

CITATION: Sistem Muhendislik Insaat Sanayi Ve Ticaret Anonim Sirketi v. Kyrgyz Republic,
2014 ONSC 2407
COURT FILE NO.: CV-11-9419-00CL
DATE: 20140415

**SUPERIOR COURT OF JUSTICE – ONTARIO
COMMERCIAL LIST**

RE: Sistem Muhendislik Insaat Sanayi Ve Ticaret Anonim Sirketi,

AND:

Kyrgyz Republic and Kyrgyzaltyn JSC

BEFORE: Justice J.A. Thorburn

COUNSEL: *G. Pollack* and *S. Frankel*, for the moving parties
B. Casey and *C. Doria*, for the responding parties,

HEARD: December 17 and 18, 2013

ENDORSEMENT

Relief Sought by Sistem

[1] Sistem seeks a declaration that the Kyrgyz Republic (the Republic) owns or has an equitable or other right, property or interest in Centerra shares registered in Kyrgyzaltyn JSC's name.

[2] Sistem also seeks an Order permitting the Sheriff to seize enough of the Centerra shares (or dividend monies paid on those shares) in Kyrgyzaltyn JSC's name to satisfy Sistem's arbitral award.

History of this Proceeding

[3] In 1992, Sistem entered into a joint venture with a Kyrgyz company to build the Hotel Pinara in Bishkek, the capital of the Republic. The Kyrgyz company went bankrupt and Sistem purchased its interest in the project. Sistem became the sole owner of the project in 1999. In 2005, Sistem was evicted from the Hotel Pinara at gunpoint and the property was expropriated.

[4] Sistem commenced arbitration proceedings against the Republic pursuant to a bilateral investment treaty between Turkey and the Republic. An arbitral tribunal was constituted

pursuant to the International Center for Settlement of Investment Disputes, an organ of the World Bank.

[5] On September 9, 2009, the arbitral tribunal held that the Republic was legally responsible for the illegal expropriation of the Hotel Pinara and was ordered to pay to Sistem \$8.5 million US plus interest and costs of over \$600,000. The arbitral award is final and binding.

[6] Sistem has tried to enforce the award without success.

[7] On October 10, 2010 Sistem filed an Application in the Ontario Superior Court for an order recognizing the Award and rendering it enforceable in Ontario. The Republic was served but filed no responding materials.

[8] On January 5, 2011 Echlin J. granted an Order recognizing and enforcing the award in Ontario and ordering the Republic to pay Sistem in accordance with the arbitration award.

[9] In August 2011, Sistem brought a motion to add Kyrgyzaltyn as a party to this proceeding and to seek declaratory relief to permit the seizure of enough of the Centerra shares to satisfy the award. Both the Republic and Kyrgyzaltyn were served and neither filed responding materials. Cumming J. allowed Sistem's motion and found that "given the evidentiary record, Sistem has an arguable case that the subject shares in Centerra are properly subject to attachment in satisfaction of the Award." The Amended Notice of Application was issued and served on both the Republic and Kyrgyzaltyn.

[10] In July 2012, Brown J. dismissed Kyrgyzaltyn's motion to set aside the Recognition Order. He also ordered that if the Republic intended to participate in this proceeding, it would have to file an appearance by September 1, 2012. It did not do so. That time was later extended to March 2013 but the Republic still did not participate.

[11] On August 17, 2012, Strathy J. (as he then was) granted an *ex parte* motion for a Mareva injunction to prevent Kyrgyzaltyn's disposition of the Centerra shares or dividends declared on those shares. He found that "there is evidence to support Sistem's position that Kyrgyzaltyn holds the shares for the Republic" and "there are reasonable grounds to believe that there are assets of the Republic, or assets held for its benefit, in this jurisdiction." The Mareva injunction was extended by Newbould J.

[12] Pursuant to the Mareva injunction, 4,000,000 Centerra shares registered in Kyrgyzaltyn's name remain frozen and more than \$11.2 million in dividend monies are being held in trust to the credit of these proceedings.

