

The review of an application for the issuance of the applicable license is conducted in two stages – initial and final. There will also be a special procedure for the licensing of branches of foreign investment companies in Azerbaijan. Only branches of foreign investment companies that have received the license in question may engage in the following services in the territory of Republic of Azerbaijan:

Primary investment services

- The acceptance and execution of clients' orders in relation to transactions with securities or derivative financial instruments
- The management of individual investment portfolios
- The provision of investment advice
- The placement and underwriting of securities (with and without an underwriting commitment)
- Transacting with securities and derivative financial instruments for their own account in the capacity of a member of a depository and stock exchange
- Margin trading

Auxiliary investment services

- The management of clients' securities accounts, including executing transactions related to encumbering securities and derivative financial instruments
- Lending funds or securities to investors for trading with securities and derivative financial instruments
- Conducting investment and financial analysis related to securities and derivative financial instruments
- Acting as a security trustee for secured bonds
- Foreign exchange activities in relation to conducting primary investment services

New minimum charter capital requirements will be promulgated by the regulator.

New qualification requirements for directors of professional participants in securities markets

In general, the laws of Azerbaijan do not require directors serving on the supervisory board or executive officers of professional participants in securities markets to possess any special qualification, nor does a prior criminal record normally disqualify a director or officer from such a position. That will change with the introduction of new qualification requirements for such directors of investment companies, stock exchanges, clearing houses and central depositories, including the introduction of educational requirements and requirements related to relevant professional experience.

New merger controls

Along with the general requirements contained in various other acts of legislation (e.g., antimonopoly consent), the prior written consent of the regulator must be obtained for the acquisition (whether directly indirectly) of a major shareholding in a professional participant in securities markets (i.e., 10 percent or more). Further, such consent would also be required each time a purchase will cause the purchaser's shareholding to equal or exceed the thresholds of 25 percent, 50 percent or 75 percent, subject to the condition that no person may own more than 50 percent of the charter capital of more than one investment company.

Creation of a Clearing House Compensation Fund

One of the mandatory options that clearing houses must select in order to reduce the risks related to the activity of clearing transactions executed in the after-hours trading system is the establishment of a clearing house compensation fund (other options include the insurance of assets, obtaining guarantees or security for assets, etc.).

The Clearing House Compensation Fund shall be financed from a range of sources, including membership dues paid by the members of the clearing fund and income from investing in funds. Such funds may then be used to settle the mutual obligations of the members of the clearing house vis-à-vis each other in relation to transactions concluded during after-hours trading, where a member is unable to settle.

Amendments to the Civil Code

A new concept of derivative financial instrument was introduced into the Civil Code, defined as a contract to buy, sell or swap underlying assets. Securities, foreign exchange, interest spots, profitability, derivative financial instruments, commodities, financial indices, credit risk, etc. may serve as underlying assets.

The proposed amendments provide for three types of derivative financial instruments – futures, options and swaps.

Futures are derivative financial instruments for the sale and purchase of a predetermined type and amount of an underlying asset at an agreed date and price. Options are derivative financial instruments that grant a unilateral right to its holders to buy, sell or swap an underlying asset. Finally, swaps are derivative financial instruments under which two parties exchange the same type of underlying asset.

Consequently, derivative financial instruments will not be considered to be securities and will avoid regulation under the existing securities regulations (advertising, registration, etc.). That said, please note that the regulator is charged with preparing special rules on the placement and circulation of derivative financial instruments in a standardized form over stock exchanges.

Finally, derivative financial instruments are expressly excluded from the Azerbaijani gaming laws.

Advertising Law

The new Advertising Law contains certain restrictions related to the advertisement of securities in Azerbaijan, an activity which is defined as information distributed using various means and methods in any form for the purpose of attracting the attention of the consumer to the subject-matter of the advertisement, creating and maintaining interest in and increasing awareness about the product and stimulating the sale thereof.

These restrictions include, along with a previously effective prohibition to advertise unregistered securities, restrictions related to advertisement of securities before a decision about the sale of such securities is adopted, as well as providing information that contradicts information contained in the prospectus.

Law stated as at 15 July 2015.

Your Key Contacts



James E. Hogan
Office Managing Partner,
Baku
D +994 12 4 90 75 65
james.hogan@dentons.com



Ulvia Zeynalova-Bockin
Partner, Baku
D +994 12 4 90 75 65
ulvia.zeynalova-bockin@dentons.com