Journal
of the Russian Academy of Legal Sciences

RUSSIAN LAW:
THEORY AND PRACTICE

Issue 1, 2017

Published twice yearly
under the editorship of V.S. Belykh

RUSSIAN LAW: THEORY AND PRACTICE

No. 1 • 2017

Distribution Section:

Tel/fax: (+7)(495) 617 1888

Index:

"Agency for distribution of foreign publications" — 91885.

1000 copies/

Contact Us :
Editorial Council:

(+7)(343) 245 9398;
e-mail: belykhvs@mail.ru

Editorial Board:
(+7)(495) 953 9108;

e-mail: avtor@lawinfo.ru

Publisher's Address for Correspondence:

RAUN, Kosmodamianskaya Quay, 26/55 Building 7, Moscow 125057, Russia
e-mail: avtor@lawinfo.ru
(+7)(495) 951 6069 (Russia)

The Russian Law: Theory and Practice is registered with the Russian Ministry of Press, TV Broadcasting and Mass Communications. Regn. 77–1578, Jan. 28, 2000. Published twice yearly.

Authors: When sending a manuscript to Publishing House "Jurist", the author may express nonconsent to the publication of an English-language version.

TABLE OF CONTENTS

ENVIRONMENTAL LAW

COMPARATIVE LAW

ARBITRAL LEGISLATION

DEAR READERS!

The year of 2017 has come. In the Oriental Calendar, this is the year of the Fire Rooster, which promises to be more successful and eventful. According to the oriental calendar, the rooster is the most colorful, sociable, and exquisite. It likes to attract attention and adores basking into compliments. The most important during this year is to accept any changes in your life philosophically. As our Prime Minister said, "There is no money but you take care!"

In real life, this year will not be easy for many countries in the world, including Russia, especially in economy. The economic situation in Russia has worsened after the U.S. and European states imposed various sanctions, including financial ones. The sharp decline of oil prices is the most painful for the Russian economy. Russia needs oil at a price not lower than USD 100 per barrel to balance its budget. Currently, one barrel of oil costs USD 56, though some analysts forecast USD 20-25 per barrel of oil in the short term. In short, we shall see what we shall see! Russia has passed through many disasters, wars, and revolutions. We will also come through this difficult situation!

2017 is also rich in memorable and historic events. For example, 5 February marked the 295th anniversary of the adoption of the Statute on the Succession to the throne, the 18th of February is the day when Peter III issued a Manifesto "granting freedoms and liberties to the Russian nobles" (255th anniversary), 18 April is the day of Ice Battle (775th anniversary), 19 May is the Pioneers Organization Day (95th anniversary), 8 September is the day of the 205th anniversary of the Battle of Borodino, 2 November is the 100th anniversary of the" Declaration of the Rights of the Peoples of Russia", 7 November is the 100th anniversary of the Great October Socialist Revolution.

2017 is rich in memorable days connected with City Days in Russia. 4 June is the City Day of Togliatti (280th anniversary), 27 August is the City Day of Rostov Veliky (1155th anniversary) and Kostroma (865th anniversary), 3 September is the City Day of Moscow (870th anniversary), 17 September is the City Day of Stavropol (240th anniversary)

On 8 — 9 June 2017, the XI Session of the Euro-Asian Law Congress "Legal Issues of the Modern World Order's Perfection" will be held in Yekaterinburg. The work of the session will be organized in the format of plenary meetings, meetings of expert groups and round-table discussions.

On 23 July, the founder of the Business (at present — Entrepreneurial) Law Subdepartment, the Faculty of Legal Service in the National Economy System (at present — the Institute of Law and Business of the Ural State Law University) professor, Doctor of Law, Honored Lawyer of the Russian Federation Vasiliy

Stepanovich Yakushev would be 95 years. Therefore, on 19-20 October 2017, the first Yakushev's readings will be held in the memory of this remarkable and high-skilled professional.

Dear readers, take care of yourselves and your relatives. Love your neighbors as yourselves. Not to lose yourself in this raging world is very important.

We are open to cooperation and ready to publish articles, information and advertisement in our "Russian Law: Theory and Practice" journal.

Editor-in-Chief, Doctor of Law, Professor **V.S. Belykh**

THE CONSTITUTIONAL FRAMEWORK OF NATIONAL INTERESTS ENSURANCE IN THE UNITED STATES: A RUSSIAN COMPARISON

Robert Allen Sedler
Distinguished Professor of Law
Wayne State University
Detroit, Michigan, U.S.A.

Abstract
This article discusses the constitutional framework of national interests ensurance in the United States under the 18th century American Constitution and makes some comparisons with the constitutional framework of national interests ensurance in Russia under the 20th century Constitution of the Russian Federation. The 18th century American Constitution reflects 18th century notions of checks and balances and separation of powers between the legislative, executive and judicial branches. There are specific powers allocated to each branch and some interactions between the branches. This applies to national interests ensurance as well. So, while Congress has the power to declare war, the President is the Commander-in-Chief of the Armed Forces, and there is some tension between these powers when the President takes action to commit the United States to armed conflict. So too, while the President has the power to enter into treaties on behalf of the United States, every treaty must be approved by a two-thirds vote of the Senate. The one exclusive power over foreign affairs that the American Constitution gives to the President is the power to recognize foreign governments, and Congress cannot interfere with that power.

Keywords: 18th century American Constitution, separation of powers, international law, Presidential disapproval of legislation, Congressional grant of broad power to President to administer and enforce legislation, Russian President and Russian foreign policy, "political question", American President and recognition of foreign governments, Congressional power over foreign affairs and conflict with Presidential power, President and Congress and armed conflict, executive agreements, Cuba and Cuban trade embargo, Iranian nuclear agreement, American sanctions, Russia, and Ukraine.

Under the Russian Constitution, the President directs the foreign policy of the Russian Federation, enters into international treaties on behalf of the Russian

Federation, and recognizes foreign governments. The President is the Commander-in-Chief of the Armed Forces, and in the event of aggression or the threat of aggression, the President can declare martial law and can introduce a state of emergency. The President decides on issues of citizenship and can grant asylum. In the area of foreign affairs, the General Assembly has only specific and limited powers, such as the Council of Federation having to approve using the Armed Forces of the Russian Federation outside the territory of the Russian Federation.

However, while the American Constitution does not give the American President the same degree of formal power over foreign affairs and thus over national interests ensurance as the Russian Constitution gives to the Russian President, the way that the constitutional framework of national interests ensurance operates in practice in the United States gives the President the primary responsibility for national interests ensurance, and in this respect, the American President has almost as much power as the Russian President.

There are *five reasons* why this is so. **One:** the American President has the same power as the Russian President to disapprove legislation, and so the American President can disapprove legislation purporting to limit Presidential power in the area of foreign affairs. This means that although the President cannot act contrary to a law of Congress, the only laws of Congress that could restrict Presidential power are laws that were enacted at an earlier time. **Two:** since the Constitution vests the entire executive power in the President and does not provide for a separate "government" to administer the laws, Congress can and must grant broad discretion to the President to administer and enforce legislation that Congress has enacted, and Congressional authorization in the area of foreign affairs will be broadly construed. **Three:** the power to recognize foreign governments belongs exclusively to the President, and it is a very important power. **Four:** under the "political question" doctrine, the federal courts will not entertain direct suits between the President and Congress over questions of Presidential and Congressional power, so most Presidential actions, including involving the nation in armed conflict, will not be reviewed by the courts. While there is a common understanding between American Presidents and Congress as to when Congressional authorization for military action is or is not required, it is entirely up to the President whether or not to seek Congressional authorization in a particular case. **Five:** the President has the power to enter into executive agreements with foreign nations, thereby avoiding the requirement of the Senate approval of a treaty by a two-thirds vote and the overwhelming majority of agreements between the United States and foreign nations take the form of executive agreements.

The article also discusses recent examples of the constitutional framework of national interests ensurance in the United States: the President's recognition of Cuba

and the Cuban trade embargo; the Iranian nuclear agreement; and the imposition of American sanctions against Russia over "the situation in Ukraine".

I. Introduction

In this article I will discuss the constitutional framework of national interests ensurance in the United States under the 18th century American Constitution and make some comparisons with the constitutional framework of national interests ensurance in Russia under the 20th century Constitution of the Russian Federation[1]. I will begin by discussing Congressional and Presidential Power under the American Constitution. I will then discuss the constitutional framework of power over foreign affairs under the American Constitution and the constitutional framework under the Russian Constitution. Following that, I will discuss the roles of the American President and Congress in involving the nation in armed conflict and the American President's power to enter into executive agreements. I will then discuss three recent examples of the constitutional framework of national interests ensurance: (1) the President's recognition of Cuba and the Cuban trade embargo; (2) the Iranian Nuclear Agreement; and (3) the imposition of American sanctions against Russia over "the situation in Ukraine". I will conclude with some brief observations about the constitutional framework of national interest ensurance in the United States at the present time.

II. Congressional and Presidential Power under the 18th Century American Constitution

Perhaps, the best way to understand the constitutional framework of national interests ensurance in the United States is to compare the 18th century Constitution of the United States (hereafter "the American Constitution"), adopted in 1787, with the 20th century Constitution of the Russian Federation (hereafter "the Russian Constitution"), adopted in 1993. In 1787, the United States had limited involvement with the international world. The main involvement would be with Great Britain and its Canadian colony on the northern border, and the major foreign policy concern of the Framers of the Constitution would be a war with Great Britain, which indeed occurred in 1812. Since international law was not very developed in 1787, it is not surprising that international law was not a part of the American Constitution. International law is not only a part of the Russian Constitution, but under the Russian Constitution, it is a superseding norm. The Russian Constitution

[1] This article is an expanded version of a paper that I presented on June 18, 2015, at the 9th session of the Euro-Asian Juridical Congress held at the Ural State Law University, Yekaterinburg, Russia. The subject of the Congress was "Law and National Interests in Modern Geopolitics". At that time, I was honored by being named an Honorary Professor of the Ural State Law University.

provides that universally recognized principles and norms of international law as well as international agreements are an integral part of the legal system, and further that if an international agreement of the Russian Federation establishes rules, which differ from those stipulated by law, then the rules of the international agreement shall be applied[2].

The result is just the opposite under the American Constitution. A treaty is not superior to a law of Congress, and if an earlier treaty is inconsistent with a law of Congress, the law of Congress controls, even though this puts the United States in violation of its obligations under international law[3].

The primary purpose of the American Constitution was to establish a national government that would share power over domestic matters with the thirteen states that had emerged from the 1776 Declaration of Independence in and the successful War of the American Revolution while in American constitutional theory, the newly independent states succeeded to the sovereignty formerly exercised by the British Crown over domestic matters[4], the states did not succeed to the sovereignty formerly exercised by the British Crown over foreign affairs. Rather that aspect of sovereignty devolved upon "the Union of States" that was waging the Revolutionary War and that successfully concluded the peace with Great Britain. Since sovereignty over foreign affairs never belonged to the states, it is deemed in American constitutional theory to be inherent in the national government that was subsequently established by the Constitution. Thus, the national government has the inherent power to conduct the

---

[2] Russian Constitution, Art.15, sec.4. However, if the Constitutional Court finds that a treaty violates the Russian Constitution, the treaty is inoperative. Russian Constitution, Art.125, sec.6.

[3] Chae Chin Ping v. United States, 130 U.S. 581 (1889). This result is deemed to follow from the language of the Supremacy Clause, Art.VI, sec.2, which refers to "[t]he Constitution and the Laws of the United States which shall be made in pursuance thereof and all Treaties made, or which shall be made, under the Authority of the United States". Since this provision treats laws and treaties equally, the Court held that in the event of a conflict, a later law would supersede an earlier treaty.

[4] In American constitutional theory, upon Independence, all of the 13 former colonies became "free and independent states", which meant that they succeeded to the sovereignty over domestic matters formerly exercised by the British Crown. Since each state obtained its sovereignty by way of succession upon declaring Independence from Great Britain, it was not necessary to have a national Constitution to give the states power. State sovereignty is thus "given" in the American constitutional system. As a part of this sovereignty, each state has its own system of laws and its own courts and possesses the general regulatory and taxation power. In the constitutional sense then, American states are "independent sovereigns" and cannot be considered "subdivisions" of the national state. See the discussion in Robert A. Sedler CONSTITUTIONAL LAW IN THE UNITED STATES 91 (2nd ed. Wolters Kluwer 2014) (hereafter "Sedler, CONSTITUTIONAL LAW"). In contrast, under the Russian Constitution, the constituent entities of federation established by the Russian Constitution, Art.5, are not sovereign and can only exercise certain powers jointly with the National Government and other powers that are not exercised by the National Government (Russian Constitution, Art.72, 73).

foreign affairs of the Nation, and as regards the constitutional allocation of federal and state power, the foreign affairs power is an exclusive federal power[5].

While the Framers of the Constitution recognized the need to establish a federal government, they were "men of the states" and were concerned that the newly established federal government would attempt to usurp the power of the states. The Constitution that they adopted thus reflects the 18th century notions of checks and balances and separation of powers. There is a legislative branch, Congress, consisting of a House of Representatives and a Senate[6], an executive branch in which the entire executive power is lodged in the President of the United States[7], and a judicial branch, with specific powers allocated to each branch and some interactions between the branches. **So,** while Congress has the power to declare war[8], the President is the Commander-in-Chief of the Armed Forces[9], and as we will see, there is some tension between these powers when the President takes action to commit the United States to armed conflict. So too, while the President has the power to enter into treaties on behalf of the United States, every treaty must be approved by a two-thirds vote of the Senate.

As part of the system of checks and balances, the Framers made the President an integral part of the legislative process. In order for a bill to be enacted into law, it must be passed by both Houses of Congress and then presented to the President for

[5] *See* Sedler, CONSTITUTIONAL LAW IN THE UNITED STATES 275. The states are prohibited from entering into a treaty or alliance with a foreign nation, but may, with the consent of Congress, enter into an agreement or compact with a foreign nation. Pursuant to U.S. Constitution Art.I, sec.10, cl.3., American states, with the consent of Congress, have entered into agreements with Canada and Canadian provinces and with Mexico.

[6] At the Constitutional Convention of 1787, the large states wanted representation in Congress to be based on population while the small states contended that each of the sovereign states should have equal representation in Congress. The "Great Compromise" was to establish two equal branches, a House of Representatives based solely on population, with each state having at least one Representative, and a Senate with two Senators from each state regardless of population. So, a small state like Wyoming, which has only one Representative in the House, has two Senators, while the largest state, California, which has 53 Representatives in the House, has the same two Senators in the Senate. See Sedler, CONSTITUTIONAL LAW IN THE UNITED STATES 36.
Under the Russian Constitution, the Federal Assembly, Parliament, consists of the State Duma, with elected Deputies, and the Council of Federation, with two Representatives from each constituent unit of the federation, with each body having specified powers within its jurisdiction. Russian Constitution, Art.102, 103.

[7] There is no American equivalent of a "government", as provided in Chapter 6 of the Russian Constitution. The American President exercises the entire executive power and appoints the heads of governmental departments, such as the State Department, with the approval of the Senate. The President may remove a head of a governmental department or any official of the executive branch, at his sole discretion notwithstanding that the appointment of that official had been approved by the Senate. Myers v. United States, 272 U.S. 52 (1926).

[8] American Constitution, Art.1, sec.8, cl.11.

[9] American Constitution, Art.II, sec.1

his approval. If the President disapproves or "vetoes" the bill, his veto can only be overcome by a two-thirds vote of both Houses of Congress[10]. In practice, it is very rare for Congress to be able to muster a two-thirds vote in both Houses, so almost invariably the President's veto prevents the bill from becoming law[11].

Since the American Constitution vests the entire executive power in the President and does not provide for a separate "government" to administer the laws, it specifically provides that the President "shall take care that the Laws be faithfully executed"[12]. In light of this provision, Congress can and, as a practical matter, must grant broad discretion to the President to administer and enforce the provisions of legislation that Congress has enacted. In this regard, legislation containing grants of authority to the President will be broadly construed, so as to avoid any potential conflict between Congressional and Presidential power and a resulting constitutional separation of powers question. Particularly is this so when the legislative authorization in question relates to foreign affairs[13].

III. The Constitutional Framework of Power over Foreign Affairs under the American Constitution and under the Russian Constitution

As it has been stated earlier, the 18th century American Constitution reflects the 18th century notions of checks and balances and separation of powers. Although the primary concern of the Framers related to the exercise of federal power over domestic matters, these 18th century notions of checks and balances also carried over to foreign affairs. This is the crucial difference between the constitutional framework of national interests ensurance under the American Constitution and under the Russian

[10] American Constitution, Art.I, sec.7

[11] The President must approve or disapprove a bill in its entirety. Art.I, sec.7 does not permit Congress to give the President a "line item veto," by which he can disapprove only a part of a bill, such as by canceling certain spending measures that he had previously signed into law. Clinton v. New York, 524 U.S. 417 (1998).
Interestingly enough, the Russian Constitution contains an identical provision. If the President disapproves a federal law, his disapproval can be overridden only by a two-thirds vote of the total number of members of the Council of Federation and a two-thirds vote of the total number of deputies of the State Duma. Russian Constitution, Art.107.