The Issues

[13] The key issue to be determined is whether the Republic owns the Centerra shares in the name of Kyrgyzaltyn JSC or has an equitable or other right, property or interest in those shares within the meaning of section 18(1) of the *Execution Act*. R.S.O. 1990 C.E-24 such that the Sheriff should be ordered to seize and sell them to satisfy the arbitration award against the

Republic. The issue is not (as Kyrgyzaltyn suggests) whether Kyrgyzaltyn and the Republic are one and the same.

[14] If the Republic has an interest in the Centerra shares, the Respondent Kyrgyzaltyn claims the Order should not be granted as the Republic was not properly served with this Application.

[15] If the Republic does not have a right or other property interest in the Centerra shares, Kyrgyzaltyn seeks to lift the Mareva injunction so that it can dispose of the Centerra shares.

The Circumstances Surrounding Kyrgyzaltyn's Acquisition of the Centerra Shares

[16] Centerra is a publicly traded Canadian mining company that has extensive operations. Through its subsidiaries, Centerra operated the Kumtor gold mine in the Republic. Centerra's head office is in Toronto and its shares are traded over the Toronto Stock Exchange.

[17] The Kumtor project is of great importance to the economy of the Kyrgyz Republic.

[18] Originally, Kyrgyzaltyn JSC was a State Concern with no separate corporate existence. Under a plan of denationalization in 1999, Kyrgyzaltyn was created as an open Joint Stock Company wholly owned by the Republic through the State Property Fund. All assets previously owned by the State Concern were transferred to this new Corporation.

[19] Kyrgyzaltyn owns 77,401,766 shares of Centerra. The Republic is Kyrgyzaltyn's only shareholder.

[20] On December 31, 2003 the share ownership of the Kumtor mine was restructured. Centerra became the sole shareholder of Kumtor. Kyrgyzaltyn represented to Centerra that it was the "sole beneficial owner of and ... has all necessary legal ability and authority to sell and deliver the Kumtor stock."

[21] In September 2004, the Republic passed a resolution directing the State Committee for Property Administration (as a shareholder of Kyrgyzaltyn), to pass a shareholder's resolution authorizing dividend funds from the sale of 7.5 million C shares to be given to the Republic.

[22] In April 2009, Centerra, the Republic, Kyrgyzaltyn and others entered into an Agreement on New Terms.

[23] The Agreement on New Terms was part of the settlement of a dispute between the Republic and Centerra concerning the Kumtor gold mine. The Agreement on New Terms provides for the issuance or transfer of more than 43 million Centerra shares to be registered in Kyrgyzaltyn's name. All of the consideration for these new shares was given by the Republic. In exchange for the issuance and transfer of these shares, the Republic expanded the Kumtor mining concession and implemented a more favourable tax regime for one of Centerra's subsidiaries. This was recorded in the Restated Concession Agreement to which Kyrgyzaltyn was not a party.

[24] The Agreement on New Terms is governed by New York law.

[25] Section 2.2 of the Agreement provides that the treasury shares would be issued to Kyrgyzaltyn so that “Kyrgyzaltyn will beneficially own” such shares and be “entitled to all the benefits arising from such shares”. Other provisions in the agreement indicate that Kyrgyzaltyn holds the shares of Centerra “on behalf of the Government”. (The Government is referred to in these reasons as the Republic.)

Positions of the Parties

A. Sistem’s Position

[26] Sistem claims the Republic owns or has a beneficial interest in the Centerra shares.

[27] Sistem claims that as a matter of fact, the Republic owns or has an interest in the Centerra shares. The Agreement on New Terms expressly provides that the Republic has an interest in the shares of Centerra. Moreover, the Republic gave consideration for the Centerra shares issued pursuant to the Agreement on New Terms and the Republic approved the decisions concerning the disposition of the Centerra shares. The Republic’s understanding that it owned the shares is evident from the public statements made by the Republic and others.

[28] Sistem further claims that as a matter of Kyrgyz law, the Republic owns the Centerra shares. The Kyrgyz *Civil Code* permits the Republic to own property and the Republic purchased Centerra shares using Kyrgyzaltyn JSC as its vehicle. A special set of rules were enacted to control the Centerra shares. Moreover, Sistem claims the Republic exceeded its authority as a 100% shareholder of Kyrgyzaltyn.

