RISKY BUSINESS

REPORT BY GLOBAL WITNESS | JULY 2010

KAZAKHSTAN, KAZAKHMYS PLC AND THE LONDON STOCK EXCHANGE

global witness

RECOMMENDATIONS

As part of its overhaul of UK financial regulation, the government should ensure that the listings regime for the London Stock Exchange and oversight of companies by the Financial Services Authority and its successors are significantly tightened.

FOR THE FINANCIAL SERVICES AUTHORITY

1. Any company wishing to list on the London Stock Exchange should disclose the ultimate beneficial owners of its shares for the five years prior to the time of its listing.

2. Senior managers or board members of such a company should disclose any relationships with government officials which could materially affect the company, explaining the nature of these relationships and their potential impact.

3. Any research carried out on companies by their sponsors before listing should be verified by a third party to check for errors or omissions.

4. Listed companies that operate in the oil, gas and mining sectors should be required to publicly disclose all the payments that they make to foreign governments, whether in cash or in kind, on a country-by-country basis.

5. The UK should discard the "comply or explain" model of corporate governance and instead should enforce compliance in listed companies.

6. The Financial Services Authority should launch a full investigation into the findings of this report, specifically the relationship between Kazakhmys plc's senior management and President Nazarbayev of Kazakhstan, in order to determine whether this could materially affect the company.

FOR KAZAKHMYS PLC

7. The company should make public disclosures which fully address all the matters raised in this report, including:

- the relationship between its senior management and President Nazarbayev,
- the issue of political donations to the ruling party of Kazakhstan,
- the sale of an aircraft to the presidential fleet of Kazakhstan,
- the reasons for the appointment of Bolat Nazarbayev to the board of Kazakhmys in August 2004,
- the reason why the company was sent President Nazarbayev's bill from the Lanesborough Hotel in 2006.

8. The company should increase to at least 50% plus one share the percentage of shares the company sells on the market, so that the majority of the company is outside of the control of its senior managers and the Kazakh government until the above matters are clarified by the company and the FSA. Alternatively, Vladimir Kim should step down as the executive chairman of Kazakhmys plc and a new wholly independent chairman should be appointed.

Front Cover: stock broker photograph REUTERS/Stringer Russia.
Coal miners in Kazakhstan REUTERS/Arko Datta.
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EXECUTIVE SUMMARY

RISKY BUSINESS

Reuters

THE FINANCIAL COLLAPSE HAS RAISED NEW QUESTIONS ABOUT CORPORATE RISK.

The near-collapse of the global financial system has brought home to investors the urgent need to understand the true picture of risks facing their investments. The crisis has prompted deep thinking about whether the current regulations for financial markets are rigorous enough to ensure that investors have the information that they need to assess risk, and to protect the public interest in securities markets being efficient, orderly and fair.

Few sectors of the economy are as risky as the oil and mining industries, which often make significant investments in natural resource-rich countries where the rule of law can be overridden by corrupt government officials. So investors in oil and mining have to be sure that they have all of the information they need in order to properly assess these risks. They also need to be sure that the regulatory regime and the regulators of securities markets are strong enough to address the risk that oil and mining companies may be subject to interference from corrupt foreign officials.

In recent years, mining companies from the former Soviet Union, a region both rich in natural resources and notorious for high

PRESIDENT NAZARBAYEV (LEFT) OPENS THE DAY'S TRADING AT THE LONDON STOCK EXCHANGE WHILE ON AN OFFICIAL VISIT TO THE UK IN 2006.

Scott Barbour/Getty Images

levels of corruption, have gained listings on the main market of the **London Stock Exchange**. The first of these companies was **Kazakhmys plc**, a copper mining company operating predominantly in the Central Asian nation of **Kazakhstan**.

Kazakhmys is a member of the prestigious **FTSE 100 share index**, meaning that institutional investors such as pension funds which hold the savings of ordinary citizens are exposed to its performance.

A company intending to list must issue a prospectus for potential investors. Listing regulations state that this prospectus must provide information that is "necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profits and losses and prospects of the issuer."[1] Since investors rely on the prospectus to assess the risks of investing in a company, it is crucial that the information in this document is as comprehensive and impartial as possible.

- Global Witness believes that Kazakhmys plc's listing prospectus may not have provided certain information that would have been necessary for an individual to make a fully informed decision about investing in the company. As this report will explain, Kazakhmys plc's listing prospectus omitted potentially key information about the biographies of its senior managers and its beneficial ownership. Global Witness has also discovered discrepancies in the reporting of its shareholding structure before the company's incorporation in the UK and subsequent listing (see p23).

- These gaps in the prospectus matter because, as this report will also show, the company faces allegations from numerous Kazakh sources, some of them former members of the country's ruling elite, that senior executives of the company (who are also its controlling shareholders) owe their positions to the country's autocratic head of state, President Nursultan Nazarbayev (see Chapters 4-8).

- These allegations cannot be proven beyond reasonable doubt but have been voiced by sources from various spheres of Kazakh life – politics, civil society and journalism. They need to be taken seriously because they raise legitimate concerns that President Nazarbayev may be able to unduly influence the decisions taken by the company, should he choose, in a way that may be detrimental to other shareholders. They also imply a risk that, should Nazarbayev ever be replaced by a political rival, the close association of Kazakhmys' senior executives with Nazarbayev himself could lead to punitive actions by a successor government that would damage the interests of the company and its shareholders. Global Witness has also found evidence which appears to show a closer relationship between the company and the government than has been disclosed (see Chapter 10).

The political risks of an investment in a Kazakh-based company should not be underestimated. Nazarbayev has been president for the last 20 years and was recently granted by his parliament the title of "the leader of the nation", which gives him immunity from prosecution[2] despite the fact that he was accused of receiving bribes in the 1990s from foreign oil companies.

This scandal, dubbed *Kazakhgate*, led to an ongoing trial in the United States of an American businessman who is alleged to have paid US$78 million in bribes to two top Kazakh officials.[3] As Global Witness detailed in its 2004 report, *Time for Transparency*, court filings indicate that one of these officials was President Nazarbayev himself.[4]

Little has changed in Kazakhstan since then to suggest that the risk of corruption has abated and the US State Department has continued to voice concerns over the dominance of Kazakhstan's ruling elite.[5] Indeed, Kazakhstan shows signs of being a 'kleptocracy' – a country run primarily in the interests of the ruling family and its associates. Members of Nazarbayev's family are reportedly worth billions of dollars[6] and hold senior positions in state businesses.[7] As recent events in neighbouring Kyrgyzstan show, kleptocracies can lead to instability, disorder and ethnic violence, as citizens remain poor while the elite get richer.

Against this background, it becomes all the more important to ascertain what due diligence was done on Kazakhmys plc by regulators before the decision was made to allow the company to list. The London Stock Exchange is regulated by the **Financial Services Authority (FSA).** However, when Global Witness turned to the FSA with a Freedom of Information request on this subject, the request was refused on the grounds that it was not in the public interest to reveal such information. But as this report will show, the public interest clearly requires greater transparency than the FSA has provided.

Global Witness also sent Kazakhmys plc a set of detailed questions about the allegations detailed in this report. The company declined to answer individual questions but said: "As you can appreciate, the process

Alastair Grant-Pool/Getty Images

NAZARBAYEV WITH THEN BRITISH PRIME MINISTER TONY BLAIR IN THE UK IN 2006.

undertaken to prepare the [company listing] prospectus and Kazakhmys for a listing on the main London market was a very rigorous and comprehensive one, involving a thorough due diligence exercise by two international investment banks and two major London law firms. These efforts combined to produce a prospectus which, as required by law, set out all of the information that investors needed to know in order to make a properly informed assessment of a potential investment in Kazakhmys”[8] (see Chapter 12). Global Witness also wrote to Kazakhmys plc's financial sponsor for its listing, JP Morgan Cazenove, but did not receive a reply.

So the main parties involved in the listing of Kazakhmys plc, including the company itself, appear to be saying, “We are not going to provide you with detailed answers, but you should trust us anyway.” The refusal to release any information by the FSA is troubling: not only is the general public not entitled to learn what was discovered, it cannot be told anything about the due diligence process either. In the wake of the global financial crisis, which revealed huge gaps between rhetoric and practice in the financial markets, these responses are simply not adequate.

The Kazakhmys case flags wider issues that need to be addressed by securities market regulators. Kazakhmys plc is the first company from the former Soviet Union to list on London's main market. The risk in such countries where the rule of law is weak is that companies will be subject to undue pressure from ruling elites seeking favours, payments or even influence over management, to the detriment of shareholders.

Investors need to be confident that they have full information about the political risks facing companies that operate in such countries. They need to be sure that a company is not being unduly influenced from behind the scenes, and that its financial relationships with governments are not contributing to corruption.

So the FSA needs to investigate the circumstances surrounding the listing of Kazakhmys plc to determine whether the disclosures provided to investors were adequate and whether the allegations detailed in this report have substance or not.

This report also highlights the need for wider reform of listing rules. In June 2010, the UK government announced that the FSA is to be scrapped from 2012 with regulation passing to the Bank of England and other bodies.[9]

The new regulatory regime must take the opportunity to improve both regulation and oversight to ensure, in the public interest, that investors such as pension-holders are not exposed to unknown or unquantified risk from companies from corrupt countries listing on the London Stock Exchange.

CHAPTER 1

FTSE 100 INDEX: A STANDARD OF EXCELLENCE?

The importance of the companies on the FTSE 100 should not be underestimated. Some tracker funds rely on the performance of this key index, as well as certain pension funds. This means that a great number of private investors in the United Kingdom, including ordinary citizens who are saving for their pensions and may know little about corporate investment, rely in part on the performance of Kazakhmys plc. Therefore it is in the public interest that the information available on this and other companies of the FTSE 100 is comprehensive, and includes detailed material about their assets and risks.

Reuters

CHIMNEYS OF COPPER SMELTERS IN BALHASH, KAZAKHSTAN, SITE OF KAZAKHMYS' OPERATIONS.

The regulation of the London Stock Exchange is undertaken by the Financial Services Authority (FSA). The FSA has a listing division – the UK Listings Authority (UKLA) – which is in charge of approving prospectuses and the admission of securities to the official list. For companies to achieve a listing, they must comply with this body's listing and prospectus rules.

When a company lists, the most vital document is the listing prospectus. According to the handbook of the FSA, the prospectus must provide information that is "necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profits and losses and prospects of the issuer."[10] The information in this document must therefore be as comprehensive and impartial as possible.

Global Witness believes that Kazakhmys plc's listing prospectus may not have provided certain information that would have been necessary for any individual trying to make an informed decision about an investment in the company. As this report will explain, Kazakhmys' listing prospectus appears to have failed to address several key issues relating to the company's

PRESIDENT NAZARBAYEV (RIGHT) WITH HIS BROTHER, BOLAT. WHAT EXPERIENCE DID BOLAT BRING TO THE KAZAKHMYS BOARD?

The Godfather-in-Law, p321

recent past, including its ownership and links to the Kazakh president.

The following information is missing from the listing prospectus:

- The fact that Vladimir Ni, chairman of Kazakhmys Corporation LLC (Kazakhmys plc's main operating subsidiary), worked for 28 years as a top government official in Kazakhstan both pre- and post-independence, including a 13-year stint working in the office of Nursultan Nazarbayev, who is the current Kazakh president.

- The fact that Kazakhmys plc chairman Vladimir Kim worked previously as an instructor in the Kazakh communist party and was from 2002 a member of the council of President Nazarbayev's political party.

- The appointment of President Nazarbayev's brother, Bolat, to the Kazakhmys board in 2004 before Kazakhmys listed in London.

- Kazakhmys plc chairman Vladimir Kim's admission in a Kazakh court in 2001 that he had been forced to pay bribes to the then Kazakh prime minister.

Global Witness believes that the following issues have not been explained in a satisfactory manner in the listing prospectus for investors to make an informed assessment of Kazakhmys plc's prospects.

- How Kazakhmys' top managers came to own virtually all of the company's shares before the initial public offering (IPO) on the London Stock Exchange.

- The beneficial ownership of Kazakhmys in the years leading up to the listing.

- The problem of corruption in Kazakhstan, the 'kleptocratic' nature of the regime – a country run primarily by and for the benefit of the ruling family and its close associates – and the risks that this poses to a company with its operations in Kazakhstan.

This last issue is of great concern because Global Witness has spoken to many sources who allege that a close relationship currently exists between Kazakhmys managers Vladimir Ni, Vladimir Kim and President Nazarbayev. They claim that as a result Kazakhmys plc is not an independently run company, but has the potential to be an instrument of an undemocratic leader in a country that is perceived by many observers to be corrupt.

This relationship would create a conflict of loyalty with the potential to affect the company in a way that may not be in the interests of the company's minority shareholders. The question is especially pertinent when considering the fact that Kazakhmys plc's chairman holds this position in an executive capacity and is also the company's largest shareholder, which in itself raises other issues about his independence (see Chapter 11). In such a situation, the protection of the rights of minority shareholders could be in jeopardy.