[12] American Constitution, Art.II, sec.3.

[13] See *Dames & Moore v. Regan,* 453 U.S. 654 (1981), where the Court found Congressional authorization for the President's entering into a claims settlement agreement with Iran as part of the conditions for the release of American hostages that were detained in Iran following the storming of the American Embassy in the wake of the 1979 Iranian revolution. The settlement agreement required the United States to terminate all suits brought against Iran in American courts, to nullify existing attachments obtained in connection with such suits, to prohibit future litigation against Iran, and to provide for the resolution of all claims against Iran through binding arbitration before an Iran-United States Claims tribunal. The Supreme Court found authorization to nullify the attachments in specific legislation, and found that Congress had long recognized the President's authority to settle international claims of American nationals by executive agreement.

constitution. The Russian Constitution gives the President very extensive powers over foreign affairs, with only a limited role for the General Assembly. The American Constitution, by contrast, gives both the President and Congress broad powers over foreign affairs. As we will see shortly, the President has the exclusive power to recognize foreign governments. The President also has powers over foreign affairs as the Commander-in-Chief of the Armed Forces and as the representative of the nation in foreign affairs[14]. But Congress can also use the legislative power to regulate foreign affairs, and, as we will see, if there is a conflict between the exercise of power by the President and the exercise of power by Congress over a matter that comes within the powers of Congress, the law of Congress controls.

Under the Russian Constitution, the President directs the foreign policy of the Russian Federation, enters into international treaties on behalf of the Russian Federation, and recognizes foreign governments[15]. The President is the Commander-in-Chief of the Armed Forces, and, in the event of aggression or the threat of aggression, can declare martial law and can introduce a state of emergency[16]. **Finally,** the President decides on issues of citizenship and can grant asylum[17]. In the area of foreign affairs, the General Assembly has only specific and limited powers. The Council of Federation must approve using the Armed Forces of the Russian Federation outside the territory of the Russian Federation, and must approve the President's edicts on the introduction of martial law and the introduction of a state of emergency[18]. And while the General Assembly has the power to enact federal laws relating to ratification and denunciation of international treaties and war and peace[19], if such laws were passed by the General Assembly, they would be subject to the President's veto and would be very difficult to enact over that veto.

There is another very significant structural difference between the 18th century American Constitution and the modern Russian Constitution. Under the Russian Constitution, there is a separate Constitutional Court, with extensive jurisdiction to

[14] See *United States v. Curtiss-Wright Export Corporation*, 299 U.S. 304 (1936), where the Court made it clear that the President as representative of the nation does not need Congressional authorization to take action in the area of foreign affairs. However, where Congress does enact legislation authorizing such action on the part of the President, the President must act in accordance with the legislative authorization.

[15] Russian Constitution, Art.86.

[16] Russian Constitution, Art.87-88.

[17] Russian Constitution, Art.89.

[18] Russian Constitution, Art.102(1)(b)(c)(d). During the conflict in Crimea between pro-Russians and pro-Ukranians, President Putin sought the approval of the Council of Federation to send Russian Armed Forces into Crimea "until the normalization of the socio-political situation in the Crimea", and that approval was quickly granted. See Kathy Lally, Will Englund, and William Booth, "Russian Parliament Approves Use of Troops in Ukraine", The Washington Post, March 1, 2014.

[19] Russian Constitution, Art.106(d)(e)(f).

decide constitutional questions at the request of any of the components of the Russian Federation, such as in a dispute between the President and the Federal Assembly, over which component has the power to take a particular action[20].

In the United States, in contrast, there is no separate constitutional court. While the Supreme Court and the lower federal courts have the power to decide constitutional questions relating to separation of powers, the Supreme Court has held that the federal courts may entertain constitutional challenges only in suits brought by individuals or institutions that have suffered a clearly identified injury from the action alleged to be unconstitutional[21]. The Court will not entertain a suit by a Member of Congress or Congress itself against the President alleging that the President did not have the authority to take the action that he did, and will instead require the branches to resolve this "political question" among themselves as equals[22].

The only exclusive power over foreign affairs that the American Constitution gives to the President is the power to recognize foreign governments, and Congress cannot interfere with that power[23]. Very recently, the Supreme Court held unconstitutional a law of Congress that the Court saw as interfering with the President's recognition power. The United States, like the Russian Federation and many other nations, does not recognize Israel's sovereignty over Jerusalem, which Israel annexed in 1967 following its capture of East Jerusalem during the 6-day war, and like the Russian Federation, the United States maintains its embassy in Tel-Aviv rather than in Jerusalem. The American Secretary of the State issues passports for children of American citizens born abroad, and when a child is born in Jerusalem, the passport lists the place of birth simply as "Jerusalem" rather than as "Jerusalem, Israel". If the child were born in Moscow, the passport would list the place of birth as "Moscow, Russian Federation". Congress had enacted a law requiring the President to list the place of birth for a child born in Jerusalem as "Jerusalem, Israel", the Supreme Court held that this law intruded on the President's exclusive power of recognition, since American Presidents have refused to recognize Israeli sovereignty over Jerusalem, and so was unconstitutional[24].

In this connection, it may be noted that the American President can refuse to recognize a foreign government, even though that government is entitled to recognition under international law, since, as it has been pointed out earlier,

[20] Russian Constitution, Art.125, sec.2-5.

[21] As in the cases discussed in notes 24, 26, and 27, *infra*.

[22] See *Goldwater v. Carter,* 444 U.S. 996 (1979). *See generally* the discussion of the "political question" doctrine in Sedler, AMERICAN CONSTITUTIONAL LAW 77-81.

[23] The exclusive nature of this power is based on the "reception clause", Art.II, sec.3, "[H]e shall receive Ambassadors and other Public Ministers..."

[24] Zivotofsky v. Kerry, 135 S.Ct. 2076 (2015).

international law is not a part of the American Constitution[25]. Thus, American Presidents refused to recognize the communist government of the former Soviet Union until 1933, although that government came to power and was entitled to recognition no later than November, 1917. Likewise, American Presidents refused to recognize the communist government of China until 1978, although it came to power in 1949. In 1961, following American conflict with the Castro government in Cuba, the President broke off diplomatic relations with Cuba. President Obama recently acted to restore diplomatic relations with Cuba, and both nations are now in the process of doing so.

However, apart from recognizing foreign governments, as stated previously, both Congress and the President have power over foreign affairs, and where Congress enacts legislation that is within Congressional power, the President cannot act contrary to the law of Congress. This is so even when the President is acting under his power as the Commander-in-Chief of the Armed Forces. For example, when President George W. Bush set up military commissions to try "unlawful enemy combatants" for violations of the laws of war, that action was unconstitutional, because the procedures for trials before military commissions provided for in the President's order were inconsistent with the procedures contained in a law of Congress providing for trials before military commissions[26]. Similarly, when there was the danger of a nationwide steel strike during the Korean War, President Truman issued a Presidential order directing the Secretary of Commerce to take possession of most of the nation's steel mills. The President justified the order on the basis of his power as the Commander-in-Chief, contending that continued steel production was necessary to the war effort. Not only was the use of this seizure technique not authorized by any federal law, but to the contrary, a federal labor law specifically provided a process for dealing with a nationwide labor stoppage. The Court held that the Presidential order was unconstitutional, since the matter in issue came within the legislative power of Congress, and the President could not rely on his power as the Commander-in-Chief to act contrary to a law of Congress[27]. In both of these cases,

[25] Art.15(4) of the Russian Constitution states that uniform recognized principles and norms of international law should be a part of the legal system of the Russian Federation. But that provision does not say that these principles should determine whether the Russian President must recognize a foreign government, and it may be assumed that the President is not constrained in his decision whether or not to recognize a foreign government.

[26] *Hamdan v. Rumsfeld,* 548 U.S. 557 (2006).

[27] *Youngstown Sheet & Tube Co. v. Sawyer,* 343 U.S. 579 (1952). See also *Medellin v. Texas*, 552 U.S. 491 (2008). The International Court of Justice had rendered a decision that the United States had violated the Vienna Convention on Consular Relations, which requires law enforcement officials to inform arrested foreign nationals of their right to notify their consulate of their detention. The State of Texas had not done this with respect to a Mexican national who had been arrested and convicted in Texas. President George W. Bush sent a memorandum to the Texas state courts advising them that

the relevant laws had been enacted at an earlier time and so were not subject to a current Presidential veto. As a practical matter, if Congress disagrees with a foreign policy action currently being taken by an American President, such as the multilateral agreement to restrict Iran's ability to develop a nuclear weapon, as we will see, Congress' effort to enact a law prohibiting that action likely would be stopped by a Presidential veto.

While no two constitutional regimes are identical, I want to compare the results in these two cases with the results that I think would obtain under the Russian Constitution in the unlikely event that these hypothetical cases would take place in Russia[28]. The *first case*, involving the American President's executive order establishing military commissions, would not arise in Russia, since under the Russian Constitution, only the President as commander-in-chief would have the authority to establish military commissions. The *second case*, involving the American President's seizure of the steel mills during a time of war, would seem capable of arising in Russia if the General Assembly had enacted a law governing nationwide strikes and the Russian President ordered the seizure of the steel mills at a time when Russia was at war. Under the Russian Constitution, edicts and regulations of the Russian President cannot conflict with federal laws[29]. But the Russian Constitution, unlike the American Constitution[30], authorizes the President in the event of aggression or threat of aggression against the Federation to declare martial law and in certain circumstances, to declare a state of emergency[31]. If the federal constitutional law applicable to martial law or state of emergency so provides, the Russian President might be able to take such action without regard to the contrary legislation. Again, this hypothetical case is unlikely to arise in Russia.

IV. The Roles of the American President and the Congress in Involving the Nation in Armed Conflict

As it has been emphasized, the 18th century American Constitution embodies the principle of checks and balances, and this principle extends to the roles of the

they must adhere to the decision of the International Court of Justice. Since the Vienna Convention is not a self-executing treaty, it requires implementing Congressional legislation, and none had been enacted. Because this was so, the Supreme Court held that the decision of the International Court of Justice was not binding domestic law, and the President did not have the power under Art.II to order the Texas courts to reopen the state court criminal judgment in this case.

28 Not being a Russian constitutional commentator, I do so with a high degree of caution.

29 Russian Constitution, Art.90(3).

30 There is no provision for martial law or for a state of emergency under the American Constitution. No matter what happens, such as the attacks on 9/11, the federal government can only take those actions authorized by existing laws or by the enactment of new laws.

31 Russian Constitution, Art.87-88. The President's declaration of martial law or a state of emergency must be approved by the Council of Federation. Russian Constitution, Art.102(1)(b) (c).

President and Congress in involving the nation in armed conflict. While Congress has the power to declare war[32], the President is the Commander-in-Chief of the Armed Forces[33], and there is some tension between these powers when the President takes action to commit the United States to armed conflict. While at the time of the adoption of the American Constitution in 1787, the only likely possibility of a war was with England, those provisions remained unchanged as the United States has become a world power and very frequently engages in armed conflict in many parts of the world. The Russian Constitution, perhaps reflecting the history of foreign invasions of Russia, gives the President the power and duty to repel foreign aggression, including the power to declare martial law and a state of emergency[34]. It is also fair to say that the Russian Constitution does not contemplate the widespread involvement of the Russian Federation in foreign wars. While the Russian President, in the exercise of his power to direct the foreign policy of the Federation and his power as Commander-in-Chief, could propose to commit the Federation to foreign wars, the Russian Constitution specifically requires that the Council of Federation approve the use of the Armed Forces of the Russian Federation outside the territory of the Russian Federation[35].

The United States, by contrast, has long engaged in armed conflict throughout the world, both when it was the victim of foreign aggression in World War II[36] and more recently when, for one reason or another, it has become involved in armed conflict in many different parts of the world. As stated previously, there is some tension between Congress' power to declare war and the President's power as Commander-in-Chief when the President takes action to commit the United States to armed conflict. However, again as stated previously, the determination of which branch has the constitutional power to act in a particular situation is considered by the Supreme Court to be a "political question" that will not be determined in a suit between the branches themselves. As a result, the law relating to the exercise of military power by the President and by Congress has not been definitively resolved by the Supreme Court. But there has been what may be called a common understanding between American Presidents and Congress over a long period of time as to when Congressional authorization is and is not required. That common understanding is usually, though not always, followed by the President when deciding whether or not to take military action.

---

[32] American Constitution, Art. 1, sec. 8, cl.11.

[33] American Constitution, Art. II, sec.1

[34] Russian Constitution, Art.87-88.

[35] Russian Constitution, Art.102 (1)(d). The Council did so when the President proposed to send Russian troops to Crimea. *See* note 18, *supra*.

[36] This is the American term for what in Russia is called the Great Patriotic War.

We begin by noting that there is no provision in the American Constitution that restricts in any way military intervention on the part of the United States, and as far as the Constitution is concerned, of course, it is completely irrelevant that a particular military intervention by the United States may violate international law[37]. In the United States then the only constitutional question regarding war and military intervention relates to separation of powers and when Congressional authorization is or is not required for military action.

The separation of powers question is avoided, of course, whenever the particular intervention is authorized by Congress. Congress may authorize military intervention by a formal declaration of war, as it did against the Axis powers in World War II following the bombing of Pearl Harbor by Japan, or by a concurrent resolution granting authority to the President to take military action, as Congress did prior to the Gulf War against Iraq in 1991. Congress also adopted concurrent resolutions in 2001, authorizing President George W. Bush to initiate military action against the Taliban regime in Afghanistan, and in 2003, authorizing the President to initiate military action against the Saddam Hussein regime in Iraq[38]. While Congress did not specifically authorize the President to take military action in Vietnam and to continue military action when it evolved into a full-scale war between the United States and its South Vietnam allies on one side and the Viet Cong and North Vietnam, on the other side, President Johnson claimed that the 1964 Gulf of Tonkin resolution authorizing military action following an incident in the Gulf of Tonkin, provided sufficient authorization for full-scale American military involvement in Vietnam.

It has been assumed as a part of the common understanding that Congressional authorization is not required when the President commits the United States to military intervention that is specifically called for under the nation's treaty obligations: the ratification of the treaty by the Senate satisfies the requirement of Congressional authorization for the military action taken by the President pursuant to the treaty. American military involvement in Korea in 1950, following an invasion of South Korea by North Korea, was pursuant to a resolution of the United Nations Security Council, and the American troops served as part of a United Nations force that was led by an American commander. Since this was so, President Truman did not seek Congressional authorization for the American military involvement in Korea. In more recent times, American military involvement in Bosnia and Kosovo was part of a North Atlantic Treaty (NATO) force, and President Clinton did not seek

[37] For example, in the 2003 invasion of Iraq by the United States, President George W. Bush initiated the action despite the failure of the United Nations Security Council to adopt a resolution specifically authorizing the use of military force against Iraq in order to secure its compliance with prior Security Council resolutions.

[38] President Eisenhower also obtained Congressional authorization by joint resolution prior to sending American troops into the Formosan Straits in 1955 and into Lebanon in 1958.

Congressional authorization for either involvement. For the same reason, President Obama did not seek Congressional authorization for American participation in the NATO bombing of Libya, designed to overthrow the Gaddafi regime.

It is also a part of the common understanding that the President as Commander-in-Chief can act without Congressional authorization in "emergency-type" or "short-term temporary" situations, such as an armed attack on the United States or a threat to American citizens or property in a foreign country. This basis for American military intervention was relied on by President Reagan in 1983, when he sent American troops into Grenada, an island country in the Caribbean, claiming that the safety of Americans attending a medical school in Grenada was in danger due to actions of a newly installed government that was favorable to Cuba. The Americans were evacuated from Grenada and the pro-Cuban government was overthrown in the process. This basis for military intervention would also support the bombing of Libya by President Reagan in 1986 in reprisal for a terrorist attack in Germany in which American servicepersons were killed, and the sending of American troops into Panama by President George H.W. Bush in 1990, to capture a Panamanian general and former President and bring him to trial in the United States for an alleged violation of American drug laws.

Finally, it has also been assumed as a part of the common understanding that Congress can preempt military action by the President through the use of its appropriations power under Article I, sec.8, to specifically prohibit the use of appropriated funds for a particular military action or for any other purpose. No President has ever asserted the authority to expend appropriated funds contrary to a restriction specifically imposed on the use of such funds by Congress. For example, for a period of time Congress specifically prohibited the use of appropriated funds to provide assistance to an anti-government resistance group in Nicaragua, and although President Reagan wanted to fund the resistance group, he complied with the restriction. Congress imposed this restriction in an appropriations bill, which the President must sign or veto in its entirety, and so may be faced with the difficult choice of approving an appropriations bill in its entirety or vetoing the bill and engaging in a "test of wills" with the Congress over military appropriations.

In the War Powers Resolution of 1973, enacted over President Nixon's veto, Congress attempted to exercise a degree of control over the President's commitment of American troops to a foreign military intervention by requiring the President to submit a report to Congress within 48 hours of the President's taking such action. The submission of the report triggers a 60-day period, during which the troops must be removed unless Congress has declared war or has specifically authorized the use of military force, or has extended the period. Congress can also direct the removal of the troops within the 60-day period by means of a concurrent resolution. American

Presidents have sometimes complied with the War Powers Resolution and sometimes have not.