[29] Thirdly, Sistem contends that Kyrgyzaltyn does not and cannot own the Centerra shares. According to article 222 of the Kyrgyz *Civil Code*, in order to own shares, a party must have the right to possess, enjoy and dispose of property. Sistem claims Kyrgyzaltyn does not have the right to enjoy or dispose of the shares without the approval of the Republic.

[30] In her affidavit, Ms. Smanalieva, Sistem’s expert on the law of the Republic concludes that the Republic is the true owner of the shares and that Kyrgyzaltyn holds the Centerra shares on behalf of the Republic. She, unlike the Respondent’s expert Ms. Molodanova, reviewed the Agreement on New Terms before providing her opinion.

[31] The court should therefore find that the Republic has an interest in the shares within the meaning of section 18 of the *Execution Act* and the Sheriff should be ordered to seize enough of those shares to satisfy Sistem’s arbitration award against the Republic because they are either held by or for the Republic.

B. Kyrgyzaltyn JSC’s Position

[32] Kyrgyzaltyn JSC claims the Republic has no ownership or beneficial interest in the Centerra shares.

[33] As a matter of fact, Kyrgyzaltyn keeps its own accounts, shares are registered in its name and dividends are paid to it. Kyrgyzaltyn is a large company specializing in the development of gold deposits. It participates in other ventures for the development of gold deposits. The terms of the Agreement on New Terms make it clear that Kyrgyzaltyn (not the Republic) is the owner of the Centerra shares:

- (a) the Agreement on New Terms provides for the issuance or transfer of more than 43 million Centerra shares to be registered in Kyrgyzaltyn's name;
- (b) Article 2.1(a) of the Agreement on New Terms provides that the Centerra shares are to be held, "for the benefit of and on behalf of Kyrgyzaltyn...";
- (c) Section 2.2(a) provides that the Centerra shares "shall be issued by Centerra to Kyrgyzaltyn so that Kyrgyzaltyn will beneficially own and be entitled to all the benefits arising from (including the exercise of all rights attaching to) such shares, subject only to the terms of this Agreement on New Terms and the Restated Shareholders Agreement..."; and
- (d) resolutions enacted by the Republic direct its State Committee to call shareholder meetings as a shareholder of Kyrgyzaltyn not as an owner of the Centerra shares.

[34] Although the Republic directed the State Committee to bring shareholder meetings and shareholder resolutions to transfer funds from Kyrgyzaltyn to the Republic, this was done in the Republic's capacity as sole shareholder of Kyrgyzaltyn.

[35] Kyrgyzaltyn takes the position that the talk of share ownership on the part of the Republic and others is of no legal significance.

[36] Kyrgyzaltyn submits that as a matter of law, there is nothing expropriating the shares from Kyrgyzaltyn nor does the Agreement on New Terms contain a provision that Kyrgyzaltyn is a trustee or agent of the Republic.

[37] Ms. Molodanova, an expert in Kyrgyz law, states that the Republic, as 100% owner of the shares, had the legal right to make decisions regarding the disposition of those shares.

[38] Frank Hebert, general counsel for Centerra, states in his affidavit that he is "aware that Kyrgyzaltyn was intended to be, and is, the beneficial owner and not merely the nominal owner of the shares of Centerra". He claims that although securities law disclosure recognizes that the Republic owns 100% of the shares in Centerra through its 100% control of Kyrgyzaltyn, this is not intended to change legal ownership.

[39] Kyrgyzaltyn takes the position that even if the court determines that the Republic has an interest in the Centerra shares, the Sheriff should not be directed to seize them as the Republic was not properly served with this Application record and the affidavits and other evidence in support thereof.

[40] If the Court finds the Republic does not have an interest in the Centerra shares, the injunction preventing Kyrgyzaltyn from enjoying or disposing of the shares should be lifted.

The Law

A. How to Approach the Main Issue

[41] The court must review the evidence, read the underlying Kyrgyz law, determine credibility and come to its own conclusion as to the “right, property or interest” in the Centerra shares within the meaning of the *Execution Act*. (*Ferranti-Packard Ltd. v. Cushman Rentals Ltd.* (1981), 30 O.R. (2d) 194 (Div. Ct.) aff’d (1981), 31 O.R. (2d) 799 (C.A.) at para 5, *Canada Life Assurance Co. v. Canadian Imperial Bank of Commerce* (1977), 14 O.R. (2d) 777) and *Lister v. McAnulty*, [1944] S.C.R. 317 at 5).