CHAPTER 2

KAZAKH BUSINESS COMES TO THE UNITED KINGDOM

Kazakhstan may be Central Asia's economic powerhouse but its human rights and civil liberties record is less than stellar.[11] Yet this did not prevent the Organization for Security and Co-operation in Europe (OSCE), an organisation that works on issues including human rights and press freedom, giving Kazakhstan its chairmanship in 2010 despite a lack of progress in these areas. This means that Kazakhstan, ranked 'not free' by the American NGO Freedom House,[12] and a country which has never had an election judged by the OSCE itself to have met democratic standards,[13] is currently the standard bearer of free elections.

The United Kingdom seems to be soft-pedalling the nature of Nazarbayev's regime, with muted criticism of such issues as human rights, democratisation and good governance. Kazakhstan's vast reserves of oil, gas and minerals, and the appearance of Kazakh companies on the London Stock Exchange, may be contributing to this lack of criticism.

October 2005 saw Kazakhmys plc, a Kazakh natural resources company (*mys* is Kazakh for copper), with the majority of its operations in Kazakhstan, become the first company from the former Soviet Union to be granted a listing on the main market of the London Stock Exchange,[14] raising over US$491 million in capital.[15]

At the time, Clara Furse, the Chief Executive of the London Stock Exchange, commented, "We are delighted that Kazakhmys has chosen London for its primary listing. The capital raised in this IPO demonstrates the strength of London's markets and investor confidence in its world-leading regulatory and corporate governance standards."[16]

Three months later Kazakhmys plc became a member of the prestigious FTSE 100 share index, among other mining companies such as Rio Tinto and BHP Billiton.

Kazakhmys plc seems to be an attractive investment: it operates 15 open pit and underground mines, making it the tenth largest producer of copper in the world,[17] with earnings in 2009 of US$1.63 billion.[18] The company's move from a "low-cost mining company based in Kazakhstan"[19] to a major FTSE 100 company happened at a relatively quick speed: it was reported that Kazakhmys chairman Vladimir Kim first announced the company's intention to list in late May 2004.[20]

An article from *The Times* reported that Kazakhmys' original auditor, KPMG, walked away from the firm, saying that it would take too long to do the due diligence in the proposed timeframe. Ernst & Young stepped in and employed a team of 156 people to go through the company's books, according to the same article.[21]

CHAPTER 3

KAZAKHMYS PLC & PRESIDENT NAZARBAYEV: AN UNDISCLOSED INFLUENCE?

Kazakhmys plc's listing on the London Stock Exchange and its accession to the FTSE 100 provoked much interest both in London and in Kazakhstan. However, not all commentators viewed this particular listing with enthusiasm. Speaking to *The Sunday Times* **in November 2005, one institutional investor said: "We are getting concerned about foreign companies coming here and getting into the FTSE 100 because of their size. They can raise cheap capital from tracker funds as well as the institutions and yet we don't really know much about them."[22]**

In Kazakhstan too, eyebrows were raised when Kazakhmys listed; in October 2005, a letter was written to the FSA by a group of Kazakh opposition politicians stating that they had only learnt that Kazakhmys plc's senior managers owned nearly all of the shares of the company – one of Kazakhstan's largest – from the listing prospectus and the British press.[23] For the general public of any country to learn the ownership of a major company in this way is an extraordinary state of affairs.

The fact that little seemed to be known about Kazakhmys plc and its Kazakh managers before it listed prompted Global Witness to look further into the matter. Global Witness has interviewed a dozen people familiar with the situation regarding business in Kazakhstan. These include three former members of the Kazakh government, Kazakh opposition politicians, journalists and members of Kazakh civil society. Some now live in exile, others are still resident in Kazakhstan. The sources are not drawn from the same 'group' (for example, the same opposition party) but from a diverse set of interested parties, some of whom profess a dislike for each other.

All of the sources who claim knowledge of Kazakhmys – nine in total – voiced the same opinion, that the company's major shareholders and key managers maintain a close relationship with the Kazakh president, Nursultan Nazarbayev, and that this relationship could allow Nazarbayev to influence the way the company is run if he so chooses. Some sources allege that Nazarbayev influences the company in actuality. The allegation is serious enough for further investigation, especially when there are precedents in Kazakhstan that indicate that the country's private business sector is heavily influenced by Nazarbayev and his family (see p15).

As of March 2010, three senior Kazakh managers of Kazakhmys owned 47.6% of the company, according to the 2009 Kazakhmys annual report. The Kazakh government owns

15%.[24] Therefore if these men do not act independently of President Nazarbayev as the Global Witness sources allege, then the company would be subject to the influence of someone who is not a shareholder. It would mean that other shareholders would be essentially powerless to prevent the Kazakh managers from making a decision that was against their interests, because these men, together with the government, own over 50% of Kazakhmys plc shares. It would also mean that the company's standing could be jeopardised if a political rival of Nazarbayev were to assume office, as this new president could potentially remove the current management, freeze the shares of the senior managers and take other actions that may undermine the company.

As one local analyst, Dosym Satpayev, head of the Risk Assessment Group in Kazakhstan's largest city Almaty, alleged to *The Times* in the year following Kazakhmys plc's listing: "Practically all big companies are controlled by the President's family. It's safe for foreign investors, but only as long as this particular elite stays in charge." It is not clear whether he had Kazakhmys plc in mind when he made these comments. Satpayev also noted that "transparency is not Kazakhstan's strong point".[25]

A link can be made from Kazakhstan's 'first family' to Kazakhmys. A press release from the company, dated 31 August 2004 (before Kazakhmys plc listed on the London Stock Exchange), indicate that a man by the name of "Nazarbayev Bolat Abishevich" had been appointed as a board member.[26] The fact that this man has the same patronymic (Abishevich) as President Nazarbayev himself indicates that the two men either have the same father or a father with the same first and last names.[27] Furthermore, a report in *The Times* newspaper from June 2006 – after Kazakhmys plc had listed on the London Stock Exchange – states, "Mr Novachuk [Kazakhmys' then-finance director and current CEO]… admits that the President's brother is on the board"

though he denied that the president's family controls the company.[28]

Global Witness could not find out much information about Bolat Nazarbayev and his background in business. An English-language media archive search on this man produces only a few results: in articles from the late Nineties, he is reported to be involved with companies called BN Consulting LLP[29] and BN Munai LLP.[30]

It is unclear whether Bolat Nazarbayev is still involved with Kazakhmys. Global Witness asked Kazakhmys plc to confirm whether Bolat Nazarbayev was appointed to the Kazakhmys board in 2004, and to ask whether he is still involved with Kazakhmys and whether he ever owned shares in the company. Kazakhmys declined to answer individual questions (see Chapter 12).

Global Witness believes that Kazakhmys appears to have failed to fully disclose the links between the company's management and President Nazarbayev, information that would be, in Global Witness' opinion, material to investors. The company's listing prospectus does not even mention those links between the company and the Kazakh president that are beyond reasonable doubt; for example, it makes no mention of the involvement of the president's brother in the company. The FSA should investigate to ascertain whether the company's disclosures in the listing prospectus were adequate in this regard.

CHAPTER 4

TESTIMONY FROM FORMER GOVERNMENT MINISTERS

In early 2010, Global Witness conducted an interview with Mukhtar Ablyazov, a Kazakh businessman, who from 1998-99 was the Kazakh Minister for Trade, Energy and Industry. He left government to co-found an opposition party in 2001, before being jailed in July 2002 on corruption charges he maintains were motivated by his involvement in the Kazakh political opposition.[31]

He was pardoned in May 2003,[32] and then relocated to Moscow before returning to Kazakhstan in 2005 to head BTA, the country's largest bank. In February 2009, the Kazakh state bought 75% of the bank's shares; Ablyazov was removed from the bank's management and accused of money-laundering and fraud.[33] The Kazakh government maintained that the share purchase was necessary to avoid a default,[34] while Ablyazov accused the government of "corporate raiding". Ablyazov then fled Kazakhstan, describing the charges against him as "baseless and politically motivated."[35]

FORMER MINISTER FOR TRADE, ENERGY & INDUSTRY, MUKHTAR ABLYAZOV.

Kplus TV

Ablyazov's position in the Kazakh government in 1998-99 meant he would have been in close contact with Nazarbayev regarding the running of Kazakh enterprises. According to Ablyazov, speaking to Global Witness:

When I was in charge of Kazakhstan's energy grid in 1997, I was very clearly told that I should be careful about shutting off energy for Kazakhmys, because it's Nazarbayev's. I was also told this about […] many other industries I knew were at that time controlled by Nazarbayev.

Concerning [Kazakhmys], Nazarbayev personally phoned me. There was a situation where Kazakhmys was not paying for the transfer of their energy, I limited their energy supply. And their bosses responsible for electricity told me in a very daring way, "Now you'll get a phone call and you'll turn it back on again". And I really did get a phone call from Nazarbayev, but I didn't switch it back on, and the person who spoke to me like that was eventually fired.

In 1997, the Kazakh government was still a 35% shareholder in Kazakhmys, though Ablyazov alleged later in the interview that President Nazarbayev still controls the company today: "At his command at any point [now] they could rewrite everything as he says."

Allegations similar to Ablyazov's are also made by Rakhat Aliyev, Nazarbayev's former son-in-law, who was forced to leave the country in 2007 after a very public and acrimonious split with the president. Aliyev is a controversial figure in Kazakhstan: his marriage to Nazarbayev's eldest daughter Dariga meant that for many years he was part of the ruling elite, reportedly controlling a variety of Kazakh business interests.[36] Following his exile to Austria, Kazakhstan asked the authorities there to extradite him on charges of extortion and kidnapping of officials from Nurbank, a Kazakh bank. Aliyev has maintained that the charges are politically motivated.[37]

Before falling from favour, Aliyev held high positions in Kazakh state structures: in 1996 he was head of the tax police,[38] in 2001 he became the deputy head of the National Security Committee,[39] in 2002 the Kazakh Ambassador to Austria[40] and, in 2005, First Deputy Foreign Minister.[41] Both his positions in government and his familial relationship to Nazarbayev would mean that he had unfettered access to the Kazakh president over many years.

In 2008, Rakhat Aliyev published a book, *The Godfather-in-Law*, which documents his time in Kazakhstan. Aliyev calls Kazakhmys "one of the flagships of the Godfather-in-law's [ie President Nazarbayev's] financial and industrial empire."[42] According to Aliyev, speaking to Global Witness in 2007, "not one penny can leave [the company] without Nazarbayev['s permission]."

At the beginning of the book, Aliyev states that in April 2006 he secretly recorded the last conversation he had with Nazarbayev before he left the country. In this conversation, he alleges that Nazarbayev said: "[Kazakhmys] is a company that works for me and does whatever I want." Later in the conversation, Aliyev alleges that Nazarbayev qualified this statement by saying, "Well, [Kazakhmys LLC Chairman] Vladimir Vassilyevich [Ni] – Kazakhmys – I don't have anything in particular to do with it, but I tell you they are prepared to do anything."[43]

Global Witness has written to Kazakhmys plc for their response to these allegations. The company replied (see Chapter 12) but chose not to respond to individual questions. One section of the letter stated: "as a listed company we are subject to the Listing, Disclosure and Transparency Rules of the FSA which require us, amongst other things, to make full and timely disclosures about the Company and its listed securities, including the interests of the directors and their connected persons in the Company's shares."[44]

Mikhail Evstafiev / Creative Commons

NAZARBAYEV'S FORMER SON-IN-LAW RAKHAT ALIYEV.

"Not one penny can leave [Kazakhmys] without Nazarbayev['s permission]."

(Rakhat Aliyev)

CHAPTER 5

VLADIMIR VASSILYEVICH NI: KAZAKHSTAN'S MOST POWERFUL PENSIONER?

Global Witness has spoken to nine sources who maintain that Kazakhmys plc's relationship with President Nazarbayev is manifested through Vladimir Vassilyevich Ni, a Kazakh businessman of Korean origin. The sources all allege that Vladimir Ni is currently a key unofficial figure in the presidential circle, while at the same time holding the positions of non-executive director of Kazakhmys plc and the chairman of the board of Kazakhmys Corporation LLC, the company's main operating subsidiary in Kazakhstan which runs the copper mines.

Vladimir Ni's biography from the listing prospectus is only three lines long: "Aged 72 [in 2005]. Mr Ni has been Vice-chairman of the Board of Directors of Kazakhmys Corporation since 1999. He is also a director of TOO HOZU Corporation. He graduated from the Kazakh Mining Metallurgical Institute. Mr Ni is a mining engineer by profession."[45] In 2006, the Kazakhmys Plc chairman Vladimir Kim described Ni as having had "a long and successful career in the domestic mining industry."[46]

Vladimir Ni did study as a mining engineer but he only spent four years working for a coal-mining company, according to a published biography.[47] The prospectus neglects to mention the 28-year period when Ni worked as an assistant in the top government offices in the country, including a 13-year period working in the office of Nursultan Nazarbayev.