There are a number of constitutional problems with the War Powers Resolution, including the fact that it directly interferes with the President's power as Commander-in-Chief to respond to "emergency-type" situations, discussed above, and that it amounts to an impermissible "legislative veto" insofar as it allows Congress to overturn Presidential action by means of a concurrent resolution instead of by means of legislation[39]. The Resolution stands on stronger constitutional footing insofar as it declares that the intervention must comes to an end after 60 days unless Congress has declared war or authorized the military action. However, if the President does not end the intervention after the 60-day period, the only "constitutional remedy", so to speak, is for Congress to enact legislation prohibiting the use of appropriated funds to support the military intervention, and the President can veto that legislation. Any effort by Congress to challenge the President's action in court will fail, because the courts will invoke the political question doctrine and will refuse to decide whether the President is constitutionally required to remove the troops[40].

V. The American President's Power to Enter into Executive Agreements

The President also has the power to enter into executive agreements with foreign nations. Under the Constitution, it was contemplated that an agreement between the United States and a foreign nation would take the form of a treaty, which must be approved by a two-thirds vote of the Senate. However, for many, many years, the practice has grown up by which the President can avoid the need for Senate approval of a treaty by instead entering into an executive agreement with one or more foreign nations. The authority of the President to enter into executive agreements is based on his power under Article II as the representative of the nation in foreign affairs. The overwhelming majority of agreements between the United States and foreign nations take the form of executive agreements, and the Supreme Court has upheld the validity of executive agreements entered into by the President with a foreign nation or nations on behalf of the United States[41].

[39] Under Art.I, sec. 7, Congress can only override a Presidential action by means of legislation, which includes the power of the President to veto the legislation. See *Immigration and Naturalization Service v. Chandra,* 462 U.S. 919 (1983).

[40] The matter of the roles of the President and the Congress in involving the nation in armed conflict is discussed in Sedler, AMERICAN CONSTITUTONAL LAW at 268-272.

[41] The question has arisen in the context of the Supreme Court holding that an executive agreement, like a treaty, overrides inconsistent state law under the Supremacy Clause, U.S. Const., Art. VI, sec. 2. See e.g., *American Insurance Association v. Garamendi*, 539 U.S. 396 (2003); *United States v. Belmont,* 301 U.S. 324 (1937); *United States v. Pink,* 315 U.S. 203 (1942). The Court has had no occasion to decide whether a later executive agreement prevails over an inconsistent earlier law of Congress,

While many of the executive agreements involve minor matters, some involve very important matters, such as the General Agreement on Tariffs and Trade (GATT) in 1948. It remained in effect until 1995, when the International Trade Organization (ITO), established under GATT, was replaced by the World Trade Organization (GTO). Note that the Russian Federation joined WTO in 2012, after 18 years of negotiations. One of the problems in Russia's joining WTO reflects the fact that in the United States, both Congress and the President have power over foreign relations. During the time of the Soviet Union, Congress enacted the Jackson-Vanik Amendment, which denied the Soviet Union normal trade relations with the United States under the "most favored nation" provision, which required that a benefit for one member of the ITO applied to all ITO members. Congress gave the President the authority to waive the restrictions of Jackson-Vanik, and ever since 1992, with the fall of the Soviet Union, the President has waived the restrictions for Russia every year. But Congress did not repeal Jackson-Vanik until 2012, upon Russia's accession to membership in the World Trade Organization, and for many years, it had been an irritant in American-Russian relations.

In any event, most executive agreements are concluded with a single nation, and some involve very important matters. Some of the executive agreements entered into between the United States and the Russian Federation include plutonium production reactors, cooperation in research on radiation effects, elimination of the application of high-enriched uranium for peaceful uses of nuclear energy, aviation safety, the transit of American armaments and military personnel through the territory of the Russian Federation to Afghanistan, the establishment of a direct secure communications system between the United States and the Russian Federation, the continuation of the 1972 agreement on the prevention of incidents over the high seas, cooperation in the fields of meteorology, hydrology and oceanography, scientific and technical cooperation in the earth sciences, the importation into the United States of firearms and ammunition from the Russian Federation, the certification of seafood products from the United States to the Russian Federation and very importantly, cooperation in outer space, including the International Space Station.

In this regard, it may be noted that under Article 86 of the Russian Constitution, the Russian President is given both the power to direct the foreign policy of the Russian Federation and the power to hold negotiations and sign the international treaties of the Russian Federation. By entering into an executive agreement under the power to direct foreign relations rather than under the power to enter into a treaty, the Russian President avoids the requirement of ratification by the State Duma just as the American President by entering into an executive agreement can avoid the requirement of ratification by a two-thirds vote of the Senate. More importantly, as a

although a strong argument can be made that a law of Congress should prevail over an inconsistent executive agreement.

practical matter, when seeking to enter into an agreement with the Russian Federation, the American President is much more likely to use an executive agreement rather than a treaty because of the difficulty of obtaining Senate ratification of the treaty, and the Russian President will have to use the same method in order to enter into an agreement with the United States.

VI. Recent Examples of the Constitutional Framework of National Interests Ensurance in the United States

I will now discuss three recent examples of the constitutional framework of national interests ensurance in the United States: (1) the President's recognition of Cuba and the Cuban Trade Embargo; (2) the Iranian Nuclear Agreement; and (3) the imposition of American sanctions against Russia over the "situation in the Ukraine".

A. The President's Recognition of Cuba and the Cuban Trade Embargo.

The constitutional framework of interests ensurance in the United States with respect to American relationships with Cuba since the Castro government came to power in 1959 may best be described as follows: (1) President Eisenhower recognized the Castro government in 1959, President Kennedy broke off diplomatic relations with Cuba in 1961, shortly before leaving office, and President Obama restored diplomatic relations with Cuba in 2015; (2) Congress has enacted a series of laws imposing a sweeping commercial, economic and financial embargo on Cuba; (3) Congress has given the President broad authority to administer the embargo, including the authority to relax or waive many, but not all, of its restrictions; (4) Over the years, various Presidents have relaxed or waived some restrictions of the embargo, and following his recognition of the Castro government, President Obama has relaxed or waived a significant number of the more onerous restrictions.

While President Eisenhower recognized the new Castro government in January, 1959, shortly after it came to power, relations between the Cuban government and the United States began to deteriorate in 1960 after the Cuban government seized American-owned oil refineries. The conflict escalated when President Eisenhower then cut off the Cuban sugar quota, thus banning exports to the major market for Cuban sugar. Cuba then expropriated all the American-owned properties, and President Eisenhower prohibited all exports to Cuba, except for nonsubsidized food, medicines and medical supplies President Eisenhower broke off diplomatic relations with Cuba on 3 January 1961, shortly before leaving office. In the Foreign Assistance Act of 1961, Congress authorized the President to establish a total embargo on all United States trade with Cuba. Pursuant to this authorization, in 1962, the President suspended preferential and most-favored nation tariff treatment to Cuba, and in

1963, the Treasury Department issued the Cuban Assets Control Regulations (CACR), which imposed a comprehensive set of economic sanctions, including a freeze on all Cuban-owned assets in the United States and restrictions on all commercial, financial and travel transactions with Cuba by American citizens. In 1982, the Secretary of State added Cuba to the list of countries supporting terrorism for its complicity with the M-19 Movement in Columbia. Being put on the list would exclude Cuba from a wide range of American foreign assistance programs. In the same year, the Treasury Department announced the reimposition of travel restrictions to Cuba, with some exceptions for American government officials, scholars, journalists, and Cuban-Americans visiting their relatives. The exception was slightly broadened by the Clinton Administration to allow persons seeking to travel for "clearly defined educational or religious activities" and "for activities of recognized human rights organizations". A 1992 law, the Helms-Burton Act, among other restrictions, prohibited foreign subsidiaries of American corporations from engaging in transactions with Cuba and prohibited ships with Cuban goods from entering American ports. A 2000 law allowed trade with Cuba in agricultural products, medicines, and medical supplies, but prohibited direct public or private export financing for this trade, so all transactions must be in cash[42].

Once President Obama decided to restore diplomatic relations with Cuba, he was able to use the authority granted to him by Congress to relax or waive a significant number of the more onerous restrictions[43]. First off, the President removed Cuba from the list of nations supporting terrorism. This will make it easier for Cuba to access multilateral loans and have other economic advantages, such as lowering the interest rate on loans to the Cuban government[44]. American air carriers can now schedule flights to Cuba, and individuals can travel on their own instead of in groups so long as they certify that the visits are for educational, religious, cultural, journalistic,

[42] Congressional Research Service, "Cuba-U.S. Relations: Chronology of Key Events, 1959-1999," Updated December 14, 1999; United States International Trade Commission, "The Economic Impact of U.S. Sanctions with Respect to Cuba," Investigation No.332-413, February, 2001.

[43] Interestingly enough, the main source of the authority to relax or waive sanctions on Cuba results from the fact that Cuba is subject to sanctions under the Trading with the Enemy Act. In order to be able to exercise this authority, the President must make a yearly determination that "the exercise of those authorities with respect to Cuba is in the interests of the United States". President Obama has made this determination every year, as past Presidents have had to do in order to make Cuba subject to sanctions under the Act. See "President Obama reauthorizes Cuba listing on 'Trading with the Enemy Act,'" http://abcnews.co.com/Politics/president-obama-reauthorizes-cuba-listing-trading-enemy-act/story?id=33690036, Sep.11, 2015.

[44] *See* Randal C. Archibold, "Cuba Moves Closer to Exit of Terror List," New York Times, April 24, 2015, p.A.6; Victoria Burnett, "Barriers Remain for American Business in Cuba," New York Times, April 16, 2015, p.A.9

humanitarian or family purposes[45]. The Office of Foreign Assets Control will license certain American businesses to establish and maintain a physical presence in Cuba. These include news bureaus, providers of telecommunications or internet-based services, mail carriers, certain cargo transportation and travel providers, and exporters or agricultural products and private construction products. There now will be no limit on the amount of donative remittances that can be sent to Cuba and no limit on funds that people can bring to Cuba[46].

President Obama has made some other changes, and may be able to make some more, but the fact remains that the laws of Congress establishing the Cuban embargo remain in effect. Only Congress can repeal those laws, and until it does so, we will have the seemingly anomalous situation in which the United States has resumed diplomatic relations with Cuba, but a considerable part of the Cuban embargo remains in effect. This situation results from the fact that the constitutional framework of national interest ensurance in the United States allocates power both to the President and to Congress. The President has exercised his authority to resume diplomatic relations with Cuba and to ease some of the restrictions of the Cuban embargo, but Congress has the power to establish the Cuban embargo and has been unwilling to repeal it.

B. The Iranian Nuclear Agreement

The operation of the American constitutional framework of national interests ensurance with respect the Iranian nuclear agreement begins with the American imposition of sanctions against Iran. The sanctions have been imposed pursuant to numerous laws of Congress relating to matters such as claimed Iranian support of terrorism, Iran's development of ballistic missiles, alleged human rights abuses by the Iranian government, claims that Iran has engaged in destabilizing regional activities, and claims that Iran is in the process of developing nuclear weapons. Under these laws, the President has broad authority both to impose additional sanctions and to modify or waive existing sanctions, and Presidents Clinton, George W. Bush, and Obama have all issued executive orders relating to the Iranian sanctions[47].

It is precisely because President Obama had the authority to modify or waive existing sanctions against Iran that he was able to use his power to enter into agreements with foreign governments and to act as the representative of the United

[45] *See* Peter Baker & Randal C. Archibold, "U.S. to Ease Limits on Cuba Travel, Opening the Door to Commercial Flights," New York Times, January 16, 2015, p.A.6.

[46] http://www.steptoe.com/publications — 10820.html, Oct. 16, 2015.

[47] *See* Gregory Korte, "Obama signs executive order revoking Iran nuclear sanctions," USA Today, Jan. 16, 2016; Barbara Slavin, " U.S. options for sanctions relief on Iran,"http://www.al-monitor.com/pulse/originals/2014/06/Iran-sanctions-expiration/6/16/2014.

States in foreign affairs[48], to make the United States a part of the "5+1 group"[49] that entered into negotiations for the Iranian nuclear agreement. The main provisions of the Iranian nuclear agreement prevent Iran from producing enough material for a nuclear weapon for at least 10 years and impose new provisions for inspection of Iranian facilities, including military sites. In exchange for these restrictions on Iran, certain sanctions imposed by the members of the "5+1 group" and the United Nations gradually would be lifted[50]. The President had the power to issue an executive order removing the American sanctions called for in the agreement, because those sanctions had been added by executive order in the first place[51].

Many members of Congress were opposed to the deal and wanted to block it. But the only way that Congress could do so was by enacting legislation that prohibited the United States from entering into the agreement and that prohibited the President from waiving the American sanctions called for in the agreement. In order for Congress to enact such legislation, of course, it had to survive a Presidential veto, and President Obama made it clear that he would veto any effort by Congress to interfere with the Iranian nuclear agreement. Had Congress been able to override the veto, as a constitutional matter, the President would be bound by the legislation and would be precluded from carrying out the agreement. Unlike the Russian Constitution, which gives the President very extensive powers over foreign affairs with only a limited role for the General Assembly[52], under the American Constitution, foreign affairs is an area in which both Congress and the President have power, and if there is a conflict between the exercise of power by the President and the exercise of power

[48] As discussed previously, while the only agreement between the United States and a foreign power that is covered in the Constitution is a treaty, which requires a 2/3rds ratification by the Senate, it is well recognized that the President as the representative of the nation in foreign affairs can enter into executive agreements with foreign nations on behalf of the United States.

[49] The 5 permanent members of the United Nations Security Council, the United States, Russia, Great Britain, France, and China, plus Germany.

[50] *See* "Iran nuclear deal is done," httw://www.cbsnews.com/news/us-iran-nuclear-deal-lift-sanctions-enrichment-stockpile-centrifuges/July 14, 2015; David E. Sanger and Michael R. Gordon, "Iran negotiators face late obstacles to a deal", http://www.nytimes.com/2015/03/15/world/middleast/iran/ March 14, 2015.

[51] *See* Korte, *supra*, note 47. When the President began to lift the sanctions called for in the agreement, the President issued a statement advising that under the agreement, the United States would only be lifting the nuclear-related sanctions on Iran. The statement emphasized that under the deal the following sanctions would remain in place: sanctions on missile technologies and conventional weapons; sanctions based on Iran being listed as a state sponsor of terrorism and targeted sanctions on individual's connected with Iran's support of terror. The statement also pointed out that the President had the authority to target Iran's development of nuclear missiles, the authority to target Iran's human rights abuses and censorship, and the authority to sanction Iran's destabilizing regional activities, including in Syria and Yemen. See https://whitehouse.gov/issues/foreign-policy/Iran-deal, January 16, 2016.

[52] *See* the discussion, *supra*, notes 15-18, and accompanying text.

by Congress, so long as the matter comes within the powers of Congress, the law of Congress controls[53]. But any current attempt to curtail the President's power must survive a Presidential veto, which, as a practical matter, is extremely unlikely to occur. Congressional opposition to the Iran nuclear deal dissipated when, in the face of a Presidential veto, the House did not consider legislation to overturn the deal, and under the Senate rules, there were not enough votes to bring a resolution of disapproval to the floor for a vote[54].

As the Iran nuclear deal indicates, as a practical matter, the American President has the same power as the Russian President to commit the United States to agreements with foreign nations. The only restriction on the American President is that the President cannot take action that is inconsistent with a law of Congress, but again, as a practical matter, Congress has granted the President broad authority to take most actions connected with foreign affairs, and any Congressional effort to limit the President's authority would be subject to a Presidential veto.

C. The Imposition of American Sanctions against Russia over the "Situation in Ukraine"

The American President and Congress have acted together in imposing sanctions on Russia for its annexation of the Crimea and its alleged military support of the separatists in eastern Ukraine. President Obama acted first in accordance with legislation giving the President broad powers to act in foreign affairs by declaring a "national emergency". On 6 March 2014, when Russia was in the process of recognizing Crimea as an "independent state", laying the ground work for its annexation by Russia, the President issued an executive order imposing a travel ban and freezing the American assets of Russian nationals who were determined by the American Secretary of the Treasury to have "asserted governmental authority in the Crimean region without the authorization of the Government of Ukraine", and whose actions were found to "undermine democratic processes and institutions in Ukraine". On March 16, March 17, and March 20, the President issued additional executive orders, finding that the actions of the Russian Federation, including its purported annexation of Crimea and its use of force in

[53] *See* the discussion, *supra*, notes 26-27, and accompanying text. The only exclusive power over foreign affairs that the Constitution gives to the President is the power to recognize foreign governments, and Congress cannot enact laws restricting the President's recognition power. *See* the discussion, *supra*, notes 23-24, and accompanying text.

[54] *See* Jennifer Steinhauer, "Democrats hand victory to Obama on Iran nuclear deal," New York Times, September 10, 2015, http://nytimes.com/2015/09/11/uspolitics/Iran-nuclear-deal-senate. In the cases where the Court held that the President's actions were contrary to a law of Congress, the law of Congress had been enacted at a time preceding the President's actions.