[42] The Agreement on New Terms is governed by the laws of New York. Kyrgyzaltyn accepts that, for the purpose of this Application, New York law is the same as Ontario law. It is also agreed that the basic Canadian notions of corporate law apply in Kyrgyzstan.

B. Kyrgyz Law

[43] Article 169 of the Kyrgyz *Civil Code* provides that, “bodies of state authority...may...acquire and exercise property and individual non-property rights and obligations. ...Other legal entities or citizens may act on behalf of the state.”

[44] Article 222 of the Kyrgyz *Civil Code* provides that there are three essential elements of ownership: the right to possess, enjoy and dispose of property. The right to enjoy is defined as the “right to use natural qualities of the property and to gain profit out of it.” The right to dispose is defined as taking actions regarding the property “at his own discretion...including the right to alienate his own property to the ownership of other persons and to pledge his property and encumber it”.

[45] Decree Number 1141-IV of the Kyrgyz Parliament dated April 30, 2009 provides that the Centerra shares transferred to Kyrgyzaltyn pursuant to the Agreement on New Terms are for “the benefit of the Kyrgyz Republic”.

[46] Article 38 of the Kyrgyz law on Joint Stock Companies (such as Kyrgyzaltyn) provides that decisions about the execution of major transactions, the size and procedure for payment of dividends, and the use of company funds are reserved exclusively for the general meeting of shareholders.

C. Section 18 of the Execution Act

[47] Section 18 of Ontario’s *Execution Act* enables the sheriff to “seize and sell any equitable or other right, property, interest or equity of redemption in or in respect of any goods, chattels or personal property”. Section 14 of the *Act* provides that every seizure and sale of an interest in security “shall include all dividends, distributions, interest and other rights to payment.”

[48] The wording of section 18 is broad. If the Republic has “any” equitable or other interest in the Centerra shares, Sistem can seize that right, property or interest.

[49] The word “interest” in section 18 includes a beneficial interest. In *Banglar Progoti Ltd. v. Ranka Enterprises Inc.*, [2009] O.J. No. 1470 at paras 8 and 27-29 (Ont. S.C.) the court granted a declaration that the debtor had a 100% beneficial interest in real property that could be seized pursuant to a writ of seizure and sale.

[50] In *Nishi v. Rascal Trucking Ltd.*, 2013 SCC 33, Rothstein J. on behalf of the Court, held that, “A purchase money resulting trust arises when a person advances funds to contribute to the purchase price of property, but does not take legal title to that property. Where the person advancing the funds is unrelated to the person taking title, the law presumes that the parties intended that the person who advanced the funds would hold a beneficial interest in the property in proportion to that person’s contribution.”

[51] Similarly, in *Hamilton v. Hamilton*, [1996] 92 O.A.C. 103 at para. 39, the court held that where there is a direct financial contribution to the acquisition of a property, there is a resulting trust in favour of the party that advanced the funds.

[52] In *1454495 Ontario Inc. v. J=Systems Inc.* [2002] O.J. No. 486 at paras. 3 to 4 and 23 to 25, the court held that the debtor’s rights in certain shares constitute an interest that can be seized and sold pursuant to section 18(1) of the *Execution Act*, notwithstanding that another party also has significant rights in the shares. The court held that, “there are residual rights remaining [in the shares] which are subject to seizure and sale under the *Execution Act*.”

D. Analysis and Conclusion

[53] The question to be determined is whether the Republic has legal right to or beneficial interest in the Centerra shares such that they can be seized to satisfy an award payable by the Republic.