According to the Kazakh version of *Who's Who*, Vladimir Ni was born in 1932 and after his position at the coal-mining company, he spent 11 years in the Kazakh GosPlan, the State Planning office, when Kazakhstan was part of the Soviet Union.[48] In 1970 he switched professions, working in the Directorate of Affairs (in Russian, *upravlenie delami*) in one of the most powerful offices in the country, that of the Kazakh Council of Ministers.[49]

In 1985, Ni became an assistant to Nursultan Nazarbayev, who had been appointed the previous year to the position of chairman of the Kazakh Council of Ministers. Following the collapse of the Soviet Union, Nazarbayev became the new republic's first president and Ni became Nazarbayev's deputy chief-of-staff. In September 1996, Ni became the chief-of-staff,[50] a powerful member of the presidential executive branch with unrivalled access to the head of state.

All of this information is absent from the Kazakhmys plc listing prospectus. Indeed, Global Witness could find no mention in

ImagineChina

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any subsequent statement by Kazakhmys that acknowledged Ni's former government positions.

Several sources have told Global Witness that Ni worked his way up to a position of great trust with Nursultan Nazarbayev as it was his job to organise Nazarbayev's day-to-day affairs, his meetings, trips and accommodation around the country.

Mukhtar Ablyazov's position in government in 1999 would have enabled him to see at first hand who President Nazarbayev's most trusted advisors were at that time. Speaking to Global Witness in early 2010, Ablyazov commented:

Mr Ni, as far as I knew in 1998-99, was Nazarbayev's closest friend. Many of his relatives, members of his clan, worked with Nazarbayev. But Ni was close to him personally. And whenever we met in a closed circle with the president, it was visible that Ni and Nazarbayev are in a very close personal relationship, because [Ni] allowed himself the kind of jokes about Nazarbayev that no one else would dare utter. Some of them could be considered insults. Nazarbayev reacted in a warm way, he smiled.

Ni left the position of Nazarbayev's chief-of-staff in August 1998 – officially ending a 13-year period of working directly with Nazarbayev – and joined Kazakhmys in June 1999.[51]

"It was visible that Ni and Nazarbayev are in a very close personal relationship, because [Ni] allowed himself the kind of jokes about Nazarbayev that no one else would dare utter. Some of them could be considered insults. Nazarbayev reacted in a warm way, he smiled. "

(MUKHTAR ABLYAZOV, FORMER KAZAKH MINISTER FOR TRADE, ENERGY AND INDUSTRY)

CHAPTER 6

IS NI AN UNOFFICIAL ADVISOR TO THE KAZAKH PRESIDENT?

The nine Global Witness sources who professed a knowledge of Kazakhmys alleged that Vladimir Ni's relationship with President Nazarbayev did not end in 1998, and that Ni continues to assist the president to this day in his business affairs and financial matters relating to his political party.

Out of the nine, three are former government ministers, one who is still operating in Kazakhstan. The fact that these individuals have occupied top positions in the Kazakh government means they would have been in a position to assess presidential advisors. In his book, Rakhat Aliyev alleges that Ni remains "unofficially one of the central shadow treasurers and advisors to Nazarbayev"[52] and elsewhere refers to him as "'keeper of the treasury' or the 'administrator of public accounts.'"[53] Mukhtar Ablyazov also asserts that Ni's close working relationship with the president continued even after Ni had left the presidential office: "Nothing changed [after Ni left the presidential office], they [Nazarbayev and Ni] became even closer friends. […] [Ni] remains the most powerful person. I don't think there is anybody equal to him – not the prime minister, not [Nazarbayev's son-in-law, Timur] Kulibayev."

At the very least, Ni should be considered an associate or colleague of President Nazarbayev due to his former employment in the presidential office. Given this information, it would be reasonable to consider the possibility that the company may suffer unduly if a rival of Nazarbayev were to assume office. This should be included in the section detailing the company's risk factors. Yet regarding this possible eventuality, the prospectus states only: "Should a new president be elected, the pro-business atmosphere in Kazakhstan could change."[54] Given all that is known about the kleptocratic aspects of the state in Kazakhstan, it could be argued that this risk factor has been understated, even if the allegations made by the various sources regarding Ni's current situation are disregarded.

Global Witness wrote to Kazakhmys plc to comment on the perception that Vladimir Ni and Nursultan Nazarbayev remain close associates, and asked why Ni's employment history was not included in the prospectus and why Kazakhmys seems never to have acknowledged Ni's former employer in any other public statement. We also wrote to Vladimir Ni himself at the company's London address. Kazakhmys plc replied but declined to answer individual queries. The letter stated: "We have always tried to maintain the highest standards of public reporting, beyond the requirements of our listing, because we believe that a commitment to transparent disclosure will benefit all of our shareholders and other stakeholders."[55]

DOING BUSINESS IN A KLEPTOCRACY

The listing in the United Kingdom of a company with its operations in Kazakhstan raises many issues. Kazakhstan is a country with a poor human rights record and is perceived to be highly corrupt. Kazakhstan's first appearance in Transparency International's Corruption Perceptions Index in 1999 saw the country ranked 84th out of 90 countries examined, with a score of 2.3 (10 being the highest score, representing a country perceived to have a low level of corruption).[56] Nine years later, Kazakhstan scored 2.2, ranking it 145th out of 180 countries.[57] The country is perceived to have improved a little in its 2009 ranking, scoring 2.7.[58]

In 2005, the year Kazakhmys plc listed in London, the World Bank gave Kazakhstan an 18.4 score out of 100 for control of corruption (meaning that Kazakhstan is perceived to be among the most corrupt twenty percent of countries in the world) and 25.7 for rule of law.[59] Both scores have worsened since then.

There is evidence to suggest that corrupt practices reach right to the presidential office. As Global Witness explained in its 2004 report *Time for Transparency*,[60] information regarding a scandal commonly referred to as *Kazakhgate* was revealed in a US Grand Jury indictment of James Giffen, an American businessman allegedly involved in setting up schemes to benefit President Nazarbayev.

The indictment alleges that in the 1990s Giffen helped two high-ranking individuals from the Kazakh government – dubbed KO-1 and KO-2 – to personally benefit from the country's state oil business. Cross-checking the US indictment with mutual legal aid requests and Swiss court documents relating to the matter reveals KO-1 to be the then-Kazakh Oil Minister Nurlan Balgimbayev and KO-2 to be President Nazarbayev himself.[61]

The indictment states that millions of dollars of the fees paid by US oil companies found their way into a Swiss bank account in the name of Orel Capital Ltd, a company beneficially owned by Nazarbayev and his heirs, according to Swiss court filings. Nazarbayev allegedly spent this money on, amongst other things, some US$45,000 of fees for an exclusive Swiss boarding school for his youngest daughter.[62] Balgimbayev allegedly bought with the money more than US$180,000 in jewellery and a stay at a Swiss spa. Giffen is alleged to have purchased an array of luxury items, including millions of dollars' worth of jewellery, fur coats, a speedboat and two American snowmobiles for the Nazarbayev family.[63] Giffen has denied the charges. It also came to light that in 1996 Nazarbayev had secretly held in his own name a billion dollar fund of government money. When this was revealed in April 2002, the then Kazakh prime minister commented: "The head of state was left with no other choice except to take all responsibility on himself."[64]

The power of the Nazarbayev family and its associates in Kazakhstan is absolute. Nazarbayev's relatives regularly feature in high-ranking positions in government and business. His son-in-law, Timur Kulibayev, has not only held many senior

JAMES GIFFEN (LEFT) WITH PRESIDENT NAZARBAYEV AND HIS WIFE.

positions in state-owned companies[65] but holds many business interests, including a majority shareholding with his wife of a Kazakh bank (Halyk Bank, which is also listed in London[66]) and much property, both in Kazakhstan and abroad. A recent story from *The Sunday Times* documented how in 2007 Kulibayev bought the former residence of Britain's Prince Andrew for £3 million more than the asking price, even though there were no other bidders.[67] At the time a spokesperson for Prince Andrew said that the sale was a straight commercial transaction, with no side deals or arrangements for the prince to benefit otherwise.[68] A journalist who visited the house in 2009 found it empty and in an advanced state of disrepair as it has not been lived in for many years.[69]

Nazarbayev's alleged involvement in *Kazakhgate* and the wealth and power of Kulibayev are just two examples which suggest that Kazakhstan is a 'kleptocracy', a country run by and for the benefit of the ruling family and its close associates. Such a system is maintained by the near-total control over most aspects of a country's society: its media, its judiciary, its political landscape and most importantly, its business. The US State Department has voiced concerns in its reports over the dominance of Kazakhstan's ruling elite.[70]

This poses a definite risk for companies with operations in Kazakhstan. However, Kazakhmys plc's listing prospectus does not address these issues regarding Kazakhstan (see Chapter 9).

CHAPTER 7

KAZAKHMYS PLC CHAIRMAN VLADIMIR KIM: FROM COMMUNIST PARTY OFFICIAL TO UK RICH LIST

The most important figure in any company is its chairman. At Kazakhmys plc, this position is held by Kazakh businessman Vladimir Sergeyevich Kim who, like Ni, is a Kazakh of Korean extraction. Kazakhmys plc's annual report from 2005 states, "the Board considers that Mr Kim's continued involvement in an executive capacity is vitally important to the Company at the present stage of its development."[71]

Vladimir Kim has profited greatly from his involvement in Kazakhmys. In 2010, *The Sunday Times* named Vladimir Kim the 14th richest person in the United Kingdom with assets worth £3.16 billion.[72] Compared to many others on this prestigious list, very little is known about the man and his reputation in the business world. The important question is: how did Vladimir Kim become such a wealthy and important figure in Kazakh (and subsequently British) business and why is his involvement so important for the company's success?

His biography in the Kazakh version of *Who's Who* gives no background in copper mining and little experience in business before his position at Kazakhmys. It states that he graduated in 1982 from the Institute of Architecture and Construction in Almaty, (then called Alma-Ata, Kazakhstan's largest city), and has a Ph.D. in technical science. From 1982, he worked for six years as a stone-mason, a supervisor and then the chief engineer in a state construction company in Almaty. This was his last position in the construction business. In 1987, he became an instructor in a regional committee of the Communist Party. The following year he became the deputy chairman of the regional executive committee of the Party, a relatively lofty position.[73] Nursultan Nazarbayev became the first secretary of the Kazakh Communist Party in June 1989.[74]

From 1989-92, Kim served as the deputy chairman and then as the acting chairman of the Cultural, Social and Scientific Development Fund of Kazakhstan. This fund seems to have functioned as a 'training ground' for many figures in Kazakhstan who would later go on to hold important positions in the government and/or state enterprises, including the Kazakh president's son-in-law Timur Kulibayev,[75] Esetzhan Kosubayev[76] (who would later become a presidential spokesperson[77] and the Kazakh Minister of Culture[78]) and Zeinulla Kakimzhanov[79] (who would later become a presidential assistant and the Kazakh Minister of Finance[80]).

Kim's biography in the Kazakh *Who's Who* states that in November 2002 he became a

KAZAKHMYS PLC CHAIRMAN VLADIMIR KIM (TOP LEFT, TOP RIGHT) AT A PRESS-CONFERENCE WITH VLADIMIR NI (BOTTOM LEFT, BOTTOM RIGHT)

Channel 31, Kazakhstan

member of the political council of the Otan Party,[81] President Nazarbayev's political party. This organisation is in many ways a successor to the Kazakh Communist Party because it features many of the same personnel, albeit based now on national rather than communist ideology. The party was then reorganised into the all-powerful Nur Otan party of today, which currently holds every single seat in the Kazakh parliament. It is unclear whether Kim still holds this or a different position in the new party.

Kim's position in the council of the Otan Party suggests that he has close ties to the Kazakh ruling elite, yet investors would not find information on this or his *apparatchik* past in the listing prospectus. Here his biography reads: "Mr Kim joined the Group in 1995, when he was appointed Managing Director and CEO of JSC Zhezkazgantsvetmet. He was elected chairman of the Board of Directors in December 2000. Mr Kim graduated from the Alma-Ata Architectural Institute in 1982 and holds both a Ph.D. and an MBA."[82]

Kim first moved into the business world in 1992, becoming the chairman of a joint venture called Samsung-Kazakhstan. As stated in the Kazakhmys listing prospectus, he then became in 1995 the CEO of Zhezkazgantsvetmet (a company based in the small Kazakh mining town of Zhezkazgan), which would later become part of the Kazakhmys Corporation.[83]

When Kim made the switch to the business world many of Kazakhstan's state-run enterprises were in a sorry condition – badly run, with weak infrastructure and massive debts: Kazakhstan desperately needed money. Consequently the government announced a wide-ranging privatisation program that year in the hope of attracting foreign investment and stimulating growth. The privatisation of large industrial assets, such as those that were later to become Kazakhmys, was the last of three phases in the privatisation plan and took over five years to fully complete.[84]

Many of these companies had large debts and lacked the managerial expertise needed to become profitable. The Kazakh government therefore agreed to hand over the management of its shares for a yearly fee; the government would still be responsible for some of the company debt, but would benefit from the expertise and capital of the foreign investor. This is what happened to Kazakhmys which in 1996 brought in the South Korean firm Samsung as its foreign partner and struck a management contract whereby Vladimir Kim became a manager in a trust arrangement of the 35% of Kazakhmys' shares owned by the government.[85]

Mukhtar Ablyazov and other sources have alleged to Global Witness that the move to bring both Kim and Samsung in was arranged by Vladimir Ni when the latter was still working in the presidential office. Ni's Korean roots would seem to make the appointment of Kim (who himself is of Korean ancestry) and the Korean company Samsung a logical step.