Ukraine, "continue to undermine democratic processes and institutions in Ukraine, threaten its peace, security, stability, sovereignty, and territorial integrity, and contribute to the misappropriation of its assets, and thereby constitute an unusual and extraordinary threat to the national security and foreign policy of the United States". These executive orders designated a number of Russian entities and individuals, including defense companies, banks, and energy companies, blocking their use of property in the United States. They also suspended credit finance that encouraged exports to Russia and financing for economic development in Russia[55]. At the same time, the European Union was imposing similar sanctions on Russia[56].

President Obama continued to impose additional sanctions on Russia, often parallel to EU sanctions. These sanctions included bans on business transactions in the United States on seven Russian officials, including the executive chairman of the state oil company *Rosneft*, and 17 other Russian companies, which were later extended to *Rosneft* itself an another energy firm, *Novataek*, and two banks, *Gazprombank* and *Vnesheconombank*, and later Russia's largest bank, *Sberbank*, and a major arms maker, *Rostec*[57].

The Russian imposition of counter-sanctions by President Putin was very measured. It consisted of banning certain American officials from entering Russia[58], and banning for one year the import of most agricultural products from the United States, the EU and other countries that had imposed Ukraine-related sanctions on Russia[59].

On 19 December 2014, President Obama issued an executive order with respect to Crimea, which by now had been annexed by the Russian Federation, but which the United States still considers part of Ukraine. The executive order prohibits American investment in what the executive order refers to as the "Crimea region of Ukraine", the importation and exportation of goods from Crimea, any American financing of a

[55] *See* U.S. Department of State, Russia and Ukraine Sanctions, http://www.state.gov/e/eb/tfs/spi/ukraine.russia Executive Order — Blocking Property of Certain Persons Contributing to the Situation in the Ukraine, http://whitehouse.gov/the-press-office/2014/03/06. For the text of the executive orders, *see* Executive Order 13660 of March 6, 2014, Federal Register, Vol.79 No.46, 6/10/2014; Executive Order 13661 of March 16, 2014, Federal Register, Vol.79, No.53, March 19, 2014; Executive Order 13662 of March 20, 2014, Federal Register, Vol.79, No.56, March 24, 2014

[56] *See* European Union, "EU sanctions against Russia over Ukraine crisis," http://europa.eu/newsroom/highlights/special-coverage/ed_sanctions/index_en.htm

[57] *See* "U.S. levels new sanctions against Russian officials, companies," *Haaretz*, April 28, 2014; Mohammed Arshad, "U.S. steps up sanctions on Russia over Ukraine," *Reuters*, September 12, 2014.

[58] *See* Neil Farquhar, "Russia Expands List of Barred Americans", *New York Times,* July 19, 2014, http://www.nytimes.com/2014/07/20/world,europe/russia-expands-list-of-barred-amercians.html.

[59] *See* Andrew E. Kramer & Neil Farquhar, "Putin Bans Some Imports as Payback for Sanctions", *N.Y.Times,* August 6, 2014, http://www. nytimes.com/2014/08/07/world/europe/putin-orders-import-ban-in-retaliation-for-sanctions.html.

prohibited Crimean transaction, and blocks the access to property in the United States of certain Crimean persons and entities[60].

Congress weighed in on the matter of sanctions against Russia by the enactment of the Ukraine Freedom Support Act in December, 2014. But Congress' doing so took the form of authorizing, but not requiring, the President to impose additional sanctions and take other actions against Russia in connection with "the situation in Ukraine". The act was passed unanimously in both Houses, and so it could have overcome a Presidential veto. But there was no reason for the President to veto it, since it simply gave him more authority — which he did not need in any event — to exercise Presidential power in this situation". There was a provision in the proposed law that would have given major non-NATO ally status to Ukraine, Georgia, and Moldova, but that provision was dropped, and the bill was enacted and signed by the President. Among other provisions, the bill gives the President the authority to penalize *Gazprom* if it is found to be withholding significant natural gas supplies from NATO states, or Ukraine, Georgia or Moldova, and the authority to impose sanctions on Russia's sole defense exporter and importer, *Rosoboronexport*, and other Russian producers if the defense sector knowingly manufactures, sells or transfers defense articles to Syria or to anti-government entities in Ukraine, Georgia, or Moldova. The law represents the view of Congress as to what sanctions the President should impose if certain events happen, but it is entirely up to the President whether or not to impose those sanctions[61]. The President has stated that: "At this time, the Administration does not intend to impose sanctions under this law, but the Act gives the Administration additional authorities that could be utilized, if circumstances warranted"[62].

The matter of the American imposition of sanctions against Russia over the "situation in Ukraine" illustrates the practical operation of the constitutional framework of national interests ensurance in the United States. While Congress and the President both have power in the area of foreign affairs, Congress may establish policy guidelines, but must rely on the President to implement those guidelines. Here Congress has expressed its will as to what sanctions the President should impose if certain events happen, but it is entirely up to the President whether or not to impose those sanctions. In the final analysis, then the American President will have the responsibility for resolving on the American side, the seeming conflict between the national interest of the United States and the national interest of Russia with respect to the "situation in Ukraine". Under the Russian Constitution, that power is expressly vested in the

[60] Executive Order 13865 of December 19, 2014, Federal Register, Vol.79, No.247, December 24, 2014.

[61] *See* "U.S. Congress passes Russia sanctions, arms for Ukraine", http://news,yahoo.com/us-congress-passes-russia-sanctions-arms-ukraine-0546211335.html; "What is Ukraine Freedom Act and what does it imply", htpp://sputniknews.com/politics/20141219/1016019302.html/

[62] "Statement by the President on the Ukraine Freedom Support Act", http://www.whitehouse.gov/the-press-office/2014/12/18/statement-president-ukraine-freedom-support-act.

President of the Russian Federation to resolve the conflict on the Russian side. Stated simply, if the conflict between the United States and Russia over the "situation in Ukraine" is to be resolved, it will be up to President Putin and President Obama to do so.

VI. Summary and Conclusion

In the United States, we live under the 18th century Constitution that reflects the 18th century notions of checks and balances and separation of powers. Under this Constitution, both the President and Congress have broad powers in the area of foreign affairs relating to the ensurance of national interests, and there are some interactions between these powers. But as a part of the system of checks and balances, the President is made an integral part of the legislative process, with the power to disapprove or "veto" legislation passed by Congress. Since the President's disapproval of legislation can only be overridden by a two-thirds vote of both Houses, it is virtually impossible for Congress to do so, with the result that the President can prevent Congress from taking any action that the President believes infringes on Presidential power. And since the American Constitution vests the entire executive power in the President and does not provide for a separate "government" to administer the laws, as it is provided under the Russian Constitution, Congress can and, as a practical matter, must grant broad discretion to the President to administer and enforce the provisions of legislation that Congress has enacted. Legislation containing grants of authority to the President will be broadly construed, so as to avoid any potential conflict between Congressional and Presidential power and a resulting constitutional separation of powers question. Particularly is this so when the legislative authorization in question relates to foreign affairs.

The only exclusive power over foreign affairs that the American Constitution gives to the President is the power to recognize foreign governments, and Congress cannot interfere with that power. Otherwise, where Congress exercises its legislative power to enact legislation regulating foreign affairs, the President cannot act contrary to the law of Congress. As a practical matter, this situation will occur only where the Presidential action is contrary to an earlier law enacted by Congress, since a contemporaneous effort by Congress to restrict Presidential power is almost certain to be prevented by a Presidential veto, as we have seen with proposed legislation to prevent the President from entering into the Iranian nuclear agreement.

There may be some tension between the role of Congress and the role of the President in involving the nation in armed conflict, since Congress has the constitutional power to declare war, but the Constitution designates the President as Commander-in-Chief of the Armed Forces. While the law relating to the exercise of military power by the President and by Congress has not been definitively settled by

the Supreme Court because of the Court's refusal to entertain suits between the President and Congress over this matter under the "political question" doctrine, there is a common understanding between American Presidents and Congress as to when Congressional authorization is or is not required. That common understanding is usually, though not always, followed by the President when deciding whether or not to take military action.

It is fair to say that American Presidents have sought or claimed Congressional authorization for military action involving a full-scale war with a foreign nation. Congressional action has been sought and authorized for American entry into World War II, the Gulf War against Iraq, military action against the Taliban regime in Afghanistan, and military action against the Saddam Hussein regime in Iraq, and Congressional authorization has been claimed for American participation in the Vietnam War. It has been assumed that Congressional action is not required when the President commits the United States to military intervention that is specifically called for under the nation's military obligations, such as American participation in the Korean War pursuant to a resolution of the United Nations Security Council, and military involvements authorized by NATO in Bosnia and Kosovo and the NATO bombing of Libya, designed to overthrow the Gaddafi regime. It is also part of the common understanding that the President as Commander-in-Chief can act without Congressional authorization in "emergency-type" or "short-term temporary" situations, such as President Reagan's sending American troops into Grenada, an island country in the Caribbean, in 1983, in order to rescue American students attending a medical school there, who were purportedly in danger due to the actions of a newly installed government that was favorable to Cuba, and overthrowing the pro-Cuban government in the process.

Finally, it is a part of this common understanding that Congress can preempt military action by the President by using its appropriations power to specifically prohibit the use of appropriated funds for a particular military action. Of course, it can only do so in an appropriations bill that is subject to veto by the President, which makes this method of preempting military action by the President very unlikely to occur.

The President's power over foreign affairs is enhanced by the Supreme Court's recognition of the President's power to enter into executive agreements with foreign nations, thereby avoiding the requirement of entering into a treaty, which requires ratification by a two-thirds vote of the Senate. The authority of the President to enter into executive agreements is based on his power under Art. II to act as the representative of the nation in foreign affairs, and the overwhelming majority of agreements between the United States and foreign nations take the form of executive agreements.

In the final analysis, the conclusion is inescapable that under the constitutional framework of national interests ensurance under the American Constitution, as that framework operates in practice, the primary responsibility for national interests ensurance rests with the President. While the constitutional framework gives both the Congress and the President broad powers over foreign affairs, the way that framework operates in practice clearly strikes the balance in favor of the President. This is so for a number of reasons. *One*: the President can veto Congressional legislation purporting to limit Presidential power in the area of foreign affairs, and it is virtually impossible for Congress to override the President's veto of that legislation. This means that while, apart from recognition of foreign governments, the President cannot act contrary to a law of Congress, the only laws of Congress that could restrict Presidential power are laws that were enacted at an earlier time, since a contemporaneous effort by Congress to restrict Presidential power is almost certain to be prevented by a Presidential veto. *Two*: since the Constitution vests the entire executive power in the President and does not provide for a separate "government" to administer the laws, Congress can and must grant broad discretion to the President to administer and enforce the legislation that Congress has enacted, and Congressional authorization in the area of foreign affairs will be broadly construed. *Three:* the power to recognize foreign governments belongs exclusively to the President, and it is a very important power. *Four*: under the "political question" doctrine, the federal courts will not entertain suits between the President and Congress over questions of Presidential and Congressional power, so most Presidential actions, including involving the nation in armed conflict, will not be reviewed by the courts. While there is a common understanding between American Presidents and Congress as to when Congressional authorization is or is not required, it is entirely up to the President whether or not to seek Congressional authorization in a particular case. *Five*: the President has the power to enter into executive agreements with foreign nations, thereby avoiding the requirement of Senate approval of a treaty by a two-thirds vote, and the overwhelming majority of agreements between the United States and a foreign nation take the form of executive agreements.

When we compare then the constitutional framework of national interests ensurance under the American and Russian Constitutions, we see that while the American Constitution does not by its terms give the American President the substantially complete power over foreign affairs that the Russian Constitution entrusts to the President of the Russian Federation, in practical operation, the American President has almost as much power as the Russian President with respect to national interests ensurance. The future of relations between the United States and the Russian Federation will be determined in large measure by the actions of the American President and the actions of the President of the Russian Federation.

DISPUTE CONCERNING THE POLISH CONSTITUTIONAL TRIBUNAL

Zdeněk Koudelka
Associate Professor, Department of Constitutional Law and Political Science, Faculty of Law, Masaryk University, Brno, Czech Republic

Abstract
Poland is currently under criticism for an amendment of the Constitutional Tribunal Act passed by the new government majority party called Law and Justice (PiS). In 2015, the legislative change was adopted, which introduced an obligation for the Constitutional Tribunal to discuss an unconstitutionality of an act only in the presence of at least 13 judges, under the chairmanship of President or Vice President of the Constitutional Tribunal. An act is unconstitutional if two-thirds of the judges vote for it. The author compares this requirement with the adjustment in Bohemia, Moravia and Silesia in the past and present.

Keywords: Poland, Constitutional Tribunal.

Poland is currently under criticism for an amendment of the Constitutional Tribunal Act passed by the new government majority party called Law and Justice (PiS). Let us look at the facts.

New Polish Constitutional Tribunal Act of June 2015

In June 2015, President Bronisław Komorowski, before the end of his term in office and that of the government of Prime Minister Ewa Kopacz, approved a completely new Constitutional Tribunal Act[1]. The President as well as the government represented the Civic Platform (PO) generally known to be heading towards defeat in the presidential as well as parliamentary elections scheduled for 2015. And that was indeed the case. The new Polish President, Andrzej Duda, a representative of the Law and Justice Party, was elected on 24 May 2015 and his inauguration was held on 5 August 2015. On 25 October 2015, the same party subsequently achieved an overwhelming victory in the parliamentary elections with an absolute majority of votes both in the Lower Chamber of the Polish Parliament (Sejm) and the Senate. The new Constitutional Tribunal Act was passed in June 2015 against the will of the opposition by the then holders of political power in the country. At that time, the

[1] Act of 25 June 2015 on the Constitutional Tribunal, Journal of Laws No.1064/2015. The Act came into force on 30 August 2015.

previous President was already defeated in the presidential elections and the defeat of the current government was imminent. The political legitimacy of that representation was considerably weakened by then. In the new Act, the Civic Platform party passed regulations making it possible to elect new judges no sooner than within three months before the mandate of the current judges of the Constitutional Tribunal expires and their term of office ends, and explicitly allowed for the transitory election by the previous Sejm of new judges in replacement of all the judges whose mandate expired in 2015. At that time, prior to the elections scheduled for later that year, the Civic Platform still held the majority in the Sejm[2]. The President of the Constitutional Tribunal, Andrzej Rzepliński, and his deputy, Stanislaw Biernat, approved for their offices by the Civic Platform, actively participated in the drafting of the Act.

Judges Inaugurated by the Civic Platform in October 2015

Polish constitutional judges are elected by the Sejm in Poland[3]. The term of office of the Sejm is four years. Its detailed regulations state that the term of office begins on the day of the first assembly summoned by President of the Republic of Poland and ends on the day preceding the day of the first assembly of the subsequently elected Sejm[4].

The Civic Platform government decided to secure posts for their candidates in the Constitutional Tribunal before their term in office ended even though they no longer had the confidence of their electorate. Therefore, they elected five new constitutional judges out of a total of fifteen on 8 October 2015, shortly before the scheduled parliamentary election at the end of 7th electoral term of the Sejm (2011-15), to replace the judges whose term in office ended in November and December of 2015, i.e. after the election of the new Polish Sejm for the 8th electoral term, which took place on 25 October 2015. Thus, all of the 15 judges of the Constitutional Tribunal were elected within two terms of the Sejm when the Civic Platform was the majority party. In 2015, the term of office for the last judges elected in the period of the first government of the Law and Justice Party 2005-07 ended. However, the Polish Constitution, by enactment of the nine-year term of office of the judges of the Constitutional Tribunal, assumes that a complete replacement can be made over up to three Sejm terms in succession for the four-year term of office of the members of the Sejm.

[2] Section 137 of the Constitutional Tribunal Act of 25 June 2015.

[3] Section 194 (1) of the Constitution of the Republic of Poland of 2 April 1997, Journal of Laws No.483/1997.

[4] Section 98 (1) and Section 144 (3) (2) of the Constitution of the Republic of Poland.

This step was not accepted by the then opposition Law and Justice Party, and was countered by the new President of the Republic of Poland, Andrzej Duda, who did not invite the newly elected judges to take their vow before him, which is the legal pre-condition of their inauguration[5]. This concerned the following judges: Roman Hauser, Krzysztof Ślebzach, Andrzej Jakubecki (due to be inaugurated on 7 November 2015), Bronisław Sitek (due to be inaugurated on 3 December 2015), and Andrzej Jan Sokala (due to be inaugurated on 9 December 2015).

The dispute was fuelled on 3 December 2015 by the Constitutional Tribunal itself, which declared the election of the new judges in 2015 by the old Sejm as unconstitutional as far as this concerned the replacement of those judges whose term of office was to end after the beginning of the term of office of the newly elected Sejm[6]. This meant in fact that the Constitutional Tribunal ruled that the judges whose term of office began in November 2015 were elected in compliance with the Constitution, while the two judges to be inaugurated in December were deemed to be elected unconstitutionally. The Constitutional Tribunal based its judgement on the fact that the provision of the Constitutional Tribunal Act passed by the Civic Platform in June 2015, allowing for the election of constitutional judges by the Sejm before the mandates of the current judges expired[7], may not be used Sejm to elect judges whose term of office is to start after the term of office of the Sejm electing them expires. The Constitutional Tribunal considered the fact that the 7th electoral term of the Polish Sejm, controlled by the Civic Platform, expired on 11 November 2015; however, the new Sejm was already elected in October for the 8th electoral term — with the first day of office on 12 November 2015.