As a Matter of Fact, the Republic has an Interest in the Centerra Shares

[54] As a matter of fact, the Centerra shares issued pursuant to the Agreement on New Terms are controlled by the Republic as:

- (a) although the Centerra shares in the Kumtor mine were put in the name of Kyrgyzaltyn JSC pursuant to the Agreement on New Terms, all of the consideration for those shares was provided by the Republic. (The Republic expanded the Kumtor mining concession and implemented a more favourable tax regime for one of Centerra’s operating subsidiaries);
- (b) Kyrgyzaltyn’s management cannot make any decision concerning the Centerra shares without the Republic’s approval. The Republic appoints the Board of Directors, the Audit Committee and management of Kyrgyzaltyn;

- (c) substantially all proceeds from the sale of the shares and payment of dividends are deposited to the Republic. They are included in revenues of the State, not as dividends from corporate net profits; and
- (d) the Republic is able to use the shares as collateral. (Although Kyrgyzaltyn claims it can use the shares as collateral, it has refused to substantiate this claim.)

[55] The parties intended that the Republic would have an interest in the Centerra shares. In the Agreement on New Terms, the preamble provides that Kyrgyzaltyn, “holds shares in Centerra on behalf of the Government. Kyrgyzaltyn, together with the Government, (the “Kyrgyz Side”) are the largest shareholders of Centerra”.

[56] I disagree with the position taken by Kyrgyzaltyn that the statement in the preamble that Kyrgyzaltyn, “holds shares in Centerra on behalf of the Government” has no operative effect. On the contrary, it is clear from the decision in *Disera v. Liberty Development Corp.* [2008] 63 R.P.R. (4th) 197 (O.C.A.) at para. 20, that the recital was considered in arriving at the interpretation of the intentions of the parties to that Agreement.

[57] The “Kyrgyz Side” is defined in the agreement as “the Government of the Republic together with Kyrgyzaltyn”. The “Kyrgyz Side” is referred to often in the Agreement:

- (a) the ninth recital provides that “Centerra and its shareholders, including...the Kyrgyz Side, have a vested interest in seeing the price of Centerra’s shares increase”;
- (b) Section 2.4(d) refers to “Centerra shares held by the “Kyrgyz Side”;
- (c) Section 2.5(c) provides that the “Kyrgyz Side” shall have no restrictions on the transfer or encumbrance of any common shares it holds...”; and
- (d) Section 2.5(d) provides that, “Any common shares held by the Kyrgyz Side shall be subject to the provision of section 3.8 of the 2004 Shareholders Agreement...”

[58] Members of the Republic, Centerra and others stated that the Republic was the owner of the Centerra shares held by Kyrgyzaltyn:

- (a) in a press release dated April 22, 2011, the Prime Minister of the Republic stated that “we have a 33% stake in Centerra”;
- (b) in a memorandum submitted to the International Monetary Fund on June 2013, the Republic described Kyrgyzaltyn as part of its public sector;
- (c) in a central Asia newswire of May 2, 2011, there is reference to a Bishkek news agency reporting that the Deputy Prime Minister stated that the Kyrgyz government is looking to expand its stake in Centerra;

- (d) news reports from the Republic on August 14, 2012 provide that it had received or should shortly receive certificates;
- (e) in the Management's Discussion and Analysis (MD&A) section of the 2009 annual report of Centerra, it refers to the transfer by Cameco of 25.3 million common shares "to Kyrgyzaltyn", "to the Government" and "to the Kyrgyz Government"; and
- (f) in the MD&A in the 2010 annual statement of Centerra, there is reference to "the issuance of common shares to the Government". In an April 24, 2009 press release of Centerra, there is reference to an agreement to issue 18,232,615 common shares of Centerra to the Government and to the agreement of Cameco to transfer 23.5 million shares to the Government.

[59] These statements are evidence that the Republic and Centerra believed the Republic had an interest in the shares.