The original privatisation of Kazakhmys has been questioned by a group of Kazakh opposition politicians who, citing "many irregularities", wrote to the FSA at the time Kazakhmys plc listed with their concerns. Kazakhmys' listing prospectus addresses this issue by stating, "The [Kazakhmys] Group does not consider the allegations made by this group in relation to the Group's assets to have any substance."[86] We wrote to Kazakhmys' listing sponsor, JP Morgan Cazenove, to ask what due diligence it undertook to independently ascertain whether the privatisation was completed in accordance with Kazakh and international law. The company did not reply.

COPPER CARGO IN ZHEZKAZGAN, KAZAKHSTAN.

Photo by Almaz Tleuliev / Creative Commons

CHAPTER 8

VLADIMIR KIM: JUST A "FRONTMAN"?

Given the highly centralised control of the Kazakh economy and the importance of Kazakhmys to it, it seems unlikely that Kim would have been given a position of responsibility managing the 35% of Kazakhmys owned by the state if he had not been a well-trusted member of the Kazakh establishment.

Three sources have alleged to Global Witness that his position as Kazakhmys plc chairman is primarily due to his loyalty to the current ruling regime and not his business acumen. According to the Kazakh *Who's Who*, Kim seems not have had any experience in copper mining before joining Zhezkazgantsvetmet in 1995.

According to Ablyazov, speaking to Global Witness in 2010:

I knew [Vladimir] Kim since the start of the 1990s. He is an ex-Komsomol functionary [the young people's wing of the Soviet Communist Party]. He has gone through this Soviet Komsomol school of life. Also a very flexible person. And so he was appointed the nominal owner of Kazakhmys […] Nazarbayev [assigned him] on Ni's recommendation, because Nazarbayev never knew him personally, only through Ni. In the early 1990s, nobody heard about Kim the businessman. He appeared at the company in Zhezkazgan suddenly. Then Ni represented him to Nazarbayev and they decided he should be the nominal owner.

This allegation is also made by Rakhat Aliyev, who alleges in his book that Kim is "only a frontman … Vladimir Kim did not earn or build anything himself."[87]

Another source that spoke to Global Witness about the relationship between Ni and Kim is Kazakh politician Yerzhan Dosmukhamedov (known as Eric Dos in the West), who in 1994 was the chief-of-staff to the then Kazakh vice-president Erik Asanbayev.[88] Dos now heads an opposition party in exile. In an emailed comment made to Global Witness in 2007, Dos commented, "[Ni] is the one who picked Mr Kim – Kazakhmys President – to be a puppet CEO of the Kazakhmys."

In further emailed comments from early 2010, Dos told Global Witness that he remembered that in January 1994 he was at Frankfurt airport with Kim and Ni to catch a flight back to Kazakhstan. According to Dos, Kim was carrying Ni's bags, such was Ni's status. Then unaware of who Kim was, Dos recalls that he asked Ni's wife, in Ni's presence, whether Kim was their son. She replied: "One may say so." Neither Ni nor Kim rejected this comment at the time, according to Dos.

Two other sources – a Kazakh investigative journalist and an opposition politician still active in Kazakhstan – have told Global Witness that they consider Vladimir Kim to be merely the figurehead of the company with no real power. Global Witness wrote to Vladimir Kim regarding these matters. Kazakhmys plc replied on his behalf, but did not answer our individual queries on Kim and other issues.

Vladimir Kim earned £1.81 million at Kazakhmys plc in 2009 through his salary, benefits and annual bonus.[89] Vladimir Ni, as a non-executive director of Kazakhmys plc and the chairman of Kazakhmys Corporation LLC, earned £415,000.[90]

However, in 2006, he was the beneficiary of a massive windfall from Vladimir Kim who granted Ni some of his shares, totalling 2.5% of Kazakhmys plc. These shares were valued at around £135 million, making it "possibly the biggest ever loyalty payment to a single manager", according to an article in *The Mining Journal*.[91]

This gift was, according to an announcement made by Kazakhmys plc, a reward for Ni's "longstanding business relationship with Mr Kim."[92] Vladimir Ni joined Kazakhmys in 1999. Before this Ni worked in the presidential office. Therefore, one would assume that the two men's business relationship had existed at this point for seven years, though it is unclear whether the two men were in business together before Ni joined Kazakhmys.

"[Kazakhmys plc chairman Vladimir Kim is] a very flexible person. And so he was appointed the nominal owner of Kazakhmys […] [The then presidential assistant, Vladimir] Ni represented him to Nazarbayev and they decided he should be the nominal owner. "

(MUKHTAR ABLYAZOV, FORMER MINISTER FOR TRADE, ENERGY AND INDUSTRY)

According to the Kazakh *Who's Who*, Ni was not involved in any business before Kazakhmys, apart from his position at HOZU[93] (a company that manages formerly state-owned property). If this gift is based on just a seven year relationship then this would appear to be extremely generous.

KAZAKHMYS SHARES MOVE FAST – BUT WHO OWNS THEM?

Several sources assert the influence of President Nazarbayev over the company is such that the company's senior managers who are also sizable shareholders (Kim, Ni and current CEO Oleg Novachuk) would be unable to make major decisions without his permission. In this regard, it is worth examining how the company's current shareholders came to own these shares.

The Kazakhmys listing prospectus states that the Kazakh government sold its 100% stake in Kazakhmys between 1992 and 2002 in a number of stages, via a series of privatisation auctions and tenders. By the time the company listed in 2005, virtually 100% of the company was owned by its senior managers. It is difficult to trace who owned the company at various stages in between because the available information in the listing prospectus and elsewhere is incomplete. It is therefore hard to understand how the senior managers came to own practically the entire company.

Kazakhmys plc's listing prospectus states that "between 1992 and 1995, 20% of [Kazakhmys'] share capital

KAZAKHMYS DOMINATES THE KAZAKH TOWNS IN WHICH IT OPERATES.

Almaz Tleuliev / Creative Commons

was transferred to employees and pensioners of Kazakhmys and to other investors." By the time of the listing, only 1.2% of the company was not controlled by senior managers.[94] This would suggest that the majority of Kazakhmys employees and pensioners sold their shares at some point before the company's IPO in London or had their shares diluted by subsequent share issues. Various articles in the Kazakh media quote employees who allege that they were "deceived" out of their shares through a variety of methods, including the claim that shareholders had not been properly informed about new share issues, even though these would water down their existing shareholdings in Kazakhmys.[95]

In November 2001, 10.35% of Kazakhmys belonging to the Kazakh government was sold at an auction and the government's final shares (totalling 24.65% of Kazakhmys) were sold by auction in December 2002.[96] However, the listing prospectus gives no information regarding the winners of these auctions.

According to a media report, a Kazakh company called Future Capital LLP bought the 10.35% stake in the 2001 auction for US$63.15 million.[97] Global Witness could find no information regarding this company's ownership. A Kazakhmys annual report from 2002 states that Kazakhmys guaranteed loans to Future Capital LLP to buy its shares on two occasions in 2001 and 2002.[98] The second time it did this, in December 2002, Kazakhmys agreed to guarantee further loans to Future Capital to buy the government's remaining shares even though Future Capital had already defaulted on the earlier loan[99] – a rather strange decision for any company to make. Future Capital LLP's involvement with Kazakhmys is not mentioned in the listing prospectus.

The winner of the auction of the government's final 24.65% stake in Kazakhmys in December 2002 is also unknown. According to a media article published in early 2003, a 20% stake was sold at the auction in a single lot for US$184 million.[100] The news report made it sound like an eventful auction: "It was completely unexpected that a minute before the closing of the auction, the price went up again and again and a new auction opened. What happened today exceeded all expectations, including those of the country's finance ministry," said Andrei Tsalyuk, head of information and analysis at the Kazakhstan Stock Exchange.

Yet the buyers were not named at the time; a top official at the property committee said that this information was "confidential".[101] It appears that the purchaser of the 20% share was never revealed. Kazakhmys declined to answer individual questions when Global Witness asked in 2009 for more information regarding this share purchase.

One further example of Kazakh market "confidentiality" occurred about a week before Kim announced in late May 2004 at a Moscow conference that Kazakhmys intended to list in London.[102] On 20 May 2004, 11.5% of Kazakhmys shares were sold for US$172.6 million, according to a Central Asian press report.[103] "This was an absolute record for share volume on the secondary market in a single day," said Andrei Tsalyuk, the analyst at the Kazakhstan Stock Exchange. However, Tsalyuk was unable to name the buyers or the sellers, though he surmised that it seemed evident that a change in Kazakhmys' shareholders had taken place.[104]

This implied that investors in this company in the Kazakh stock market at the time had no idea as to the identity of any new shareholders after official auctions. The company's subsequent delisting from the Kazakhstan Stock Exchange later in 2004 meant that no annual report revealed this information. Potential investors are therefore kept in the dark about former shareholders and their involvement with the company.

In a written response to questions from Global Witness, Samsung stated that it purchased 24% of Kazakhmys in three stages from 1996-98, and then a further 17.22% in November 2000 for US$110 million from a company called Neal Holding N.V.[105] Global Witness has been unable to discover who was the beneficial owner of Neal Holding N.V., which appears to be registered in the Netherlands. Samsung sold some of its shares in Kazakhmys in 2001.[105]

The table below is from the Kazakhmys listing prospectus and shows the main shareholders in Kazakhmys from 2002/03 (prior to Kazakhmys' incorporation) and 2004 /05:

However, this table does not correlate with other information from Kazakhmys' own corporate documents. A Kazakhmys financial report for 2002 says that on 1 January 2003 Samsung Corporation held 25.33% of shares with Samsung Hong Kong holding 17.22% – a total of 42.55%[106] – this is inconsistent with the chart from the listing prospectus (see below) which says that on 31 December 2002 Samsung Corporation held 60.8% of shares.[107]

Name	Percentage equity interest at 31 Dec			At 31 May
	2002	2003	2004	2005
Samsung Corporation	60.8	28.8	–	–
Perry Partners S.A.*	–	–	38.0	37.7
Cuprum Holding B.V. (Netherlands)*	–	25.7	34.0	33.7
Harper Finance Limited*	13.6	19.2	25.5	25.1
Rego International (Nevis Island)	6.9	4.9	–	–
Kinton Trade Limited*	–	–	2.1	2.3
Dillon Enterprises	1.6	5.1	–	–
Companies registered in Kazakhstan	4.6	12.3	–	–
Other minority shareholders	12.5	4.0	0.4	1.2

* Companies controlled wholly or partially by Kazakhmys senior managers according to the Kazakhmys plc listing prospectus.

THE COMPLEX HISTORY OF KAZAKHMYS SHARES. SOURCE: KAZAKHMYS PLC LISTING PROSPECTUS.

A COPPER SMELTER IN RUSSIA

Sergey Maximishin/Panos Pictures

And in a written response to Global Witness, Samsung stated that it owned much less of Kazakhmys at this time – 27.55%.[108] In other words, there are three varying accounts of the shareholder structure of Kazakhmys at the end of 2002, which raises questions about the reliability of the due diligence that was performed for the IPO.

Furthermore, information in the prospectus about Kazakhmys' beneficial owners in the years leading up to the IPO is not comprehensive. The chart gives the names of two companies, Rego International (registered in Nevis) and Dillon Enterprises (registered in the British Virgin Islands), which owned shares in Kazakhmys (totalling 10% of the company at the end of 2003).[109] But it does not name the individuals who controlled them. Giving the names of these offshore entities without their owners is essentially useless when trying to examine who owned the company. Our questions regarding the beneficial ownership of all the above-mentioned entities were not answered by Kazakhmys plc.

The listing prospectus provides information regarding shareholders in Kazakhmys from 31 December 2002, approximately three years before the company listed.[110] Kazakhmys plc is not under any obligation to provide financial information outside of a three year time frame; recommendations from the independent Committee of European Securities Regulators, a body that gives proposals to the European Commission and EU member states on regulatory practices, state that an issuer should give financial information regarding at least the last three years.[111] However, due to the issues we raise in this report Global Witness feels there is a case for the ownership structure of Kazakhmys to be clarified at all points throughout its history.