When hearing this case, the Constitutional Tribunal acted in violation of the law. Subsequent judicial review of the legislative acts passed in Poland can be judged by a five-member judicial body according to the original wording of the Constitutional Tribunal Act, unless the case is assigned by the President of the Tribunal to the general assembly as an issue of substantial significance. This is the Tribunal's President Andrzej Rzepliński initially did in the name of the Civic Platform. When, however, he saw that he would not have a sufficient number of judges in the general body to judge the case, for he himself was considered biased and he did not accept the mandate of the judges elected on 2 December 2015, he decided to refer the case for judgement to a five-member judicial body. Such a reassignment of a case from the general assembly to a five-member judicial body is not allowed by the Constitution or the Constitutional Tribunal Act.

---

5 Section 21 of the Constitutional Tribunal Act of 25 June 2015.

6 Decision of the Constitutional Tribunal published on 16 December 2015, Journal of Laws No.2129/2015.

7 Section 19 (2) of the Constitutional Tribunal Act of 25 June 2015 in the wording before it came into force, Journal of Laws No.1928/2015., shortening this deadline to 30 days.

Judges Elected by Law and Justice in December 2015

Prior to this, the Law and Justice Party passed a resolution in the Sejm on 25 November 2015 invalidating the election of 5 candidate constitutional judges on 8 September 2015, and requesting that the President of the Republic of Poland does not accept their vows. On 2 December 2015, the Sejm elected five new constitutional judges and the President accepted their vows on 3 December 2015 (4 judges) and on 9 December 2015 (1 judge). The decision of the Constitutional Tribunal of 3 December 2015, published in the Journal of Laws on 16 December 2015, was then commented on by the Presidential office. The comment was that the President cannot accept the vows of the 3 judges elected on 8 October 2015, whose election was declared by the Constitutional Tribunal to be compliant with the Constitution, for the Constitutional Tribunal seats were by then already all occupied.

In addition, on 19 November 2015, the first amendment of the Constitutional Court Act was passed[8]. Under this amendment, for example, the term of office of President and Vice-President of the Constitutional Tribunal was shortened to three years and the deadline for the commencement of the process of election of a new judge before the expiry of the term of office of the existing judge, was shortened from 3 months to 30 days. This amendment was however declared by the Constitutional Tribunal as mostly in violation of the Polish Constitution on 9 December 2015[9]. The decision was published on 18 December 2015[10].

Judges Struggle for Incumbencies

According to the original Act on the Polish Constitutional Tribunal of 1985, the rights and obligations of the judges of the Constitutional Tribunal were governed by the Supreme Court Act[11]. Until 1997 the retirement of judges was not covered by the Polish law. Judges retired according to the general pension scheme regulations. The

[8] Act on the Amendment of Constitutional Tribunal Act of 19 November 2015, Journal of Laws No.1928/2015. http://dziennikustaw.gov.pl/du/2015/1928/1

[9] Decision of the Constitutional Tribunal, published on 18 December 2015, Journal of Laws No.2147/2015.

[10] The Czech Television programme called *Události, komentáře (Events, Comments),* ČT 24 on 19 January 2016, featured a discussion about the criticism of the central European institutions based in Brussels levelled at Poland, and concerning the election of a government in Poland that is not pro-European. The programme included an incorrect statement by European MP Stanislav Polčák (TOP 09), who said that the new Polish government refused to publish the decision of the Polish Constitutional Tribunal of 9 December 2015 concerning constitutionality of the amendment of the Constitutional Tribunal Act. This nonsense was confirmed by the present Prime Minister's Secretary for European Matters, Tomáš Prouza. In reality, the decision was published as early as 18 December 2015, Journal of Laws No.2147/2015.

[11] Section 16 (1) of the Act on the Constitutional Tribunal, Journal of Laws No.98/1985. I would like to express my thanks for the information provided by a leading Polish constitutionalist, Boleslaw Banaszkiewicz of Warsaw.

old-age pension was much lower than the salary a judge received when active, which was also true for many other social fund pensioners.

In the executive legislative acts that followedthe passing of the Polish Constitution of 1997 the retirement of judges of general, administrative and military courts was regulate[12]. Under this retirement scheme the judge's appointment was effective untill the end of the judge's life. Thus, a retired judge remained in quasi-employment without actually having to work. This is a mere legislative fiction aimed at dealing with the fact that the level of old-age pensions due to judges was deemed to be unjust in the perception of other citizens of the Polish State. The Constitution does not classify the Constitutional Tribunal and the State Tribunal as a common court. The difference is that common courts, including administrative and military courts, are named using the Slavic term for the court[13], while the Constitutional and the State courts are named after the Latin "tribunal"[14]. The provisions of the Constituton referring to the judges of the Constitutional Tribunal do not deal with retirement but the term of office of the Constitutional Tribunal judge[15]. Common court judges are not appointed for a term of office and retire for age or health reasons, which is formally their last stage of of their career. In case of the Constitutional Tribunal judges, there is the 9-year term of office[16] after which they cease to be constitutional judges.

When in 1997, following the passing of the new Constitution, President Aleksander Kwaśniewski initiated amendments to the court and tribunal legislation, the Constitutional Tribunal judges influenced the President and made sure that the Constitutional Tribunal Act of 1997, as did the Act of 1985, included an inconspicuous legislative reference to the rights and obligations of Supreme Court judges[17]. Thereby, the judges of the Constitutional Tribunal, in spite of the absense of any explicit clause referring to their retirement in the Act, secured the standard retirement provisions reserved for judges, including the financial benefits associated, and they began to interpret any legislation concerning them in this context.

The Constitutional Tribunal Act of 2015 openly restates the to-date privileges of constitutional judges:

— The salary of a judge is five times the average wage calculated without the costs of social insurance. The average is calculated from the second quarter when most employers pay out mid-year bonuses and contributions until the summer holidays,

[12] Section 175 of the Constitution of the Republic of Poland
[13] In Polish — "sąd".
[14] Tribunal in Ancient Rome meant the raised seat of a judge.
[15] Section 196 (3) of the Constitution of the Republic of Poland.
[16] Section 194 (1) of the Constitution of the Republic of Poland.
[17] Section 6 (8) (originally (4)) of Act on the Constitutional Tribunal, Journal of Laws No.643/1997.

which means that this average is generally higher than the annual average wage[18]. In the case of a decrease in the common average wage, the salary of Constitutional Court judges is preserved without any reductions. Even if Poland went bankrupt and the rest of the nation started dying of poverty, the judges of the Constitutional Court wish to have their incumbencies preserved regardless the poverty of the people and the State;

— Combining the judge's position with a salary for full-time research or academic work[19]. Profit-making activities outside the Tribunal are the reason why the Constitutional Tribunal decisions take such a long time. This is true despite the fact that, as a body responsible exclusively for a review of constitutional standards and not dealing with the constitutional complaints of private individuals, the Polish Tribunal has to deal with a considerably lower number of cases than constitutional courts in other countries;

— Retirement after expiry of the official term of office with the right to old-age pension, regardless the age, in the amount of 75% of the current salary of Constitutional Tribunal judge[20];

— Right to an earlier retirement for health reasons[21];

— Right to severance pay in the amount of six monthly salaries upon retirement[22]. This incumbency is quite peculiar and incompatible with the ideas of social justice and equal rights under law. The reason is that while under labour law a severance pay is treated as compensation for losing a job, the retirement of a judge is not such a case. The judge retains the title of a judge, the use of the office car from time to time, and receives the salary of a judge although he does not have to work as judge any longer. The right to severance pay upon retirement is excused by the fact that in 1997 the provisions for the retirement of judges were added to the Supreme Court Act while someone "forgot" to cancel the previous provision on severance. But why was this error retained in the new Constitutional Tribunal Act of 2015? When it comes to the benefits of the Constitutional Tribunal judges, the law, logic and common sense remain silent.

The Act on the Polish Constitutional Tribunal, whose draft was prepared by the affected judges themselves, confirms the words of the Roman Emperor Vespasian: "*Money does not stink*". It is not surprising that in the course of the dispute about the composition of the Polish Constitutional Tribunal in 2015-16 neither the judges appointed by the Law and Justice Party nor those appointed as representaives of the

[18] Section 33 (1) and (2) of the Constitutional Tribunal Act, Journal of Laws No.1064/2015.
[19] Section 23 (2) of the Constitutional Tribunal Act of 2015.
[20] Section 37 and Section 40 (2) of the Constitutional Tribunal Act of 2015.
[21] Section 38 of the Constitutional Tribunal Act of 2015.
[22] Section 40 (1) of the Constitutional Tribunal Act of 2015.

Civic Platform questioned these incumbencies. Every judge, be it "Paul or Saul", wanted to retain them. However, the incumbencies of the Constitutional Tribunal judges are immoral. That is why the Constitutional Tribunal has earned the charisma of "a drenched rag" in the eyes of many ordinary Poles, not in the least interested in its composition.

Second Novella of the Constitutional Tribunal Act of December 2015

The Polish Parliament, with the consent of Polish President, passed another amendment to the Constitutional Tribunal Act in December 2015[23]. The principal change was the strengthening of collective general decision-making process of the Constitutional Tribunal at the cost of small judicial bodies. In principle, now all 15 judges will be ruling in the general assembly, unless otherwise stipulated by law. Any cases, not decided by the general assembly of all the judges, will be heard by a seven-member body instead of the to-date three-member one. There were also five-member bodies in addition to the three-member ones, deciding, for example, on the non-constitutionality of legislative acts. This competence is now reserved for the general assembly of the Constitutional Tribunal.

The general assembly of the Polish Constitutional Tribunal will now make decisions in a quorum of at least 13 of the total 15 members, including the compulsory presence of the President or Vice-President. The decisions will be reached by a two-thirds majority. The most important power of all constitutional courts is the power to revoke ordinary legislative acts on the basis of their incompliance with the Constitution. In our country, the Constitutional Court can thus cancel an ordinary legislative act in its general assembly in the presence of at least 10 judges. At least 9 judges have to vote in favour of revoking the act. Therefore, in the quorum of 10 judges 9 judges represent a 90% majority. When comparing this with the Polish Constitutional Tribunal you can see that while our quorum requirement is 3 judges less — 13 judges in Poland, 10 judges in our country, the requirement for passing a decision is similar in both countries in terms of the proportion of the total number of judges in the court, two thirds in Poland (60% of the 15 judges), or three fifths in our country (66.6% of the 15 judges or 90% of at least 10 judges present).

The fact that the amendment to the Constitutional Tribunal Act of December 2015 introduces the rule that the general assembly makes decisions in substantial matters is an attempt to rectify the previously to-date non-constitutional situation, as the Polish Constitution requires a simple majority of votes for decisions made by the Constitutional Tribunal[24]. The Constitution does provide any rules for decision

[23] Act on the Amendment to the Constitutional Tribunal Act of 22 December 2015, Journal of Laws No.2217/2015.

[24] Section 190 (5) of the Constitution of the Republic of Poland.

made by a smaller judicial body. Previously, when non-constitutionality of a legislative act or an international treaty or other important matters were decided by five-member bodies of the Constitutional Tribunal, including cases where legislative acts were revoked on the basis of non-constitutionality, which is always a cardinal question and where the judicial power intervenes with the legislative power, the joint will of the Sejm, the Senate and President of the Republic of Poland could be thwarted in practice by just three judges in a five-member judicial body, even if all the other judges of the Constitutional Tribunal might consider the legislative act to be in compliance with the Constitution. This situation was in contradiction with the Polish Constitution, requiring a simple majority of all the judges to decide about these matters. If non-constitutionality of a legislative act could be decided by just three judges, then this was a minority of all the constitutional judges.

The new amendment is disputable in the fact that it is not clear whether the constitutional requirement of majority of votes may be interpreted at the sole discretion of the legislator and who would decide whether this majority is to be defined as simple, absolute or qualified. It also remains unclear whether it is necessary to use the narrow interpretation in terms of absolute majority and whether this absolute majority should be calculated from all or just the judges present at the hearing. Where the Constitution is tacit, a more detailed stipulation of these matters by ordinary legislation is a must.

Decision-making by the Supreme Court institutions in general assembly rather than in small judicial bodies serves the idea of achieving consistency of decisions in similar cases. Even our constitutional court is criticised for lack of consistency in its decision-making in the various three-member bodies. The Constitutional Court of the Czech Republic has decided to prevent this by delegating some matters to the general assembly[25], albeit this is not directly required by the law (constitutional complaints against President, the Parliament and special bodies of the Supreme Administrative Court, electoral matters relating to parliamentary and presidential elections), and further by introducing rotation of judges between the judicial bodies every two years since 2016[26]. These changes are governed by the effort to eliminate inconsistency of decision-making. However, these changes are still insufficient, for consistency of decisions may only be achieved by decision-making in the general assembly of all the judges in all matters. This is how the Supreme Court of the USA or Denmark decides, for example. In our country and in Slovakia the most important competence of the Constitutional Courts — the right to judge on the constitutionality

[25] Communication of the Constitutional Court on delegation of power, Journal of Laws No.52/2014.

[26] Decision of the General Assembly of the Constitutional Court on appointment of the Senate of 8 December 2015, Org. 60/15.

of ordinary legislation — is also decided by the general assembly and not by the smaller judicial bodies of the Constitutional Courts.

By comparison, it is noteworthy that the First Republic Czechoslovakian Constitutional Court had to make decisions about the invalidity of an ordinary legislative act by the majority of at least five out of the total seven members in the presence of a quorum of at least five members[27]. This meant that any decision about the invalidity of an unconstitutional act required the consent of 71% of all judges or a unanimous decision in the quorum of at least five judges. Even the act on the first Czechoslovak Constitutional Court required the presence of the President or the Vice-President and other four members of the court. The President was even given the decisive vote in the case of equal distribution of votes, which however did not apply to decisions invalidating legislative acts, where at least five affirmative votes were required. The Czechoslovak Federal Constitutional Court decided about non-constitutionality of a legislative act also in it is a general assembly where at least nine of the total of twelve judges had to be present, or three quarters of all judges (75%)[28]. Decisions were passed by an absolute majority of votes, with the exception of changes to legal opinions previously expressed by the Constitutional Court in the matters of Constitution interpretation where at least 9 judges had to be present.

The Polish amendments strengthening the general assembly decisions at the cost of small legislative body decisions are fully compatible with the European principles of constitutional judicature. They are also close to our constitutional law. Therefore, criticism of these steps is based on non-legal arguments. These are the same arguments for which the new Hungarian constitution was also criticised, including, for example, the ridiculous criticism of the fact that the Hungarian Minister of Finance would be allowed to take part in the meetings of the board of the Hungarian National Bank, which has been a long established rule in our country and elsewhere, and which has never been contested[29]. What does not matter in our country and in other countries did matter in Hungary. As in the case of Hungary, in Poland the real reasons behind the criticism lie in the fact that both countries, in compliance with the will of their electorate expressed in the general elections, chose a path different to the one preferred by the minority losing the elections, and dear to certain Brussels officials. But that is the essence of democratic elections.

The First Vice-President of the European Commission, Frans Timmermans, before President Duda signed the act amending the Constitutional Tribunal Act, called for a suspension of the approval process. The Luxembourg Minister for Foreign

[27] Section 8 of the Act on the Constitutional Court, Journal of Laws No.162/1920.

[28] Section 9 of the Act on organisation of the Constitutional Court of the Czech and Slovak Federative Republic and on proceedings before this court, Journal of Laws No.491/1991

[29] Section 11 of the Act on the Czech National Bank, Journal of Laws No.6/1993.

Affairs, Jean Asselborn, whose country held the European Union presidency in the latter half of 2015, said on 24 December 2015 that the developments in Warsaw remind him of the dictator regimes in post-Soviet countries and that following the restriction of the independence of courts, restriction of the freedom of expression may be expected next and thus the European Union is obliged to impose respect for the fundamental freedoms and should act on this matter[30]. The President of the European Parliament, Martin Schulz, even spoke about a State coup in connection with the post-election changes in Poland.

When assessing these threats to Poland by Brussels officials, one cannot but recollect the Brezhnev doctrine of restricted sovereignty of socialist States. In today's Europe, countries can be free but only if their idea of freedom corresponds to the political ideas of Brussels. This is not real freedom, though. And it is not sovereign Statehood either. Both the Hungarian and the Polish examples show that heads can be raised and foreign pressure may be opposed. The question whether courts decide about certain matters in their general assembly or in small judicial bodies, and what the composition of these will be is a purely internal issue falling within the sovereign powers of any State that is not a protectorate[31].