Kyrgyz Law Provides that the Republic has an Interest in the Centerra Shares

[60] Secondly, the Republic chose to enact special Kyrgyz laws and other rules to confirm the Republic's interest in the Centerra shares and control their use. For example,

- (a) Law number 142 incorporates the Agreement on New Terms into Kyrgyz law. It provides that if there is a conflict between the Agreement on New Terms and other legislation, the Agreement prevails;
- (b) Resolution 253 authorizes Kyrgyzaltyn "to receive and hold shares in the company Centerra Gold Inc., which are owned by the Government of the Kyrgyz Republic";
- (c) Decree Number 1141-IV provides that the 43 million Centerra shares transferred pursuant to the Agreement on New Terms are for "the benefit of the Kyrgyz Republic";
- (d) Order Number 495-R, establishes a commission to "develop proposals for the effective use of the shares of the Kyrgyz side in the company Centerra Gold Inc." The Deputy Minister of State Property was a member of the commission; and
- (e) the Republic directed the State Property Fund to prohibit the sale of Centerra shares without an appropriate government resolution and ordered that proceeds from the sale of Centerra shares be used in the manner determined by the Republic. According to its enabling legislation, the State Property Fund "represents the interests of the state as owner of state property."

[61] In 2006 and 2011 the Republic convened working groups to advise the Republic as to how shares could be effectively used. This occurred outside the framework of the shareholders

meeting and outside the scope of powers given to Joint Stock Companies as set out in Article 38 of the *Civil Code*. Moreover the funds were assigned to the Republic's revenues as "future dividends" to be declared by Kyrgyzaltyn, a move that is not permitted under Kyrgyz law.

The Republic has an Interest in the Centerra Shares

[62] I accept Kyrgyzaltyn's position that it is a large company with other interests. However, insofar as the Centerra shares issued pursuant to the Agreement on New Terms are concerned, Kyrgyzaltyn acted in accordance with instructions of the Republic and had no real control over the use or disposition of those shares independent of the Republic.

[63] However, one party may have a beneficial interest even where another party also has an interest in the property. (See *Nishi v. Rascal Trucking Ltd.*, and *1454495 Ontario Inc. v. J=Systems Inc.* cited above.)

The Republic Had the Opportunity to Participate in this Application

[64] The Republic was party to the arbitration proceeding brought by Sistem. It refused to pay the arbitration award. Thereafter the award was recognized by the Ontario court. Kyrgyzaltyn was added as a party to the Application to enforce the award. This Application is in furtherance of the payment of the arbitration award as in this Application, Sistem seeks to effect seizure of the Centerra shares registered in the name of Kyrgyzaltyn in order to satisfy the arbitration award against the Republic.

[65] In two separate sets of reasons, Brown J. directed that if the Republic intended to participate in this application it would have to file an appearance. The Republic chose not to deliver any responding materials. This Court and the Court of Appeal have both dismissed requests by Kyrgyzaltyn to dismiss proceedings because the Republic had not been properly served. The Republic had ample notice of Sistem's request for relief and the opportunity to respond.

Summary of Conclusions

[66] I find that the shares of Centerra held in the name of Kyrgyzaltyn pursuant to the Agreement on New Terms may be seized to satisfy the arbitration award against the Republic.

[67] The Republic owns all of the shares in Kyrgyzaltyn and Kyrgyzaltyn owns the Centerra shares in question.

[68] The Republic has a beneficial interest in the shares because it gave all of the consideration for the issuance of these shares, the terms of the Agreement refer to the "Kyrgyz Side" (which is defined to include the Republic and Kyrgyzaltyn), and the Republic has actual control over the Centerra shares. Special laws were enacted to effect that control pursuant to Kyrgyz law.

[69] Kyrgyzaltyn has the right to manage the asset at the direction of the Republic.

[70] The fact that Kyrgyzaltyn may be a large company with other interests is of no consequence as the question is not whether Kyrgyzaltyn has other interests separate and apart from those of the Republic, but rather whether these Centerra shares in the name of Kyrgyzaltyn can be seized to satisfy the arbitration award.

[71] A declaration is granted that the Kyrgyz Republic has an equitable interest in the Centerra shares issued in the name of Kyrgyzaltyn pursuant to the Agreement on New Terms.

[72] Moreover, in accordance with Section 18 of the *Execution Act*, the Sheriff shall seize the Centerra shares as the Republic has “an equitable or other interest” in them. In accordance with Section 14 of the Act, that interest includes “all dividends, distributions, interest and other rights to payment.”

[73] The Application is granted. The Applicant is entitled to its party and party costs. If the parties cannot agree on the quantum of costs payable, they may provide me with brief written submissions and a Bill of Costs within 14 days.

Thorburn J.

Date: April 15, 2014