CHAPTER 9

VLADIMIR KIM TESTIFIES IN A KAZAKH COURT THAT HE WAS FORCED TO GIVE BRIBES

As highlighted above, Kazakhstan is perceived to be a highly corrupt country; in addition to the *Kazakhgate* scandal, in recent years several high profile bribery cases in Kazakhstan have hit the headlines.[112] Yet Kazakhmys plc's listing prospectus does not name bribery and the corruption of public officials as a risk factor, which in Global Witness' opinion is a fact that investors need to know to make an informed decision regarding an investment in a Kazakh-based company. The words 'corruption' and 'bribery' are not even mentioned in the entire prospectus. This is even more surprising given the fact that in 2001 Kazakhmys plc chairman Vladimir Kim testified in a Kazakh court that he had given bribes to the government official who was on trial at the time.

Kim had been called as a witness at the trial of former Kazakh Prime Minister Akezhan Kazhegeldin who was accused of several crimes, including abuse of power and tax evasion.[113] Kazhegeldin was being tried in absentia, having fled the country some years before, maintaining that the trial was politically motivated[114] as he had fallen out with Nazarbayev and announced his intention to run for the Kazakh presidency against Nazarbayev in the 1999 election.[115]

The weekly news bulletin of the Embassy of Kazakhstan in the United Kingdom – compiled, it says, from its own sources and various agencies – gave an extensive report of the trial and Kim's testimony. The report says that Kim was forced to spend more than US$400,000 on expensive gifts to Kazhegeldin: "Kim characterized the demands as 'pure extortion', but said Kazakhmys felt compelled to try to satisfy the premier as the company was "experiencing some very difficult times."[116]

Other media reports from the time of the trial state that Kim had needed to take out several loans from Samsung, which was then a major shareholder in Kazakhmys, to cover the bribes and that he had, at the time of the trial, still not repaid the loans fully. According to the reports, Kim added that no-one except him knew that he had taken the loans from Samsung as under the company's unwritten laws employees of his rank could borrow any amount of money under the obligation to return it unconditionally.[117] In response from questions from Global Witness, Samsung replied that the company never had such an "unwritten policy" in its history and that the company had never provided a loan to Vladimir Kim.[118]

At the time, Kazhegeldin stated that the charges against him were politically motivated. We wrote to Kim to ask him for his comment. Kazakhmys plc replied on his behalf but declined to answer individual questions. The situation is troubling; not only has the matter yet to be clarified, it was also not dealt with in the Kazakhmys listing prospectus, despite the seriousness of the admission from Kim, the fact that Kazhegeldin denied the charges and that the trial was widely reported at the time in Kazakhstan.

Around the time Kazakhmys listed, the FSA and UK Listings Authority were informed about Kim and his testimony at this trial in a letter from a Kazakh opposition group. The group did not receive a reply, according to one of the group's associates.[119]

"Directors are required to demonstrate unquestioned honesty and integrity, a willingness to question, challenge and critique, and a desire to understand and commit to the highest standards of governance. Each Director must ensure that no decision or action is taken that places his interests in front of the interests of the business."

(KAZAKHMYS PLC ANNUAL REPORT 2009)[120]

THE REALITIES OF KAZAKHSTAN ARE A WORLD AWAY FROM THE GLOSS OF THE LONDON STOCK EXCHANGE.

Chris Stowers/Panos Pictures

CHAPTER 10

THE AUDIOFILES, AN AIRCRAFT AND A HOTEL BILL

Michael Davis, Creative Commons

THE INTERIOR OF A VIP AIRBUS 319.

In November 2007, Vladimir Ni was caught up in a controversy concerning allegations that he was still aiding the president in, amongst other matters, the purchase of a presidential plane. These and other allegations stem from a series of audiofiles that were posted on the internet, which would, if genuine, indicate a much closer relationship between Ni, Kim and Nazarbayev than has been disclosed and indicate that Ni's role in particular in Nazarbayev's affairs is very significant.

The audiofiles themselves purport to be tapped phone conversations from late 2007 in Russian between government officials and Kazakh businessmen. The files have not been verified as genuine; a top sound expert told Global Witness that the files were highly compressed and that the original recordings would be needed in order to conclusively determine whether the files are genuine.[121]

However, the allegations that stem from the files are serious enough to warrant an independent investigation to take place outside of Kazakhstan and be executed by people with no vested interest. Global Witness calls on the people responsible for recording the audiofiles to submit the original recordings to an independent expert to be verified.

In *The Godfather-in-Law*, Rakhat Aliyev reproduces transcripts of the conversations and alleges that three of the voices on the audiofiles are those of Vladimir Ni, Vladimir Kim and President Nazarbayev.[122] Kazakh sources have expressed a view to Global Witness that one of the voices on the audiofiles sounds similar to that of President Nazarbayev.

In one audiofile, a man speaks to an individual he calls 'Volodya', diminutive of the name Vladimir. They discuss the capacity of an aircraft, before the first man passes the phone to a third individual, referred to as "Nursultan Abishevich".[123] The following transcript has been translated by Global Witness from the file posted on the internet. The transcripts in Aliyev's book allege that the man who starts the conversation (voice 1) is Vladimir Ni, that the man referred to as 'Volodya' is Vladimir Kim (voice 2), and the man who then joins the conversation is President Nazarbayev (voice 3).[124]

Voice 1: Volodya, you remember we discussed the new plane, the 330.
Voice 2: Yes?
Voice 1: I don't understand why I wrote 100 people?
Voice 2: No, it's 35 plus 12, this makes 35 plus 12.
[…]
Voice 1: I'll hand the receiver to Nursultan Abishevich now.
Voice 2: Ok.
Voice 3: Hello.
Voice 2: Hello, Nursultan Abishevich.
Voice 3: Good afternoon, Vladimir Sergeyevich. How are you?
Voice 2: I would like to congratulate you! I heard you speaking yesterday! Well, of course, we will do as you say.
Voice 3: Everything will be ok.
Voice 2: Thank you, thank you, Nursultan Abishevich! Vladimir Vassilyevich has told you about this plane. Please forgive us, we need to do something.
[…]
Nursultan Abishevich, I beg your pardon. You are the owner of the plane; it is here already. But someone has to decide how to arrange it on the inside.
[…]
And, which is most important, Nursultan Abishevich, we have so many planes – can't we afford a plane for the Boss? Frankly, I have been tackling this plane for two years. I am sorry.
Voice 3: It's too big, you see.
Voice 2: Nursultan Abishevich, you are yourself bigger than the plane!
Voice 3: Understood.
Voice 2: That's why, you see, please excuse me. … This one has already been purchased for you. So, if you say we have to take it apart… But it has been purchased already.
[…]
Nursultan Abishevich, may I ask you a question? Do you like the plane?
Voice 3: Of course I do, but it's mighty big.
Voice 2: Nursultan Abishevich, let the next Kazakh presidents fly smaller planes. We have one president, let him fly a bigger plane. This will be a plane like Putin's, he ordered it already. But you will be the first to have it! You know, your Airbus, the one you have now, an identical one has arrived for Putin. Don't you know? Has he told you?
Voice 3: Which one?
Voice 2: A small Airbus. He has received one like that.
Voice 3: Like mine?
Voice 2: Yes, it has arrived a year later. Of course, we follow everything.
[…]
320 will come in a year. You will be able to fly it in February-March next year. It will have no match. There are three of them in the world. You will drop all these Boeings, you will fly to Saudi Arabia for example and they will say to you, "Oh! What a plane of yours! We would all like to have such planes." We have bought over everybody's head. I swear! You won't believe.
Voice 3: Good. Ok. The state can do this. Bye now.
Voice 2: Thank you, thank you!

The men thus appear to be discussing the purchase of a plane for a president; 330 and 320 are models of airplanes built by the aircraft manufacturer, Airbus. An Airbus 320 costs around US$20 million.[125] In Kazakhstan, the management of presidential aircraft falls under the jurisdiction of the Directorate of Affairs of the President (*upravlenie delami Prezidenta*), according to a government decree from 2002.[125] As highlighted above, Ni worked in this office in the 1990s. According to opposition politician Eric Dos, speaking to Global Witness in 2007, Ni had been in charge of the purchase of the first presidential plane in 1994 when Ni worked in Nazarbayev's office and Dos in the Vice-President's.[126]

In a second audiofile, voices seem to be discussing donations to the Nur Otan party (the political party headed by Nursultan Nazarbayev). A man is asked by another individual whether he has transferred money to this party. The man says he has. The transcript provided by Aliyev in his book alleges that the man asking whether the money has been transferred is Vladimir Ni.[127] In a third file, a man asks another individual whether he made the payment to the "Nur Otan account". The man replies, "Yes, 20, exactly 20." The transcript provided by Aliyev alleges that this reply is given by Vladimir Ni and that the figures represent millions of dollars.[128]

In a further audiofile, a man is heard discussing with a woman the construction of what is referred to as a "party building". The man says, "I'm paying 30 of it and Volodya is paying the remaining 70." Aliyev's transcript alleges that the conversation is between Ni and his wife.[129] If Aliyev's allegations are true and the files genuine, it would mean that Vladimir Ni is both canvassing for money for President Nazarbayev's party and actively paying money towards the party and party infrastructure.

Following the revelation of the audiofiles in November 2007, Kazakhmys held a press-conference in Kazakhstan. A subsequent report on a Kazakh television news programme described the audiofiles as "crude falsifications". Vladimir Kim, on camera, then states, "Can you really imagine talking to the president in this fashion?" Vladimir Ni then says that he was not involved in the conversations that were posted on the internet.[130]

Concerning the allegation regarding the aircraft, Ni added: "We, the company, ordered an aircraft for our own use… The state bought the aircraft from us. We did not give it as a present as was written [on the internet]… It lawfully purchased [the aircraft] for the presidential aviation fleet."[131]

Information should be available to shareholders when a company buys and sells such an expensive asset as an aircraft. However, Global Witness could find no mention of the purchase of a plane and subsequent sale to the presidential fleet in Kazakhmys annual reports or press releases. The company's annual report of 2006 mentions that it uses its own aircraft to operate a regular commercial service between Almaty and Zhezkazgan,[132] and the 2007 annual report states that the company spent money on new aircraft as part of the fleet replacement programme,[133] but we could find no reference to Kazakhmys selling a plane to the presidential fleet.

Global Witness also examined websites detailing the histories of state-owned planes. This can be done by tracking planes' serial numbers. Websites indicate that the Kazakh government has owned or leased at least two VIP Airbus aircraft. The first, a 319, serial number UN-A1901, was leased to the Kazakh government between January 2007 and June 2008.[134] Another Airbus, a newly built 320 model, serial number UP-A2001, was bought by the Kazakh government in 2007[135] and was photographed in Palma, Majorca by a plane-spotter in late July 2008.[136] Global Witness could find no plane currently owned by the Kazakh government and listed on these websites that was previously owned by Kazakhmys.[137] Nor could we find an Airbus 330 model (mentioned at the start of the audiofile) owned by the Kazakh government.

Global Witness wrote to Kazakhmys to ask for more information regarding the sale of the aircraft that Ni mentioned and asked both him and Vladimir Kim in what way they considered the audiofiles to have been fabricated. We also asked if the company had made any political donations to parties in Kazakhstan, as Kazakhmys annual reports 2006-09 only mention that it did not give any money for political purposes in the United Kingdom, nor make any donations to EU political organisations.[138] The company declined to answer individual questions (see Chapter 12) and Ni and Kim did not respond to requests for comment.

The audiofiles, if genuine, would confirm the allegation made by a number of sources, that Vladimir Ni aids President Nazarbayev in his affairs, that both Ni and Kim are closer to Nazarbayev than has been disclosed, and that these relationships would have the potential to affect Kazakhmys plc's operations.

It is therefore up to the FSA to investigate the veracity of the audiofiles and the information contained in them. It should investigate the relationship between Kim, Ni and Nazarbayev, whether the company has done enough to disclose this relationship and Ni's admission about the company selling a plane. Clarifying this relationship would be vital to ascertain how and for whose primary benefit Kazakhmys plc is run.

DINING OUT – BUT AT WHOSE EXPENSE?

Global Witness has obtained one piece of evidence that suggests that Kazakhmys plc has helped the Kazakh government in the arrangement of the president's travel plans. It is a copy of a hotel bill for Nazarbayev's stay in the Lanesborough Hotel when he stayed in the United Kingdom on an official visit in November 2006. The bill is for around £36,000 and was sent to a Mr John Rosewell at Kazakhmys plc. The bill includes over £1,600 of dining and beverage charges made from 19 to 23 November. The bill appears to have been paid in advance by a bank transfer from Kazakhstan though it is not clear by whom.[139] It is unclear why Kazakhmys plc was sent the bill in the first place, as presumably the Kazakh Embassy in London would arrange the logistics of the presidential visits to the United Kingdom. Global Witness wrote to Kazakhmys plc to ask if the bill had been sent to the company, and for what reason. The company declined to answer individual questions. Global Witness tried to contact Rosewell directly at the company's headquarters in July 2010 but a switchboard operator said he was not listed as working there. The Lanesborough Hotel declined to comment on the hotel bill.