[30] http://zpravy.idnes.cz/evropska-komise-vyzyva-varsavu-aby-zvazila-sporny-zakon-o-ustavnim-soudu-1ul-/zahranicni.aspx?c=A151225_112519_zahranicni_ert

[31] For example, the changes in composition and decision-making practice of the Constitutional Court in Bosnia and Herzegovina were laid down by the Dayton Peace Treaty stating that three out of the nine judges would be foreigners selected by President of the European Court for Human Rights. Unilateral change is not possible under the current legal situation. In fact, Bosnia and Herzegovina is thus an international protectorate. The protector is the high representative for Bosnia and Herzegovina, who may even recall any local official, including members of the collective head of the State — presidency of Bosnia and Herzegovina. This is definitely not what sovereignty of a State is about.

CREATION OF A FUNDAMENTAL LAW: DESIGN OF A CONSTITUTION PROTOTYPE BY PUBLIC CONSCIOUSNESS

Sergey F. Udartsev
Doctor of Law, Professor, Director of Research Institution of Legal Policy and Constitutional Legislation of the KAZGUU University, Astana, the Republic of Kazakhstan

Abstract
The article considers the issue related to a historical search of public consciousness and practical application of mechanisms and means of the rule of law protection. The article gives different options of fixing and protecting the rule of law that were used even in ancient times (religious ideas and condemnation; formation of people's consciousness in the process of legal and moral upbringing; appointed and elected officials as personified keepers of law; interpretation of law by Roman lawyers; protecting bodies of cosmic basics of the rule of law mentioned by Plato, etc.). The author proves that the way of social creation of modern constitutions is a historically long search for the most suitable form to ensure unity, stability and hierarchy of the legislation system.

Keywords: constitution, the rule of law, fundamental law, constitution, legal rule, public consciousness, law practice, hierarchy of law, legal system stability.

A Constitution, as a form of a legal document possessing the superior power and as a set of some crystallized functions in the legal system, firstly appeared as a written constitution in the end of the XVIII century (the US Constitution).

However, such a phenomenon as an "unwritten" or "disjointed" constitution — considered as a set of rules, which organizes the activity of the state and protection of subjects' (citizens') rights and written in many statutes — was created much earlier, for example, in Britain, especially after the Glorious Revolution of 1688.

Documents similar to a Constitution, but with other titles may be found in other times, for example, in the Middle Ages.

Long before it occurred, the set of hierarchical relations and interactions in the legislation system was evolving for a long time; different options and types of legislation as well as their various conceptual explanations beginning with law and legal thought of the Ancient East were tried out.

While the sphere of law evolved, the public consciousness and political-legal practice were searching for, advancing and testing some models of protection of

the rule of law, interaction of law branches, stabilization of law and order as well as law improvement. This process was accompanied by appropriate arguments, explanations and concepts and involved some elements of political, legal, moral and religious consciousness over a corresponding period of time.

Both the legal thought of the Ancient World and its legal institutions that embodied it can provide a lot of models of ensuring the unity of the legal system, its hierarchy, interaction and stability as well as of distinguishing certain basics and creating their protection mechanisms.

Let us consider some *basic models* that existed in ancient times.

1. *The idea of divinity implied in the first texts (sources) containing fundamental legal rules.* Ancient political-legal consciousness and ancient works actually recognized the idea of divine origin of the first texts (sources) containing moral and legal prescriptions and guidelines, which later were detailed in legislation. This was reflected in the Old Testament, the Zend-Avesta, Manu's laws as well as basically in all other religious texts.

2. *Recognition of divinity of law and order, participation of Gods in its implementation.* In mythology of the ancient Sumerian civilization the creators of law and order were heavenly beings, Gods and especially the uppermost ones — the chairman of Gods Council, Anu (Ann, Enn), and the head of executive power of the divine state, Enlil. The infringement of the existed order and laws had to be perceived by the ancient people as demonstration of disrespect to Gods with further punishment. The divinity of law and order, laws, the power of a pharaoh and his close people were an attribute of public consciousness in the Ancient Egypt.

3. *Formula for damnation in Hammurabi's laws.* In opposite to the way of divinization of the early laws, the famous Babylonian tsar — Hammurabi — was probably the first person who tried to use religious-mythological means to protect *the nucleus of the legislation established by him* that was adopted as a code. All future rulers of Babylon had to guard and protect his laws, but their own should be made up in accordance with Hammurabi's laws. It was probably one of the first cases in history when the set of laws acquired the status of fundamental laws. At the same time, to provide additional protection there was a long list of curses made aimed at any person who dared to destroy or change these fundamental laws as well as at his relatives, his people, army, weapons, etc.

4. *Legal and moral education in Confucius's works as a means of strengthening the legal system.* In Ancient China Confucius's study became famous and had a great impact on the legal culture of China and its evolution that is followed even in modern China. Confucius underlined a close connection of law and morality and the priority of morality over legislation. He believed that morality was a main

component or the basis of law. The thinker concluded that in order to protect the rule of law, first of all, it is necessary to impart moral values, customs, rituals and etiquette to a person considered as main social norms that regulate the conduct of any person. According to Confucius, the basics of law have to be strengthened and protected by mastering moral values, rituals and etiquette by people, and supported by the whole system of the established steady and fair social relations. According to the thinker, if public consciousness accepts the necessary rules of behavior by upbringing and purposeful moral and legal influence, it will protect the rule of law better than their enforcement and forced punishment[1].

In subsequent ancient Chinese integrative theories, various attempts were made to produce approaches to Confucianism, Legalism and Daoism[2].

5. *Officials (appointed and elected as personal keepers of the rule of law).* In Ancient India, Emperor Ashoka conducted a widespread social program in education, health care and public construction. Ashoka also *created a position of special officials — "Makhamaters of Dharma"*. They were supposed to travel all over the country once in five years and control the maintenance of justice, laws and the subjects' rights, especially the rights of socially vulnerable groups of people, as well as check living conditions of prisoners, sick people, etc. This supervision over the protection of the rights of the subjects and the application of the emperor's laws was considered as one of the main means to maintain law and order and its stability. The actual implementation of the legislation and the subjects' rights was recognized as a basis of order, a key to maintain stability and justice of the legal system. Makhamaters of Dharma were one of the ancient state institutions protecting rights of people and included such powers which could be found in the subsequent institutions: public prosecutor's offices, state inspections and ombudsmen offices.

In Ancient Sparta, the main mechanism for protecting basics of law was also connected with the office of *special officials with broad and extraordinary powers relating to the protection of unwritten laws*, who were elected by people — ephors. Ephors had to supervise the maintenance of unwritten constitution, created by the famous ruler, Lycurgus. Ephors were elected annually during the time of autumnal

[1] About Confucius's law interpretation, see also: S.F. Udartsev. Istoriia politicheskikh i pravovykh uchenii. Drevnii Vostok. (Akademicheskii kurs) [History of Political and Legal Studies. The Ancient East (Academic Course)]. St.P., 2007, pp.385–389. The article is going to be published in English being translated by O. Kachan.

[2] S.F. Udartsev. Drevnii Kitai. Modernizatsiia i sintez razlichnykh politiko-pravovykh uchenii [The Ancient China. Modernization and Synthesis of Various Political-Legal Studies] // Ibid. pp. 462–513. About details of the public consciousness search, see also: S.F.Udartsev. Konstitutsiia i evolutsiia obshchestva (voprosy teorii i filosofii prava) [Constitution and Evolution of the Society (Issues of Theory and Philosophy of Law)]. St.P.: Universitetskii izdatel'skii konsortsium, 2015. — 388 p.

equinox (without a right to be re-elected) and had to control how properly the institutions of power functioned, including the supervision over the activities by two Sparta tsars[3]. In particular, ephors accompanied the tsars during a war and had the right to displace them in case if they were incompetent while managing troops. Ephors had the right to conduct a pre-trial arrest and displace any official, including a tsar, from executing appropriate duties. Once in nine years they looked for heavenly signs and could declare that Gods had deprived one of the tsars of their patronage[4].

6. *Interpretation of law by Roman lawyers named as "jus respondendi".* In Ancient Rome, there was one special form of law which was also a form of control over reasonable legal basics and maintenance of their principles, stability and flexibility of the Roman law which was to regulate the social life of Rome for centuries. Emperors vested the most famous, notable and honorable lawyers with the right to provide decisions to the courts on behalf of the emperor and to interpret laws, and their decisions and interpretations were accepted as laws. The development of this form of law has undergone three stages as minimum: pre-classical, classical and post-classical. During the pre-classical period, lawyers' opinions were considered in courts as one type of possible legally obtained evidence, but it had to be grounded. Then, in the classical period, it was accepted as a law. However, the number of lawyers who possessed the right of *"jus respondendi"* increased so much that in the post-classical period some limitations were imposed. In the V century, there were only five lawyers left whose opinions were accepted by judges as law (Gaius, Modestinus, Paulus, Papinian, Ulpian). If lawyers disagreed with each other, Papinian's opinion was accepted at first. If he made no statement concerning this or that issue, Paulus's opinion predominated then. However, if Paulus did not express his opinion, the decision was made by the majority of votes[5]. These lawyers

[3] According to the legend, there were two tsars ruling the country because, firstly, the throne in Sparta was passed to twins. Then such ruling by two tsars became a norm of common law. It was recognized that this tradition was initially authorized by Gods.

[4] Discussing the issue about a possibility to trust governance and the court to the best person, who "is not ignorant or does not have distorted judgement", instead of actions as a basis of law, Marsilius of Padua made the following objections to it. Firstly, "such cases occur very rarely". Secondly, the law as concentration of "common sense and sufficient experience" is more reliable, secured from occasions, "bad weaknesses and ignorance" than even the most virtuous person. "Therefore, without doubt, it is necessary to regulate civil cases by means of law rather than trust them to be solved by judges" (Marsilii Paduanskii. Zashchitnik mira [Marsilius of Padua. Defender of the Peace]. Defensor pacis // translated from French by B.U Esenova; scientific editor, introd.art., annotation by G.P. Lupareva. M., 2014, p.120).

[5] *See* also: O.S. Ioffe Yurisprudentsiia Drevnego Rima [Jurisprudence of the Ancient Rome] // O.S. Ioffe. Izbrannye trudy po grazhdanskomu pravu: iz istorii civilisticheskoi mysli. Grazhdanskoe pravootnoshenie. Kritika teorii "hoziaistvennogo prava" [Selected Works on Civil Law: from History of the Civilistic Thought. Civil Legal Relationship. Criticism of the "Economic Law" Theory]. M., 2000, pp.12–40.

wrote important works and comments on different issues relating to Roman private law, collected and interpreted the works of their predecessors.

7. *The supra-state body protecting cosmic basics of law* ("*Night Council*"). This way of protecting law basics was offered by the prominent philosopher, Plato, in his book "Laws". Plato suggested creating the superior authoritative body composed of wise and experienced citizens of Athens that would control the creation of laws and check if laws corresponded to sovereign virtues under divine cosmic laws. This *body aimed at supervising the law* had to function in early morning before its members were involved in private and state matters.

The utopian "Night Council" was Plato's non-implemented idea in the Ancient World. However, this ancient theoretical construction was far ahead of its time. To a certain extent, it seemed to be a prototype for future, more mundane institutions which appeared two thousand years later and were created to check the compliance of the national legislation with constitutional and international basics (for example, constitutional control authorities, the European Court of Human Rights, etc.).

Probably, Plato's idea related to the creation of a body for protecting basics of cosmic law will be implemented by a future cosmic civilization. However, notions about fundamental laws can significantly change at this stage of historical development.

8. Ancient Rome which made some significant changes in the development of jurisprudence — legal sciences and practices — tried *some other legal forms* for creating the core of the legislation. There were cases when the notion "constitution" was used in adopting some acts.

In Roman law, acts of Roman emperors, which had superior legal power, were recognized as constitutions. Among forms of constitutions accepted at that period, there were: "edicts - nationwide published decisions of emperors; rescripts - responses or advice of emperors to individuals and magistracies on legal issues; decrees - decisions made by emperors in cases; mandates – emperors' instructions made for officials"[6].

For instance, there are Emperor Justinian's Constitutions "On Compiling the *Corpus Juris Civilis* (the Digest)", "On Establishing *Corpus Juris Civilis* (the Digest)", etc. In his Constitution "On Compiling the *Corpus Juris Civilis* (the Digest)" of 15 December 1530, Justinian stated: "The first and foremost was to start overcoming the existing shortcomings of the predecessors' constitutions, amending and making them more precise; therefore, we compiled them in one code and removed

[6] Constitutions // History of State and Law. Glossary/ ed. by M. I. Sizikova. M., 1997, p.153.

superfluous repetitions and unfair contradictions so that their sincere character could help all people much quicker"[7]. He addressed the authors creating a new code of laws: "If you find some wrong interpretations in old laws or constitutions described by the ancient creators in their books, you must improve and correct…"[8].

In his Constitution "On Establishing *Corpus Juris Civilis* (the Digest)", Justinian writes that after the new code of laws has been established in courts while applying laws and used in other cases, "nobody can cite or mention other sources except for Institutions, Digests or Constitutions made and promulgated by us. The violator will be prosecuted for forgery together with a judge who has admitted the application (of old laws)"[9].

The above mentioned examples prove that humanity even in the Ancient World was actively searching for theoretical basics, practical means and institutions, which could ensure a sustainable legal development of the state and society, fair use of legislation and its implementation and could protect the rule of law. People's consciousness and practice used different ways of protecting the basics of law searching for future constitutional basics of law.

The formation of the constitutional basics of law continued even in the Middle Ages. Under the conditions of feudal fragmentation, cities created their own forms of legal systems, which contained fundamental laws, guidelines, and criteria. Often, they were based on the well-established customs that regulated the structure of state bodies and some peculiarities of their formation and activity.

Historians say that the first Acts of constitutional importance in Europe were the deed granted by the English King, John Lackland, which was named Magna Carta (1215), the decree of the German Emperor Charles IV named the Golden Bull (1356) and some other acts relating to public law[10]. One of the oldest surviving acts of the world is the Constitution of San Marino adopted on 8 October 1600. It was based on the Town Statute created earlier[11].

The Statute of the Grand Duchy of Lithuania of 1529[12] (the other two were adopted in 1566 and 1588 respectively) was one of the sources of the 1649 Sobornoye Ulozheniye (Russian Code). Incidentally, the present Constitution of

[7] Taken from the Constitution "On Compiling the Corpus Juris Civilis (the Dogets)" // Pamiatniki rimskogo prava. Zakony XII tablits. Institutsi Gaya. Digesty Yustiniana [Relics of Roman Law. Laws of XII tables. Gaius's Basics of Law. Corpus Juris Civilis. M., 1997, p.153.

[8] Ibid.

[9] Ibid, p.156.

[10] V. G. Grafskii. Vseobshchaia istoriia prava i gosudarstva [The General History of Law and State]. Uchebnik dlia vuzov [Textbook for Institutes of Higher Education]. M., 2000, pp.285–291, 301.

[11] San Marino (state) // Cyril and Methodius's Megaencyclopedia (http://megabook.ru (13 June 2014)).

[12] *See*: The Statute of the Grand Duchy of Lithuania of 1529 (Extract) // Reading Book on History of the Country and Law (X century — 1917) /compiled by V.A.Tomsinov. M., 2004, pp.141–158.

the Republic of Lithuania states that the legal basis for the creation of Lithuania included the Statutes of the Grand Duchy of Lithuania and the Constitution of the Republic of Lithuania[13].

As it was mentioned above, the first legal instrument named as a constitution and which still exists nowadays is the US Constitution of 1787 (which entered in force after being adopted by states on 4 March 1789). The Great Sejm Constitution of 3 May 1791 and the French Constitution of 3 September 1791 can be considered the first written constitutions in Europe. Due to turbulent political conditions, these European Constitutions were in force for a short period of time. Anyway, active search for constitutional basics never ceased and continued at different stages of the Great French Revolution[14].

Modern religious conceptions of priority of divine basics of law and religious basics of law and order have existed for thousands years; such conceptions are, for example, widespread in some countries with the Muslim legal system as well as in Israel where the basics of law is Judaism regulations, and in Vatican where the law is connected with the basics of Catholicism.

Such inventions of the legal thought and modern law institutions aimed at determining and protecting the legislation core: constitutions, constitutional laws, constitutional control bodies (courts, councils, tribunals, committees, chambers, etc.), bodies of protecting human rights and fundamental freedoms have also had a long history during the evolution of law and the legal thought.

During its historical development, humanity has accumulated multiple models of making the activity of the state and its bodies within the legal framework, of forming the basics of constitutional and welfare state, dividing powers and neutralizing political monopolism and lawlessness.

During this time, experience of checks and balances regarding different state bodies in the context of various forms of ruling was gained. Firstly, the bicameral Parliament (bicameralism), and then the constitutional justice in its different forms appeared among the established checks against "parliamentary dictatorship"[15].

However, analyzing the oldest forms of ensuring hierarchy and protection of the rule of law and the whole legal system, it is necessary to note that they are closely connected with different ideas and concepts substantiating the unity and internal

[13] Constitution of the Republic of Lithuania //www3.lrs.lt/pls/inter3/dokpaieska.showdoc_l?p_id=275374 (2014, June 13).