THE 5-STAR LANESBOROUGH HOTEL IS ONE OF LONDON'S MOST EXCLUSIVE

Global Witness

WHO OWNS THE COMPANY?

The shareholding structure of Kazakhmys was very opaque through 2004 up until the company listed on the London Stock Exchange in October 2005. As noted earlier, it was not until the issue of the listing prospectus, weeks before the listing itself, that the company revealed that its senior managers owned 98.8% of its shares.[140]

This came as a surprise to a group of Kazakh opposition politicians, who wrote in letters to the FSA that both they and the wider Kazakh public still thought that South Korea's Samsung Corporation, who had bought into the company in the 1990s,[141] remained a major shareholder. No Kazakhmys annual report (which would have contained information regarding its shareholders) was produced in 2004 as, in order for the company to be restructured and incorporated in London, Kazakhmys delisted that year from the Kazakhstan Stock Exchange.[142] Articles indicating that the company's senior managers owned virtually all of the company's shares only started appearing in the press at the end of September 2005,[143] weeks before the company listed in London, suggesting that the ownership of the company by the senior managers was not known by the general public before this point.

In a written response to questions from Global Witness, Samsung stated that in November 2001 it sold a 15% stake in Kazakhmys for US$94.73 million to a company called Cuprum Holding B.V., owned as of 2002 by Vladimir Kim according to the listing prospectus.[144] Samsung then sold the remainder of its Kazakhmys shares in August 2004. Global Witness could find no announcement on the part of Kazakhmys that the Korean company had sold these shares in 2004. Samsung responded to Global Witness that it "made public disclosures regarding the sale in compliance with applicable regulations."[145]

Samsung added that it divested its shares for many reasons, including diminishing returns and "because the overall business environment [in Kazakhstan] turned unfavorable to foreign investors due to the abolition of policies adopted to encourage foreign investment and worldwide trend of the resources nationalism. […] We thought that it was a good time to divest the shares and exit from the business because the copper price was rising. Most of the research institutions specialized in the metal industry forecasted that the copper price would be on a downward trend at the end of 2004 though it rose slightly in the beginning."

On the reason why Samsung sold its shares despite the prospect of a potentially lucrative listing in London, the company commented, "We determined that it would be very difficult for Kazakhmys to be listed in the London Stock Exchange within three or four years because Kazakhmys would not be able to satisfy all the strict and complicated listing requirements such as high environmental standards." In actual fact it took 16 months from Kim's announcement of Kazakhmys' intention to list (May 2004) to Kazakhmys plc's debut (October 2005).

Samsung sold its remaining shares in Kazakhmys (totalling 27.55% of the company) to an offshore entity then controlled by a Kazakhmys manager (who no longer works for Kazakhmys) for US$62.5 million in August 2004.[146] Samsung confirmed to Global Witness that it recorded this sale as a US$141.1 million loss, though the company added: "That was a loss appearing on the financial statement only calculated based on the equity method. The company gained profit under the cash basis method."[147]

WHERE DID THE CAPITAL COME FROM?

The near total ownership by a small group of managers of a large company like Kazakhmys would need a lot of capital: an article in *The Mining Journal* reported in 2005 that European hedge fund investors had valued the company pre-IPO at US$1.3 billion.[148] Samsung has provided some details about how much Kazakhmys' senior managers paid for the shares bought from Samsung. Yet information concerning how much the managers paid for all the shares they bought is incomplete. It also begs the question: where did these men get the capital to fund these purchases?

The Kazakhmys prospectus says that the holding companies controlled by the company's senior managers: "acquired their interests in Kazakhmys through a combination of market purchases, participation in the 2003 share issue by Kazakhmys (through pre-emptive participation and underwriting) and acquisition from Samsung and other shareholders in Kazakhmys. They acquired their shares in the company through exchanging their Kazakhmys holdings or by purchase of such shares from other existing shareholders."[149]

There is no information in the listing prospectus regarding the price these men paid for their shares, except for this sentence: "In May 2005, Mr Novachuk bought approximately 41% of the shares of Harper Finance Limited [a shareholder

WHAT DO INVESTORS IN LONDON KNOW ABOUT KAZAKHMYS' OPERATIONS IN ZHEZKAZGAN?

Global Witness

in Kazakhmys] for a consideration of approximately [US]$135 million."[150] No information is given regarding the source of Novachuk's US$135 million or other funds used to purchase shares.

The Mining Journal wrote around the time of the listing that Kazakhmys chairman Vladimir Kim was not going to sell any of his current shares and had converted his debts by taking dividends from the company, whereas two other managers (including Novachuk) had borrowed money from banks to buy shares.[151] Kazakhmys plc declined to answer individual questions when we wrote to them for more information.

THE CURRENT SHAREHOLDERS

According to the Kazakhmys 2009 annual report, as of 29 March 2010, shareholders who held more than 3% in the company were:[152]

Cuprum Holding B.V. **25.4%**

(registered in Netherlands)[153]
[owned by Vladimir Kim]

Kazakh government[154] **15%**

Tobermory Holding Europe B.V. **9.5%**

(Netherlands)
[owned by Vladimir Kim]

Harper Finance Limited **5.5%**

(British Virgin Islands)
[owned by Oleg Novachuk]

Perry Partners S.A **4.0%**

(British Virgin Islands)
[owned by Vladimir Kim]

However, the 2009 annual report also gives the number of total shares held by each director[155] – this number is larger, in Oleg Novachuk's case, than the number of shares he owns through an investment vehicle. This means that, by percentage of the company's shares, the following individuals own as of 29 March 2010:

Vladimir Kim **38.9%**

(through the above three investment vehicles)

Oleg Novachuk **6.5%**

(of which 5.5% is owned through Harper Finance Limited)

Vladimir Ni **2.18%**

= 47.58%

These tables show that the three men own 47.58% of Kazakhmys plc, either directly or through investment vehicles. The size of their combined stakes in the company has fallen since March 2007, when it stood at 59.89%.[156] Since then, the Kazakh government has bought back into the company. The allegations about Kazakhmys' relationship with the Kazakh government remain troubling because the three men's shareholdings, combined with that of the government, amount to a controlling majority stake in the company.

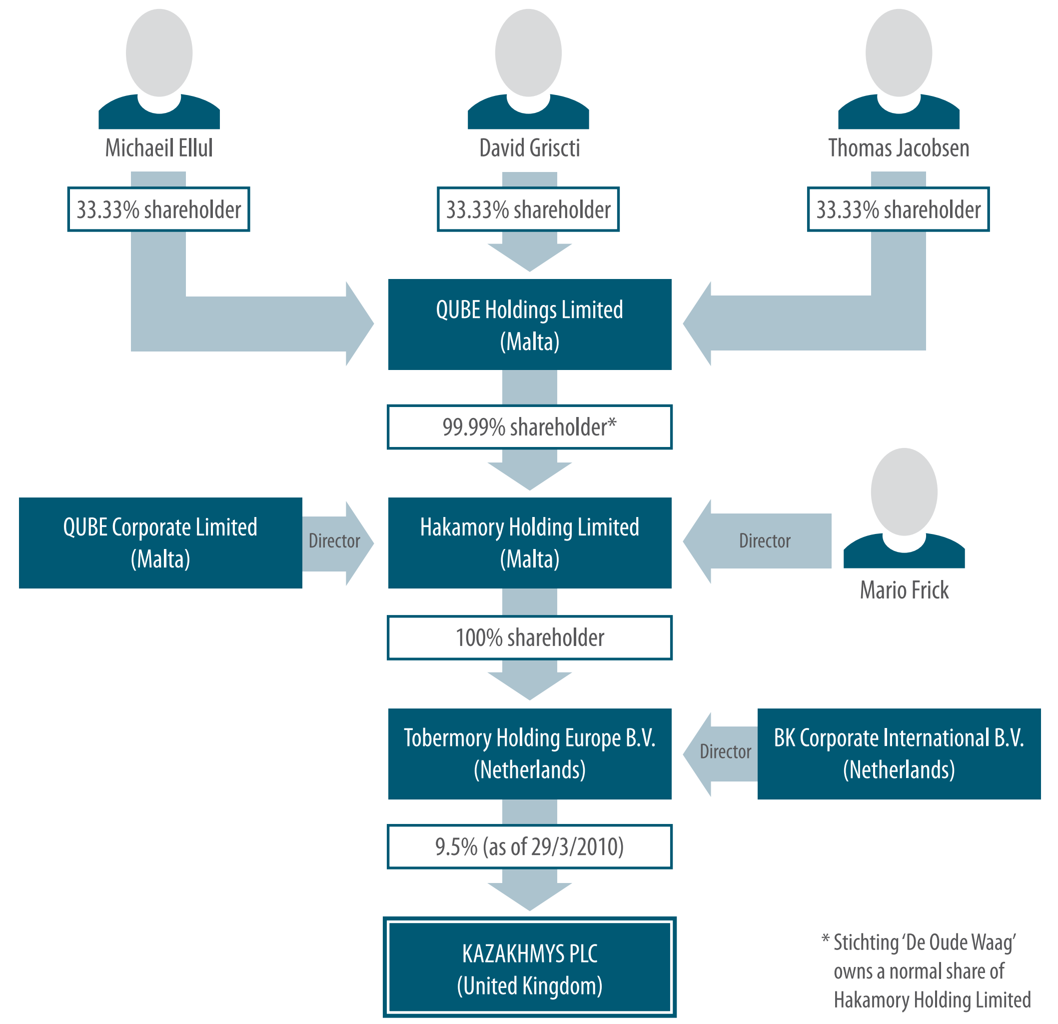
Since the company listed in London, the Kazakh managers have always owned about half or more of the company.[157] The fact that Kim is the largest shareholder in the company is important because as he is also the company chairman, it means he is not classified as independent under the Combined Code (see Chapter 11). It therefore becomes crucial whether investors can trust that these men are not influenced by political pressures and can run the company independently for the benefit of the company's shareholders.

KIM'S KAZAKHMYS OFFSHORE VEHICLES: BRITISH VIRGIN ISLANDS, LIECHTENSTEIN AND MALTA

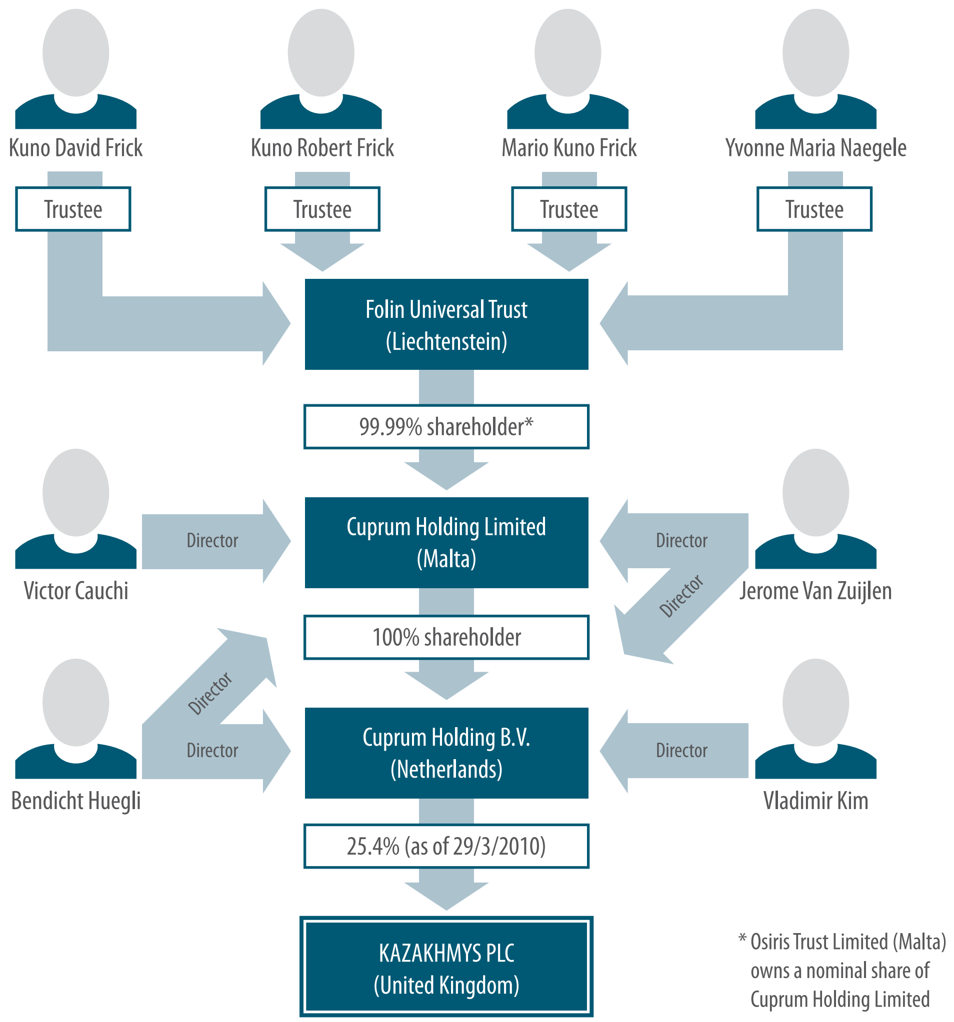
In company literature, Kazakhmys plc says that Vladimir Kim owns shares in the company through various offshore structures. Yet Kim's ownership of these offshore entities cannot be verified by publicly available corporate documents. For example, Kazakhmys' annual report for 2009 says that Vladimir Kim owns 9.5% of Kazakhmys plc through a company called Tobermory Holding Europe B.V. (registered in the Netherlands).[158] This company is in turn owned by a number of further structures, as demonstrated on the i2 chart below.

Internet searches of the three men at the top of the 'tree' reveal that they are partners in a Maltese financial services company[160] which suggests that they are nominee shareholders acting on behalf of another person or people. Kim's name does not feature on any of these corporate documents obtained from registries. The auditor's report of Hakamory Holding Limited (which owns

Structure of Tobermory Holding Europe B.V.[159]



Structure of Cuprum Holding B.V.[162]



Tobermory), dated 11 December 2008, states: "disclosure has not been made in these financial statements of the identity of the company's ultimate controlling party as required by International Accounting Standard 24. The directors [QUBE Corporate Ltd and Mario Frick] have explained that they do not have the appropriate authority to disclose the identity of the ultimate controlling party."[161] It seems odd that the directors of Hakamory Holding Limited do not have authority to disclose the identity of this party when the asset the company holds (shares in Kazakhmys plc) is openly owned by Vladimir Kim, according to Kazakhmys plc annual reports.

Another entity through which Kim owns shares in Kazakhmys plc (around 25% of the company) is called Cuprum Holding B.V. Its ownership structure is on the second i2 chart above.

Cuprum Holding B.V.'s registry records do mention that Vladimir Kim is a director of this company, along with a Swiss citizen named Bendicht Fred Huegli and a Dutch citizen named Jerôme André van Zuijlen, as shown above. However, corporate registry records leave the structure opaque, as the ultimate holding company in this structure is a trust arrangement in Liechtenstein, named the Folin Universal

"The directors have explained that they do not have the appropriate authority to disclose the identity of the ultimate controlling party..."

(FINANCIAL STATEMENTS OF KAZAKHMYS SHAREHOLDING COMPANY)[161]

Trust, whose beneficiary is not disclosed in publicly available records. According to the Liechtenstein corporate registry, this company was issued with a statute in July 1995. The statute was changed on 30 November 2006, although the same company, TTA Trevisa-Treuhand Anstalt, has managed the trust throughout.[163] It is not clear what this change in the statute indicates. The registry office in Liechtenstein told Global Witness that this document was not publicly available.[164]

Kim is not named in these corporate documents from Liechtenstein. Instead, the names of several trustees (*Treuhaender*) are given. These are Yvonne Maria Naegele, Kuno David Frick, Kuno Robert Frick and Mario Kuno Frick, all of whom are managers of companies in Liechtenstein, including TTA Trevisa-Treuhand Anstalt.[165]

Mario Frick is also named as a director of another of Kim's investment vehicles (Hakamory Holding Limited, see above).[166] He is a former prime minister of Liechtenstein,[167] who also manages a Liechtenstein bank, Bank Frick, along with Kuno Frick and others.[168]

Vladimir Kim has done nothing illegal by controlling his assets through a series of trusts and offshore vehicles. Yet the inconsistency is clear: on one hand Kazakhmys is listed on the main market of the London Stock Exchange, where companies have to be transparent and open concerning their structure, management and operations. On the other hand, the ownership structure of the company is obscured by various offshore companies and trust arrangements, with the directors of one such company stating that they do not have the authority to name the ultimate controlling party. Investors therefore have to take it on trust that Vladimir Kim is indeed the owner of these Kazakhmys plc shares.

Global Witness asked several questions to Kazakhmys plc and to Vladimir Kim about the company's shareholding structure and the offshore structures that historically and currently possess shares in Kazakhmys plc. The company declined to answer individual questions but on the company's owners it replied, "as required by the Prospectus Rules, the Company disclosed full details of its shareholders in its IPO prospectus, which were subject to extensive verification prior to publication and has continued to disclose details of its shareholders to the market and in its annual reports since IPO as required by the FSA and the Companies Acts."[169] We wrote again to ask for more details regarding the "extensive verification" of its shareholders. The company did not reply.

Global Witness requested more information from the FSA under the Freedom of Information Act regarding the due diligence that was performed on Kazakhmys before it listed. The request was refused (see Chapter 13). We also wrote to Kazakhmys plc's sponsor, JP Morgan Cazenove, to ask what due diligence it performed, including what documentation it had obtained to prove the ownership of Kazakhmys' main shareholding companies, namely Cuprum Holding B.V., Perry Partners S.A. and Harper Finance Limited. The company did not reply.

CHAPTER 11

VLADIMIR KIM'S CHAIRMANSHIP & THE COMBINED CODE

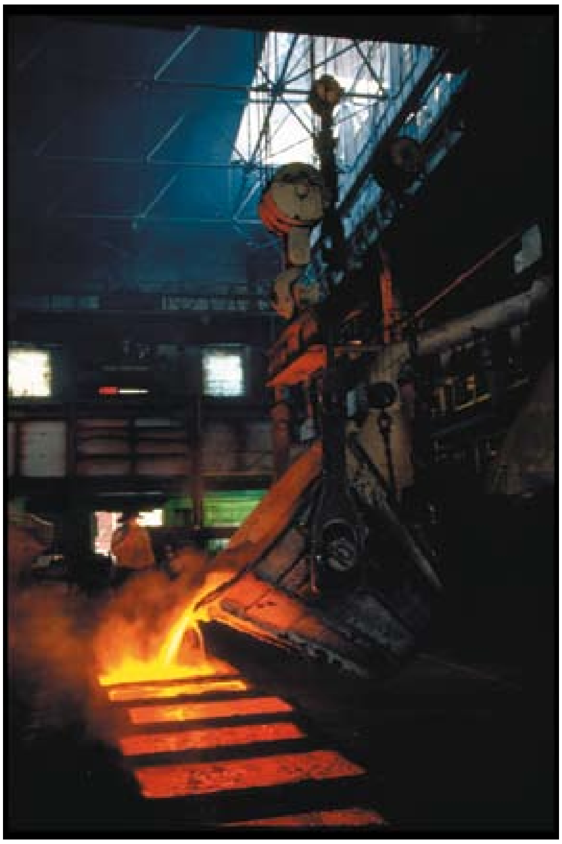
The FSA governs the London Stock Exchange but another independent regulator, the Financial Reporting Council, aims to promote confidence in corporate reporting after a company has listed with such documents as the Combined Code on Corporate Governance, which explains the principles regarding good governance.[170]

The aim of the code is of an advisory nature with the onus on a company's shareholders to decide what to do if a company is non-compliant. Listed companies are required "to report on how they have applied the main principles of the Code, and either to confirm that they have complied with the Code's provisions or – where they have not – to provide an explanation."[171] This is often referred to as the 'comply or explain' principle.

Kazakhmys plc's last annual report highlights the fact that in one key area the company has not met the requirement of the Code and continues to not be compliant: "The chairman was not independent at the time of his appointment. This arises due to Vladimir Kim's significant shareholding in the Company. Vladimir Kim joined the Group in 1995 and has made a major contribution to its development into an international company. The Board is unanimously of the opinion that his continued involvement in an executive capacity is vitally important to the success of the Group."[172]

KAZAKH COAL MINERS.

REUTERS/Stringer Russia



MOLTEN METAL BEING POURED IN UST-KAMENGORSK, KAZAKHSTAN

Robert Nickelsberg/Time Life Pictures/Getty Images)

"The Board is unanimously of the opinion that [chairman of Kazakhmys plc Vladimir Kim's] continued involvement in an executive capacity is vitally important to the success of the Group. "

(KAZAMYS PLC ANNUAL REPORT)[172]

The comment from the Kazakhmys annual report, that the board is unanimous about Kim's continued involvement in an executive capacity, does not address the issue of why Kim is the chairman. The chairman's roles, as outlined by the Kazakhmys annual report of 2009, are as follows: "setting a vision for the Group and formulation of its strategy; providing leadership to the Board, ensuring the effectiveness of the Board on all aspects of its role and setting its agenda; ensuring effective communication with shareholders; facilitating the effective contribution of non-executive Directors and ensuring constructive relations between executive and non-executive Directors; providing leadership to the senior management team; ensuring the creation and maintenance of safe working environments within the Group's operations; and maintaining effective and constructive relations with the Government and business community in Kazakhstan."[173]

A question arises from this: for the above roles to be fulfilled, why does the chairman of Kazakhmys plc have to be Vladimir Kim, who is the company's largest shareholder and not independent as defined by the Combined Code? Kim's background suggests that he would have an advantage only in the last of the above roles – maintaining effective and constructive relations with the Kazakh government and business community – though this is not specifically a chairman's job.

It is a key requirement that the chairman of a company listed in London is independent as defined by the Combined Code. It is highly unusual for a FTSE 100 chairman to own a substantial share of the company. The only other oil, gas or mining company on the FSTE 100 in a similar situation is Vedanta, where the chairman owns a controlling share in the company. The background to this firm is a little different, however: the company was founded by its current chairman back in the 1970s and was very much a family firm.[174]

There is a risk that a chairman such as Kim with executive powers and a substantial shareholding will dominate views and opinions and is unlikely to be independent or be seen to be independent. That is why the chairman is meant to be independent. One could argue that in this case, Kazakhmys plc has neither complied nor explained properly why they do not comply. It is up to Kazakhmys plc shareholders to raise this issue at the company's annual general meetings.

CHAPTER 12

THE COMPANY'S RESPONSE

Global Witness searched media archives on Kazakhmys' responses concerning the allegation that President Nazarbayev can exert influence over Kazakhmys plc through his relationship with certain managers. In a 2006 interview conducted by *The Times*, senior Kazakhmys manager Oleg Novachuk denied that the company was controlled by the family of President Nazarbayev, though he admitted that the Kazakh president's brother was on a Kazakhmys board at that time, after Kazakhmys plc listed on the London Stock Exchange.[175]

The Times of Central Asia reported in March 2006 that at a news conference in London Vladimir Kim stated, "just imagine what could happen if someone from the [Kazakh] President's Administration owned at least one stock [in Kazakhmys]. In that case we could not be listed on the London Stock Exchange."[176]

Global Witness has sought comment from Kazakhmys plc several times on these matters. Global Witness first met with John Smelt, Kazakhmys plc's Head of Corporate Communications, in May 2009 for a general discussion about company policies. This was then followed by a short email which was both sent and faxed to Mr Smelt, which asked three questions about company procedures regarding corruption and the safeguards which are in place to ensure the company is run as a business enterprise and is not unduly influenced by political pressures. The company did not reply.

Following further research, Global Witness then sent in August 2009 a series of detailed questions to company secretary Robert Welch, and different questions to Vladimir Ni and Vladimir Kim. Vladimir Ni and Vladimir Kim did not give individual replies to the letters Global Witness sent to them, but Mr Welch replied on behalf of the company:

As you can appreciate, the process undertaken to prepare the prospectus and Kazakhmys for a listing on the main London market was a very vigorous and comprehensive one, involving a thorough due diligence exercise by two international investment banks and two major London law firms. These efforts combined to produce a prospectus which, as required by law, set out all of the information that investors needed to know in order to make a properly informed assessment of a potential investment in Kazakhmys.[177]

The letter from Kazakhmys mentions research from Research Recommendations Electronic Voting (RREV, an entity that serves the corporate governance and proxy voting needs of UK-based institutional investors).[178] The letter quotes from RREV's 2008 AGM report, which states that, "since its IPO in October 2005, it has been evident that the Company takes Corporate Governance very seriously and consequently has taken steps to ensure compliance with most of the recommendations of the Combined Code. RREV would like to note that corporate governance at Kazakhmys is of a high standard."