[14] *See:* S.F. Udartsev. Iz istorii konstitutsionnoi evolutsii Frantsii [From the History of the French Constitutional Revolution] // Vestnik Altaiskoi akademii ekonomiki i prava [Herald of the Altai Academy of Economics and Law] Journal of Altai Academy of Economics and Law. Issue 1 (39). 2015, pp.89 — 95.

[15] V.D.Zor'kin. Konstitutsionno-pravovoe razvitie Rossii [The Constitutional Development of Russia]. M., 2011, p.144.

horizontal and vertical differentiation of the legal system. Legal consciousness, its doctrinal aspects, gradually became more and more important for ensuring the legal regulation, for maintaining and changing law institutions, for designing a more differentiated and hierarchical model of the legal system and its basics.

TAX COMPLIANCE IN A GLOBALIZED WORLD: A RUSSIAN PERSPECTIVE

Danil V. Vinnitsky
Professor, Doctor of Law,
Head of the Department of Tax and Financial Law
Ural State Law University

Denis A. Kurochkin
PhD Candidate, Lecturer at the Department of Tax and Financial Law
Ural State Law University

Abstract
The article is devoted to the issues of improving tax compliance in Russia. The tax gap leads to the loss of the planned revenues to the budgetary system; therefore, the Russian Federation, as many other countries, is trying to give an adequate forecast of the possible tax gap and minimize the amount of the falling out revenues. To decrease the tax gap it is necessary to adopt a complex of measures such as improving: (1) access to information needed by tax administrations, (2) exchange of information between tax administrations of different countries (3) cooperative compliance and risk management. Thus, at present Russian tax law includes both traditional and modern forms of tax control that need to be developed in the following directions: (1) providing for the expanded electronic documentation circulation between the tax administration and taxpayers, (2) reduction of time and material costs of the preparation and submission of tax returns to the tax administrations, etc. The plan "On Improving Tax Administration" adopted by Decree of the RF Government of 10 February 2014 No.162-r is aimed at the optimization of the system of tax administration and creating the atmosphere of comfortable communication with businesses. The effective elimination of the tax gap requires coordinated and consistent application of the abovementioned measures taking into account the economic situation and the actual capacity of certain categories of taxpayers in regard to paying taxes.

Keywords*:* tax compliance, tax gap, tax audit, transfer pricing, CFC-rules, voluntary disclosure programs, exchange of tax information, co-operative compliance ("horizontal monitoring"), risk management, tax administration.

1. Introduction: Tax Gap in the Russian Federation

Traditionally, the tax gap is understood as the difference between the tax that taxpayers should pay and what they actually pay on a timely basis. The tax gap measures the extent to which taxpayers do not file their tax returns and pay the

correct tax on time[1]. **Thus,** when determining the tax gap, the *amount of taxes* which have not been paid as a result of the application of tax preferential regimes provided for by tax legislation is not taken into account. In essence, the tax gap is the total arrears in regards to taxes in the case of a certain region, state, etc.

The tax gap leads to the loss of the planned revenues to the budgetary system, therefore the Russian Federation, as many other countries, is trying to give an adequate forecast of the possible tax gap and minimize the amount of the falling out revenues.

In general, in Russia the tax revenues, which are planned to be received, are included in the Law on budget (in regard to the respective financial year) on the basis of the information on the *"tax potential"* (i.e. information about amounts of taxes which hypothetically should be paid to the respective budget in accordance with tax legislation)[2]. In other words, the "tax potential" is understood as the correlation between the estimated (or calculated on the basis of the budgetary planning procedure) tax revenues per one "average taxpayer" which can be hypothetically received by the budget taking into account the level of the development of the region, the structure of the economy and the "estimated tax base"[3].

At the same time, the Federal Tax Service of Russia (***FTS***) estimates annually the level of tax expenses — the revenues falling out from the budgetary system, stipulated by the application of tax preferential regimes and other instruments (tax incentives) established by tax legislation of the Russian Federation. In particular, according to the reports of the RF FTS, from 2011 to 2013 the amount of tax expenses ("falling out revenues") of the budgetary system of the Russian Federation became 1.3 times higher (increased from 1,491,5 billion to 1,930,5 billion rubles)[4].

According to the general understanding, the tax gap (in contrast to tax expenses) can be divided into three components: (1) non-filing, (2) underreporting and (3) underpayment[5]. For instance, non-filing occurs when taxpayers who are required to file a return do not do so on time; underreporting of tax occurs when taxpayers

[1] See, for instance: https://www.irs.gov/uac/Understanding-the-Tax-Gap. International Revenue Service, USA (accessed 31 December 2016);
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/561312/HMRC-measuring-tax-gaps-2016.pdf. Revenue and Customs, UK (accessed 31 Dec. 2016); See also: N. Gemmella and J. Hasseldineb. The Tax Gap: A Methodological Review. Working Paper 09/2012. September 2012.

[2] The Tax Code of the Russian Federation, Art.41.

[3] The Budget Code of the Russian Federation, Art.131 (6), 137 (3), 138 (3), 142.1 (4), 142.8(4).

[4] The main priorities of the tax policy of the Russian Federation for 2016 and for the planned period of 2017 and 2018, Art.4.

[5] E.Toder. What is the Tax Gap? Tax Analysts: Current and Quotable. 2007. http://www.urban.org/sites/default/files/alfresco/publication-pdfs/1001112-What-is-the-Tax-Gap-.PDF (accessed 31 Dec. 2016); IRS Releases New Tax Gap Estimates; Compliance Rates Remain Statistically Unchanged From Previous Study: https://www.irs.gov/uac/irs-releases-new-tax-gap-estimates-compliance-

either understate their income or overstate their deductions, exemptions and credits on timely filed returns; underpayment occurs when taxpayers file their returns but fail to remit the amount due by the payment due date[6]. However, the RF FTS uses other classifications of cases connected with tax gap ("tax indebtedness"):

The Structure of indebtedness in regard to the budgetary system of the Russian Federation (according to the RF FTS database)[7]

Type of indebtedness	**On 01.01.2014, RUB, billions**	**On 01.01.2015, RUB, billions**	**On 01.12.2015, RUB, billions**	**Changes since the beginning of the fiscal year**	
				%	**+/-, RUB, billions**
Total indebtedness in regard to the budgetary system of the Russian Federation (including default interest and tax sanctions)	1 155,2	1 181,5	1 217,5	103,0	35,9
Unsettled indebtedness	583,3	640,6	692,6	108,1	52,0
Not subject to recovery by tax authorities	572,0	540,9	524,8	97,0	-16,0
Deferred or restructured indebtedness	18,8	18,5	19,6	106,0	1,1
To be received through law-enforcement procedure	164,8	166,3	162,2	97,5	-4,1
Suspended amounts of taxes according to the decisions of the courts or a superior tax authority	54,3	55,3	56,2	101,6	0,9
Suspended recovery due to bankruptcy	326,7	288,9	278,3	96,3	-10,7
Bad indebtedness (has to be written off by tax authorities)	11,0	14,7	11,1	75,5	-3,

It is quite interesting that in 2011 the Tax Justice Network prepared the rating of the countries in regard to the losses in tax revenues as a result of tax evasion or avoidance: Russia is in the 4th line of this rating (after the USA, Brazil and Italy)[8].

rates-remain-statistically-unchanged-from-previous-study. International Revenue Service, USA (accessed 31 Dec. 2016).

[6] See for instance: https://www.irs.gov/uac/Understanding-the-Tax-Gap (International Revenue Service, USA), See also: Tax Administration Reform and Fiscal Adjustment: The Case of Indonesia, John Brondolo, Frank Bosch, Mr. Eric Le Borgne, Mr. Carlos Silvani (2008).

[7] See: the official statistic of the RF Federal Tax Service: http://analytic.nalog.ru/portal/index.ru-RU.htm (accessed 31 Dec. 2016).

[8] A Briefing Paper on the Cost of Tax Evasion Worldwide, Chapter 3: http://www.taxjustice.net/wp-content/uploads/2014/04/Cost-of-Tax-Abuse-TJN-2011.pdf (accessed 31 Dec. 2016).

The growth of the tax gap in Russia is connected with a number of factors. But, perhaps, the problem of so-called "one-day companies" is especially essentially important for the country; in our opinion, it is one of the main reasons of the gap between the tax revenues planned and tax revenues received (at least, for the last 15 years). For instance, the damage for the budget system as a result of the transactions with the participation of "one-day companies" is estimated approximately as 30% of the total of dubious transactions — more than 450 billion RUB a year[9].

In order to settle the above-mentioned problem, the RF FTS approved a list of typical characteristics of the transactions with a "one-day company" (see: Supplement No.2 to Order of the RF FTS of 30 May 2007 No.MM-3-06/333@)[10].

The attention of the tax inspectors in Russia is also attracted by such facts as the registration of the contractor of a taxpayer with the "*address of mass of registration*"[11], the forced liquidation of a legal entity (which was the contractor of a taxpayer). See: Letters of the RF Ministry of Finance of 19 March 2010 No.03-02-07/1-118 and of 16 March 2010 No.03-02-07/1-110.

Another reason for the tax gap in the Russian Federation is tax evasion of VAT and tax on the profits of organizations. For instance, in 2010 the additional amount of VAT and of the respective default interest accounted for 133.5 billion RUB or 42.8% of the total amount of additionally received payment in the framework of the law-enforcement procedure[12]. (It is important to understand that the share of the revenues for the budget from the given taxes is quite significant and in 2015 it accounted for more than 1/3 of the total revenues — 17% (VAT) and 19% (tax on the profits of organizations))[13]. Taking into account that the tax bases in regard to VAT and tax on profits are computed following from the amount of proceeds / incomes of a company, the usual schemes of illegal evasion in regard to these taxes are relatively similar or comparable.

---

[9] See: The interview with S. M. Ignatiev, the ex-head of the Russian Central Bank: http://www.nalog-briz.ru/2013/04/blog-post_5.html (accessed 31 Dec. 2016).

[10] Here we can see some of these characteristics: *"— the absence of personal contacts of the heads of the supplying company and the buying company when discussing the terms of delivery and signing a contract; — the absence of the documentary confirmation of the authorities of the head of a contracting company, the absence of the copies of the document identifying his personality; — the absence of the documentary confirmation of the authorities of the representative of the contractor and the copies of the document identifying his personality; — the absence of the information about the actual location of the contractor and also about the location of the warehouse and/or manufacturing and/or trade premises, etc.".*

[11] "Address of mass registration" — a significant number of companies have indicated the same address as the address of their permanent office.

[12] M. O. Chirkov. Innovative Approaches to the Development of the Models of Taxpayers' behavior, Izvestiya. Altaiskiy State University, 2012, No.2-1(74), P.350.

[13] See: http://analytic.nalog.ru/portal/index.ru-RU.htm (accessed 31 Dec. 2016).

Another important reason of the tax gap in the Russian Federation is connected with the withdrawal of capital to offshore jurisdictions and, in particular, tax evasion or avoidance in cross-border situations. The Russian legislator is trying to solve these issues using the OECD and G20 recommendations, including some aspects connected with the BEPS Action Plan. For instance, in recent years (1) new transfer pricing rules (Section V.1 of the RF Tax Code), (2) new rules on the residence of organizations / companies (Art.246.2 of the RF Tax Code) and, finally, (3) the first rules on controlled foreign corporations (Chapter 3.4 of the RF Tax Code) were implemented in Russian tax legislation.

2. Improving access to information needed by tax administrations

2.1. Access to information in the framework of tax audit and tax monitoring

From procedural point of view, in most cases the need in access to tax information arises in the framework of the following procedures: (1) on-site tax audit; (2) off-site tax audit and (3) tax monitoring (in the framework of enhanced tax relations with big companies).

The RF Tax Code provides for a wide scale of legal instruments for receiving tax information — requests for documents, interrogation of witnesses, requests of clarifications, expert appraisals, etc. (see: Articles 90 — 95 of the RF Tax Code).

Off-site tax audit is conducted on the basis of tax declarations and the documents submitted by taxpayer and also other documents on the taxpayer's activities which are at the disposal of tax administration (Article 88 (1) of the RF Tax Code). In case of any contradictions in the information or in the documents submitted by a taxpayer, the tax administration may request the necessary clarifications from the taxpayer (Article 88 (4) of the RF Tax Code). Also, in a number of cases, the tax administration has a right to request from the taxpayers the documents concerning the right to apply a tax benefit and deductions (Article 88 (6 and 8) of the RF Tax Code), etc.

In the framework of the **On-site tax audit** a wide complex of the measures of tax control may be undertaken, in particular, requests for any relevant documents, interrogation of witnesses, clarifications, expert appraisals, etc. (see: Articles 90 — 95 of the RF Tax Code).

From the perspective of the information which is necessary for exercising tax audit, the activities of the so called "one-day companies" deserve special attention. Therefore and for the purposes of identifying "one-day companies", the priority is given to the creation of the database of persons who perform as nominal directors of different organizations in the same period of time, of the addresses of "mass registration" of organizations, of dubious contractors, etc. The information on the methods of conducting financial and economic activities with a high tax risk is placed

on the official web-page of the RF FTS — "www.nalog.ru" in the section *"Criteria available for independent estimate of risks"*.

From the perspective of receiving tax information it is essentially important that the RF Tax Code provides for the obligation of third parties (tax agents, contractors, banks, different state authorities) to submit tax information to the tax administration.

In particular, Article 85 of the RF Tax Code has established the obligation of the bodies conducting migration and cadastre records, other bodies and organizations to communicate the information concerning the records of organizations and individuals to the tax administration. Banks are also obligated to give the information concerning the taxpayers' records to the tax administration (Articles 85.1 and 86 of the RF Tax Code).

Besides, according to Article 93 (1) of the RF Tax Code, a tax official conducting a tax inspection has a right to demand the documents or information which a contractor or other persons may have at their disposal and which concern the activities of the taxpayer being inspected.

All the above-mentioned subjects (see: Articles 85 — 86, 93 (1) of the RF Tax Code) do not have a right to reject the submission of the information requested referring to the banking or another secret protected by law (see: Article 93.1 (6)). The exception from this rule is the information representing attorney-client privilege and auditing secrecy[14].

Besides, the tax administration has a right to request from attorneys and attorney associations the information, which is necessary to evaluate the tax consequences of the transactions concluded with the clients. At the same time, this information should be regarded as tax secrecy and should be protected from the further disclosure by virtue of law (Article 102 of the RF Tax Code). As for the information connected with the content of the legal assistance provided by an attorney, the tax administration may not demand to submit it in the light of the constitutionally significant principles of attorney activities (see: the RF Constitutional Court, Decision of 6 March 2008 No.449-O-P).

2.2. Access to information and tax databases

Significant assistance in collecting and using the information important for a taxpayer is given by services of the RF FTS: *"Business risks: check yourself and your contractor"*, *"The real identification tax number (ITN) of legal persons"*, *"Invalid certifications"*, *"Invalid ITN of individuals"*, *"Invalid ITN of legal persons"*, *"Open and accessible information on foreign organizations"*, etc.[15]

[14] The Tax Code of the Russian Federation, Art.82(4).

[15] https://www.nalog.ru/rn66/about_fts/el_usl/ (accessed 31 Dec. 2016).

The given information is especially effective in regard to tax control of VAT payments. Considering the developed case law of the RF Supreme Court a taxpayer has to check the information about his contractors and be in any other way properly careful when choosing his contractors. Thus, the check of the supplier's legal capacity by obtaining the information from the RF FTS web-page can be considered to be the evidence of the taxpayer's being properly circumspect when concluding a transaction (under the condition that the taxpayer did not have any grounds to doubt the supplier's compliance with tax legislation, etc.)[16].

2.3. Payments of tax and monitoring of the financial flows

In principle, different means of payment, both cash and bank transfers may be used in Russia to pay taxes. However, according to Article 6 of Directive of the Bank of Russia of 7 October 2013 No.3073-Y "On Exercising Cash Settlements", the cash settlements in regard to one transaction between the same persons are limited by the amount of 100.000 RUB which allows to monitor the financial flows in financial institutions.

Besides, Russian legislation provides (indirectly) for tax payments in the electronic form. For instance, in case of the taxpayer's non-compliance the debts in taxes can be enforced to be collected from the taxpayer's funds of electronic money / "electronic monetary surrogates" (see: Articles 46, 48 of the RF Tax Code). The regime of using and transferring electronic funds is determined in Federal Law of 27 June 2011 No.161-FZ "On the National Payment System".

2.4. Voluntary disclosure programs

In recent years, the attempts to conduct the so-called amnesty of capital have been undertaken in Russia: in case of disclosing by individuals the information about the property owned, the bank accounts opened and the foreign companies controlled they can be relieved from criminal, administrative and tax sanctions for the violations connected with such activities[17]. However, according to the RF FTS's statement, the process of the amnesty of capital is going quite slowly and is not up to the results planned and expected[18].

Russian tax legislation does not have any special voluntary disclosure program in place but certain features of voluntary disclosure programs can be found in the special forms of tax control — tax monitoring and transfer pricing procedures.

[16] Rulings of the Presidium of the Supreme Commercial Court of the Russian Federation of 20 April 2010 No.18162/09 in case No.A11-1066/2009, of 1 February 2011 No.10230/10 in case No.A57-22072/2009, of 19 April 2011 No.17648/10 in case No.A26-11225/2009.