However, regarding our individual questions over certain aspects of Kazakhmys' business and management, the letter from Kazakhmys plc states:

We do not believe that it is sensible to give answers to specific questions and queries that go far beyond the already rigorous disclosure requirements of a publicly listed company, particularly those which are of a personal nature or relate to individual directors or shareholders. As required by the Prospectus Rules, the Company disclosed full details of its shareholders in its IPO prospectus, which were subject to extensive verification prior to publication, and has continued to disclose details of its shareholders to the market and in its annual reports since IPO as required by the FSA and the Companies Acts. Our intention is to ensure equality of information for all market participants on the basis of a consistent high level of disclosure to the market, a standard with which we comply to the fullest extent possible, as we have done since IPO and will continue to do so.[179]

Global Witness does not agree, in light of our research, that the Kazakhmys listing prospectus gave "all of the information that investors needed to know in order to make a properly informed assessment of a potential investment in Kazakhmys".

We therefore wrote a second letter in October 2009 which stated: "We feel that the questions we posed in our first letters are of fundamental importance to inform potential and current investors as to how Kazakhmys plc is run and therefore we fail to see how answering these questions would go 'far beyond the already rigorous disclosure requirements of a publicly listed company.' The questions which are, in your words, of a 'personal nature', directly affect the ability of these managers to run the company for the benefit of its investors."

We then asked the company why it felt certain information, notably Vladimir Ni's former employment, Vladimir Kim's admission of bribery and Bolat Nazarbayev's position on the Kazakhmys board, was not deemed material for inclusion in the listing prospectus. The company did not reply.

A CLOUD HANGS OVER ZHEZKAZGAN, KAZAKHSTAN

Global Witness

CHAPTER 13

WHAT DUE DILIGENCE WAS PERFORMED?

The time taken between Vladimir Kim's announcement of Kazakhmys' intention to list and the company's debut on the London Stock Exchange was arguably relatively short – 16 months; Samsung sold its shares in Kazakhmys in 2004 thinking it would take three or four years for the company to satisfy all listing requirements.[180]

So the issue of what due diligence was performed on Kazakhmys plc in this time is crucial in addressing the concerns in this report, especially in light of the information that was not included in the prospectus and the discrepancies in the shareholding structure, as discussed on page 23. It is therefore vital to ascertain, in the interest of investors and the wider public interest in efficient, orderly and fair markets, which of the issues raised in this report were investigated before the decision was granted by the FSA to allow the company to list.

The FSA makes the final decision regarding whether a company is allowed to list on the London Stock Exchange. In 2009, Global Witness submitted a Freedom of Information Act request regarding the due diligence that was done on Kazakhmys plc performed by or submitted to the FSA. The request was refused by the FSA, which cited several exemptions. One exemption was qualified and involved the weighing of various interests: "The public interest in maintaining the exemption outweighs the public interest in disclosure of the information requested." The reason for this exemption to be maintained was that "disclosure to the public of the contents of any discussions we have had with regulated firms, or internal documents related to these discussions, would be likely to make decision-makers and firms more circumspect in the information that is asked for, and provided, in the context in the application for listing."[181]

The refusal to release any information by the FSA is troubling: not only is the general public not entitled to learn the details of what was discussed, it cannot even be told what issues were dealt with in the first place. The general public simply has to trust that the FSA is fulfilling its role as a financial watchdog. Yet this is an untenable position, as proven by the economic collapse of 2008 which called into question the effectiveness of the FSA.

In a debate on British television for the 2010 UK general election, Lord Mandelson, the then Secretary of State for Business, commented, "What we should have encouraged the Financial Services [Authority] to do is to be more intrusive," while Kenneth Clarke, at the time the Shadow Secretary of State, commented, "The regulatory system … didn't work, it was quite useless."[182] Though the two men were talking about the regulation of the banking system, it is the FSA which regulates both the banks and the London Stock Exchange. In June 2010 it was announced that the new British government would scrap the FSA by 2012 – a further indictment of the performance of this regulatory body.

The letter we received from the FSA also stated that "the process of carrying out due diligence on firms who wish to apply for a primary listing is the role of the sponsor firm."[183] A sponsor firm is a long-term financial partner which helps the company prepare for a listing by assisting the company to meet its disclosure requirements and other obligations. Kazakhmys plc's reply to our letter states that thorough due diligence was done on the company by two international investment banks. One of these was JP Morgan Cazenove (referred to hereafter as JPMC), which acted as the company's listing sponsor.

In an interview from 2003, Ken Rushton, the then head of the UK Listings Authority (UKLA), the part of the FSA that regulates stock market listings, voiced his concerns regarding the records kept by sponsors on the due diligence they had performed on a company hoping to list: "Some sponsors are not good at maintaining their records so they can demonstrate to us that proper due diligence was carried out on a listing. They don't necessarily do the due diligence themselves but they are responsible for coordinating it and therefore keeping some sort of a record of it. Some of the firms just don't have the records."[184]

Through 2003 and 2004, the UKLA undertook a review of the regulatory regime of stock market listings. The new rules finally came into effect 1 July 2005. An article from a law journal from July 2005 stated that the new rules "require a sponsor to ensure that all matters known to it which, in its reasonable opinion, should be taken into account by the UKLA in considering whether the admission of equity securities would be detrimental to investors' interests, have been disclosed with enough prominence in the prospectus. … the sponsor will now be required to declare that it has reached a reasonable opinion on the sufficiency of disclosure, rather than an opinion on the mere fact of disclosure."[185] These rules would have been in place when Kazakhmys plc listed in October 2005.

This new rule could represent something of a dilemma regarding disclosure for companies who intend to issue shares: the FSA has stated that issuing companies should use appropriate advisers from a sponsor to determine compliance with the listing rules but the whistle-blowing obligation on behalf of the sponsor may discourage these companies from full disclosure.

JPMC must have presumably told the FSA at some point that it was satisfied with the sufficiency of disclosure as Kazakhmys plc was granted a listing and debuted on the London Stock Exchange in October 2005. The time it took to prepare the company for listing was arguably relatively short, especially in light of comments from Samsung made to Global Witness that it estimated the process would take three to four years for the company to meet the listing requirements.[186] A key question that needs to be answered is whether the sponsor was aware of the information included in this report and whether it raised these issues with the FSA.

We therefore wrote to JPMC with questions regarding the due diligence it performed on Kazakhmys, whether it knew about the above issues regarding the company and certain managers, and why it chose not to include certain information in the listing prospectus. Despite various assurances from a secretary in the JPMC chairman's office that our letter was being dealt with, the company has not replied in the five months since it first received the letter.[187]

CHAPTER 14

KAZAKHMYS PLC LISTING PROSPECTUS: NEUTRAL AND COMPREHENSIVE?

Global Witness

WHAT QUESTIONS DID THE FSA ASK ABOUT KAZAKHMYS PLC WHEN IT LISTED?

The independent Committee of European Securities Regulators (CESR) is a body that gives recommendations to the European Commission and to EU member states on regulatory practices.[188] Regarding an issuer's preparation for a listing, the CESR has published recommendations identifying overarching principles that should be borne in mind when dealing with the company's operating and financial review which is part of the prospectus. The FSA will thus take into account an issuer's compliance with the CESR recommendations.

The operating and financial review must be neutral and even-handed and include "information regarding significant factors, including unusual or infrequent events or new developments, materially affecting the issuer's income from operations, indicating the extent to which income was so affected [...] Information regarding any governmental, economic, fiscal, monetary or political policies or factors that have materially affected, or could materially affect, directly or indirectly, the issuer's operations."[189]

Almaz Tleuliev / Creative Commons

KAZAKHMYS BUILDING IN ZHEZKAZGAN, KAZAKHSTAN.

In our opinion, the information in the prospectus was not even-handed, since it did not contain information regarding the senior managers' employment history and the perceived level of corruption in Kazakhstan. JPMC should have been aware of the issue concerning Vladimir Ni's work in the presidential office as biographies (such as the one in the Kazakh version of *Who's Who*) clearly mention Ni's post as Nazarbayev's chief-of-staff, a position that was also known to many people in Kazakhstan.

If this is the case, and JPMC did know about Ni's former employment history, the question then becomes why the sponsor did not deem this information material enough to be included in the company listing prospectus.

It is up to the FSA to determine whether all company executives pass compliance procedures when companies apply for a listing and it is up to the company's sponsors to provide full information regarding key personnel.

Again, however, what in our opinion would constitute key information was not included in the Kazakhmys listing prospectus. Not only was Vladimir Kim's biography very scant, the prospectus failed to mention that in 2001 he was involved in a high-profile political trial in Kazakhstan, in which he accused a former Kazakh prime minister of corruption, implicating himself in the process.

Again the question is whether JPMC knew about Kim's testimony in a Kazakh court (information about which was published in the Kazakh press and is still easily available on the internet) at the time the prospectus was written and, if so, why the sponsor did not deem this information material enough to be included in the company prospectus.

Even if JPMC had not known about Kim's testimony, it was informed by a group of Kazakh opposition politicians in a letter to the FSA that was copied to them. The letter is dated 8 October 2005, the day after Kazakhmys plc debuted on the London Stock Exchange, and so after the publication of the listing prospectus. According to an associate of the group of Kazakh politicians, they did not receive a reply.

It is up to the company's directors to ensure not only that the prospectus is accurate, comprehensive and does not mislead but also that any information subsequently discovered to be necessary for investors is communicated as swiftly as possible to co-directors, the company, the company's advisers, the FSA and the investing public. Yet JPMC, Kazakhmys plc and the FSA appear not to have issued any statement regarding any of the above omissions since the IPO.

CONCLUSION: TIME FOR A CHANGE IN REGULATION

A position on the 'blue chip' FTSE 100 share index ought to signify exemplary standards in all areas of a company's business. The purpose of the listing principles is to ensure that listed companies pay due regard to the fundamental role they play in maintaining market confidence and ensuring the integrity of the market. However, the growing number of companies listing in the United Kingdom which operate abroad and have board members from countries that are perceived to be corrupt raises the issue that the market's principles may be compromised. One commentator in *The Independent*, writing in 2006, stated: "The LSE [London Stock Exchange] has become a soft touch for any foreign company seeking a brass plate, access to capital and the kudos of a listing on one of the world's two most important markets. It may make the LSE's numbers look good [...] But ultimately, there must be a reckoning. The very success that the LSE boasts of today threatens to undermine its standing tomorrow."[190]

These companies should be welcomed to British markets on the proviso that they are well-governed and the available information is comprehensive. But at this point it is unclear what due diligence was done on Kazakhmys plc, whether these procedures were adequate and whether they dealt with the issues discussed in this report. It is unclear what research JPMC and the FSA did on Vladimir Ni and Vladimir Kim to ascertain that they were fit and proper people to be the managers of a publicly traded company.

What does seem apparent is that the FSA relies on the sponsor for the majority of its due diligence, even though it is

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in the sponsor's financial interest to see the company listed. The above comments from 2003 from the then-head of the UKLA, Ken Rushton, make it clear that the sponsor does not always do the due diligence itself[191] – making it hard to pin down who ultimately is responsible. There seems to be, from what Global Witness can ascertain, no third party check of the information. A complaints procedure is in place for those investors who feel that they have suffered a material loss over what they consider to be inadequate or misleading information but there does not seem to be an adequate system to prevent such a situation happening in the first place.

Compared to the United States, the United Kingdom's relative 'soft touch' regulatory regime has been named as a reason why companies often favour a listing in London. London Stock Exchange regulations require that listed companies have to follow certain principles or show why they do not, the 'comply or explain' model, a principles-based regulatory system rather than rules-based. Its supporters regard it as more flexible and less burdensome than the American system, while its detractors consider it to be 'wishy-washy' as it is difficult for companies to run foul of the rules. As one British parliamentarian commented in 2004, "[our regulations] simply don't produce the rattle of tumbrils necessary to change behaviour."[192]

But has the UK system gone too far in allowing flexibility? As the commentator from *The Independent* stated: "You can argue that the reporting and disclosure requirements demanded by the US authorities, and the criminal penalties that go with failure to comply, have become too onerous. But, equally, the pendulum has swung too far in the opposite direction on this side of the Atlantic."[193]

In the rush to attract foreign investment, the United Kingdom may also have neglected to ask certain ethical questions. If a person running a company is shown to be close to a corrupt government official, is the United Kingdom inadvertently giving legitimacy to authoritarian rulers and strengthening their grip on power by allowing such a company to list?

In June 2010, it was announced that the FSA is to be scrapped by 2012 and replaced by one of two new Bank of England supervision units and other bodies.[194] This is therefore a good opportunity for a re-examination of the regulations of the London Stock Exchange in order to address the issues contained in this report.

In an era of complex financial markets, it is imperative that potential investors understand the risks they are facing. Investors in companies from developing economies where there is a risk of governmental or presidential interference need to know that the company is independently governed and that its revenues are not going to support the apparatus of the ruling elite. The need is all the more important for FTSE 100 index companies which make up the investment portfolios of pension funds. The public interest, and the interest of investors, requires a regulatory system that is capable of dealing with these issues, especially the financial relationship between a state and the company. Only then will we be able to say that London's financial markets possesses, as the London Stock Exchange's Chief Executive commented at the time of Kazakhmys plc's listing, "world-leading regulatory and corporate governance standards".[195]

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