[17] *See*: Federal Law of 8 June 2015 No.140-FZ "On Voluntary Declaration by Individuals of the Assets and Accounts in the Banks and on the Amendments of Certain Legislative Acts of the Russian Federation".

[18] See: http://ppt.ru/news/134528 (accessed 31 Dec. 2016).

Thus, in case of tax monitoring the information interaction is provided by the regulation which shall include the procedure of submitting to the tax administration the documents which are the grounds to calculate taxes and (or) of the access to the databases of the organizations which possess the given documents (see: Article 105.26 (6) of the RF Tax Code). On the basis of the obtained information in the framework of tax monitoring, the tax administration prepares a motivated opinion in case the fact is established which proves wrong calculation or untimely payment of taxes by a taxpayer (Articles 105.29 — 105.30 of the RF Tax Code). The taxpayer's compliance with the motivated opinion of the tax administration sent to him in the course of tax monitoring excludes taxpayer's guilt in committing a tax law violation (Article 111 (1 (3)) of the RF Tax Code).

In addition, the tax administration and the taxpayer may conclude an agreement on pricing — the order of setting prices and applying the methods of pricing in the intra-group transactions for taxation purpose (Article 105.19 of the RF Tax Code). In case the taxpayer complies with all the terms of the pricing agreement, the RF FTS has no right to take a decision on sanctions for committing a tax infringement which involves additional calculation of taxes in regard to those controlled transactions the prices on which have been agreed upon in the pricing agreement (Article 105.23(2) of the RF Tax Code).

2.5. Disclosure programs and CFC Rules

The RF Tax Code also provides for the obligation of disclosure of the certain information according to the Controlled Foreign Corporation (CFC) rules.

Besides, residents of the Russian Federation have to notify the tax administration at the place of their residence / incorporation (see: Articles 23 (3.1), 25.12 (1, 2 and 4) of the RF Tax Code):

— about their participation in foreign organizations (if the share of such participation exceeds 10%);

— about establishing foreign structures and also about the control over them (including the cases when an individual acts as a founder of such a structure or as a person who is the beneficial owner of the income);

— about the controlled foreign organizations in regard to which they are controlling persons.

Thus, it is supposed to identify whether residents of the Russian Federation/ companies incorporated in Russia are beneficiaries of the incomes received from the sources outside Russia. Moreover, the tax administration may obtain the information about the participation of an individual in a foreign organization or its control by this individual from other sources (DTCs, Multilateral convention, etc.).

The introduction of state register of beneficiaries is not planned in Russia at the moment[19].

2.6. Transfer pricing

In accordance with Federal Law of 18 July 2011 No.227-FZ (effective since January 1, 2012) the new transfer pricing rules were introduced in the RF Tax Code (see: Section V.1). Though, on the whole, Russian legislation on transfer pricing corresponds to the general approaches of the OECD, there are significant peculiarities stipulated. In particular, currently the Russian legislation establishes the requirements to submit the documents on the sections relevant to "*local file*"[20] *(the terminology of Action 13 BEPS Plan). By virtue of Article 105.15(1) of the RF Tax Code, a taxpayer is obliged to submit the documents concerning a particular transaction (a group of homogeneous transactions) mentioned in the request for documents sent by the tax administration.*

At the same time, in practice the tax administration widely applies the clarifications of the RF FTS described in Letter of 30 August 2012 No.OA-4-13/14433@ "On Preparation and Submission of Documents for Tax Audit Purposes". In Supplement I of the given Letter of the RF FTS, there are partially the sections which correspond in their terminology to Action 13 BEPS Plan, to the sections reflected in the "master file"[21].

Thus, all the information recommended to the obligatory inclusion in the taxpayer's documentation on transfer pricing, by virtue of the provisions of Article 105.15 of the RF Tax Code, is also established in the provisions on "local file" and "master file" Action 13 BEPS Plan. However, not all the information subject to disclosure in accordance with Action 13 BEPS Plan, and also the relevant sections of the Country-by-Country Report[22] are contained in the Russian national recommendations on transfer pricing (e.g. there is no information on all the

[19] http://izvestia.ru/news/626520 (accessed 31 Dec. 2016).

[20] The local file focuses on information relevant to the transfer pricing analysis related to transactions taking place between a local country affiliate and associated enterprises in different countries and which are material in the context of the local country's tax system (Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 — 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, page 15).

[21] The master file should provide an overview of the MNE group business, including the nature of its global business operation, its overall transfer pricing policies, and its global allocation of income and economic activity in order to assist tax administrations in evaluating the presence of significant transfer pricing risk. See: Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 — 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, page 14.

[22] The Country-by-Country Report requires aggregate tax jurisdiction-wide information relating to the global allocation of the income, the taxes paid, and certain indicators of the location of economic activity among tax jurisdictions in which the MNE group operates. See: Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 — 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, page 16.

significant intra-group agreements on pricing, the description of the business of multinational corporations, etc.).

In particular, all MNE groups are required to file the Country-by-Country Report each year except as follows. There would be an exemption from the general filing requirement for MNE groups with annual consolidated group revenue in the immediately preceding fiscal year of less than EUR 750 million or a near equivalent amount in domestic currency as of January 2015[23]. Meanwhile, according to RBC analytical service[24], at the moment of conducting the analysis of multinational corporations, there were only about 143 corporations with the consolidated group revenue over EUR 750 million.

3. Exchange of information between tax administrations of different countries

3.1. Bilateral tax treaties and multilateral conventions

The participation of the Russian Federation in the international exchange of tax information is based on bilateral tax treaties and the multilateral convention — Convention on Mutual Administrative Assistance in Tax Matters[25].

However, no bilateral tax treaty concluded by the Russian Federation provides for the obligations for automatic or spontaneous exchange of tax information. At the same time, the ratification of the Convention on Mutual Administrative Assistance in Tax Matters creates the preconditions for such forms of information exchange. In particular, the Russian Federation is planning to start the automatic exchange of tax information according to Common Reporting Standard since 2018[26]. In May 2016, Russia signed the Multilateral Agreement on automatic exchange of information[27].

As for the exchange of tax information upon request, it is carried out quite intensively. According to the report of the Global Forum[28] which completed both phases of Peer Review on Russia, in the period from July 2010 to June 2013 (three years) the Russian tax administrations received and processed 7,945 requests of granting tax information and received about 100 messages containing the information in the framework of spontaneous exchange. Moreover, if to judge by

[23] Transfer Pricing Documentation and Country-by-Country Reporting, Action 13 — 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, page 21.

[24] See: http://www.rbc.ru/companies/id/21 (accessed 31 Dec. 2016).

[25] See: http://www.oecd.org/ctp/exchange-of-tax-information/Status_of_convention.pdf (accessed on 31 Dec. 2016).

[26] Ready for exchange: Russian banks will disclose the data on European clients // Rossiyskaia Business-Gazeta, No.996 (17): http://www.rg.ru/2015/05/05/fatca.html (accessed 31 Dec. 2016).

[27] http://www.rbc.ru/economics/12/05/2016/5734586b9a794759cbe87589 (accessed 31 Dec. 2016).

[28] OECD. (2014), Global Forum on Transparency and Exchange of Information for Tax Purposes Peer Reviews: Russian Federation 2014: Phase 2: Implementation of the Standard in Practice, OECD Publishing, Paris.
DOI: http://dx.doi.org/10.1787/9789264223103-en (accessed 31 Dec. 2016).

the emerging commercial courts case-law, which contains references to the evidence received in the framework of information exchange, it has really been increasing in recent years.

The negotiations on concluding double tax treaties is based (from the Russian side) on the National Model approved of by the RF Government in February 2010[29]. If to compare the content of Article 26 of the National Model with Article 26 of the OECD Model, it is possible to conclude that they fully correspond to each other. Thus, in the current situation Russia is oriented at concluding treaties taking into account the existing the OECD standard on the exchange of tax information. As for the previously concluded Russian treaties, the significant part of them does not correspond to the present version of Article 26 of the OECD Model (in particular, from the perspective of Article 26 (3) and Article 26 (4) of the OECD Model)[30]. However, the treaties which have been concluded in the 1990s are being "modernized"; as an example it is possible to mention the new protocol to the treaty between the Russian Federation and the Chinese People's Republic[31], and also the Protocol to the treaty between the Russian Federation and Cyprus[32].

So far, Russia has not concluded any agreements according to the TIEA Model; at the same time, there is a Model on exchange of tax information adopted by the Government of the Russian Federation[33] which *de facto* is the translation of the respective OECD Model. It is also necessary to point out that there is a number of treaties on exchange of information concluded with some CIS countries and they contain significant deviations from the above-mentioned Model. However, the given treaties are, in essence, quite declarative.

3.2. FATCA and issues of reciprocity ("Russian FATCA rules")

As for concluding the agreement with the USA on FATCA, Russia was conducting the negotiations on it; it was supposed to be concluded according to the 1IGA Model but the parties did not reach the point of signing it. At present, Russian financial institutions are being registered for submitting the information

[29] Decree of the Government of the Russian Federation of 24 February 2010 No.84 "On Concluding Interstate Agreements on Avoidance of Double Taxation and Prevention of Tax Evasion in Regard to the Taxes on Income and Property (revised and amended in 2012 and 2014)".

[30] See Russian Federation treaties: http://www.eoi-tax.org/jurisdictions/RU#agreements (accessed on 31 Dec. 2016).

[31] The Treaty between the Government of the Russian Federation and the Government of the Chinese People's Republic (concluded in Moscow on 13 October 2014).

[32] The Protocol of 7 October 2010 "On Introducing Changes in the Treaty between the Government of the Russian Federation and the Government of the Republic of Cyprus on Double Tax Avoidance in Regard to Taxes on Income and Capital of 5 December 1998".

[33] Ruling of the Government of the Russian Federation of 14 August 2014 No.805 "On Concluding Treaties on the Exchange of Information on Tax Matters".

to the IRS in the framework of the FATCA initiative (more than 1,300 Russian banks, stock exchange companies and other financial institutions have already been registered). When submitting tax information to the IRS, financial institutions should notify Russian tax administrations about that and also have to receive the client's consent for information transfer/submission. If a client does not give the consent, the respective financial institution receives a right to unilaterally terminate the relations with such a client (see: Federal Laws of 5 May 2014 No.112-FZ and of 28 June 2014 No.173-FZ).

Simultaneously, taking into account the reciprocity principle, the Russian Federation introduced the obligation for foreign financial organizations to provide the Russian tax administration with the information about the bank accounts of Russian citizens and legal entities (e.g. companies) controlled by Russian citizens. This obligation is provided for by Article 6 of the Federal Law No.173-FZ and is usually called "Russian FATCA". Though in December 2015, the Russian Federal Tax Service published forms for reporting under "Russian FATCA", it is still not entirely clear how "Russian FATCA" will work. Namely, (1) so far no electronic reporting is available; (2) it is not clear how foreign financial institutions should disclose the client's information if such disclosure is prohibited by their national legislation (however, the same issue is relevant for the FATCA rules introduced by the US); (3) sanctions for non-compliance with "Russian FATCA" are not yet established, etc.

Reports (in the framework of the Russian FATCA System) are to be filed with Russian tax authorities annually before 30 September of the year following the year of the accounts' opening. Reporting forms were approved by the Order of the Federal Tax Service No.MMB-7-14/501@ (effective from 18 December 2015), however, so far, no clarifications regarding completion of the forms were published.

As it was mentioned above, since 2018 Russia may start participating in CRS (Common Reporting Standard); CRS provides for more developed and elaborated system for exchange of tax information, thus, we can suppose that if Russia takes part in CRS, "Russian FATCA" will lose practical value. Some representatives of the Russian tax administration even do not exclude that when Russia becomes involved in exchange of information under CRS, Article 6 of the Federal Law No.173-FZ of 28 June 2014 will be abolished[34], or will be applicable only in regard to countries, which are not members of the CRS system.

[34] *See*: Materials of the Meeting (of 28 April 2016) of the Association of Russian Banks and of the Federal Tax Service of Russia regarding "Russian FATCA" (the representative of the RF Federal Tax Service was Dmitry Volvach, head of Standards and International Cooperation Department of the RF FTC).

3.3. Organizational and technical issues

It is important to conclude that most of the issues existing in the sphere of exchange of tax information (also mentioned in the Report of the Global Forum) have not so many legal reasons but rather organizational and technical ones (for instance, there were cases when Russian competent authorities submitted in reply to the request the copies of the documents in Russian without any explanation what kind of documents they are and what they contain)[35]. Perhaps, the reason for the above-mentioned may be connected with the large volume of cases.

As for joint audits, the possibility of conducting them is provided for by the Convention on Mutual Administrative Assistance in Tax Matters[36], ratified by the Russian Federation, however, so far, there is no information about any practice of implementation of the given document. One of the reasons is the absence of regulation of the legal status of representatives of the foreign tax administration on the territory of the Russian Federation, in particular, in the course of a tax audit. In accordance with the RF Tax Code, these persons just cannot be admitted to the materials of the tax audit, at least, because of the effective rules on tax secrecy (however, there are projects of federal laws which have to eliminate the given lacuna).

4. Co-operative compliance and risk management

4.1. Co-operative compliance ("Horizontal monitoring")

Horizontal monitoring is actively used in international practice and now is the element of the Russian tax system (see: Section V.2 of the RF Tax Code). The first agreements on horizontal monitoring were signed in Russia at the end of 2012. In particular, on 25 December 2012 the agreements on expanded information interaction — horizontal monitoring were signed between the RF FTS and a number of companies: OAO "*Rusgidro*", OAO "*INTER RAO EEC*", OAO "*Mobile TeleSystems*", "*Ernst and Yang (CIS) B. V.*"[37].

The advantages of using horizontal monitoring for taxpayers are that tax inspectors having a chance to control income and expenses records for taxation purposes in "real time" (e. g., in the accounting database of the company) cannot conduct On-site or Off-site tax audit during the period of horizontal monitoring (see: Articles 88(1.1) and 89(5.1) of the RF Tax Code). Consequently, the mistakes identified by tax administrations may be corrected nearly immediately.

[35] P.68, OECD (2014), Global Forum on Transparency and Exchange of Information for Tax Purposes Peer Reviews: Russian Federation 2014: Phase 2: Implementation of the Standard in Practice, OECD Publishing, Paris. DOI: http://dx.doi.org/10.1787/9789264223103-en (accessed 31 Dec. 2016).

[36] Federal Law of 4 November 2014 No.325-FZ "On the Ratification of the Convention on Mutual Administrative Assistance in Tax Matters".

[37] Pepelyaev S., Zaripov V. The Rating of Tax Events of 2012: from the Practitioners' Perspective, *Property relations in the RF*. 2013. No.4.

Besides, such interaction allows the tax administration to warn the respective taxpayer about tax risks and grant the tax administration's motivated opinion on specific matters upon the request of the company (see: Article 105.30 of the RF TC). Thus, the horizontal monitoring guarantees the taxpayer no extra taxes and default interest even if later the company has indebtedness as a result of following this opinion (Articles 75 (8), 111 (3.1) of the RF Tax Code).

In case of a taxpayer's disagreement with the opinion of the tax administration, a procedure of mutual agreement should be initiated in accordance with the RF FTS (see: Article 105.31 of the RF Tax Code). Thus, the horizontal monitoring (according to Russian tax legislation) supposes the following advantages for taxpayers: (1) decrease of tax risks for the taxpayer; (2) possibility to be relieved from some measures of tax control / audit; (3) possibility to be informed on the RF FTS position on planning transactions in advance, that decreasing uncertainty in application of tax laws.

4.2. Risk management

The risk management is also used in the planning of tax audit. In particular, an important point in planning On-site tax audit is the criteria of the taxpayers' independent risk appraisal provided for in Section 4 of the "Conception of the planning system of On-site tax inspections[38]. For instance, as a risk for the taxpayer the following facts should be qualified: (1) the entry of losses into the bookkeeping and tax records during several tax periods; (2) the entry of the significant amounts of tax deductions into tax returns during a certain period; (3) building financial and economic activities on the basis of contracts only with intermediaries ("chains of contractors") without any reasonable economic or business purpose; (4) the taxpayer's repeated striking of the register and getting registered again with tax administrations in connection with the changes of location ("migration" between tax administrations); (5) significant deviation of the profitability level according to the accounting data from the profitability level for the given sphere activity according to statistical information.

Besides, as it has been mentioned above, the information about the methods of conducting financial and economic activities with a high tax risk is placed on the official web-page of the RF FTS (www.nalog.ru) in the Section "Criteria available for the independent risk appraisal".

4.3. Constitutional issuers

The horizontal tax monitoring provided for in the RF Tax Code can hypothetically lead to conflicts with the principles of tax law and constitutional law, which are connected with *the possibility to apply tax monitoring only by the taxpayers with a*

[38] Adopted by Ruling of the RF FTS of 30 May 2007 No.MM-3-06-/333@.

high level of incomes and the significant value of assets (Article 105.26 (3) of the RF Tax Code), as a result the rights of other taxpayers, including the representatives of small and medium size business, will get discriminated (see: Article 3 (3) of the RF Tax Code).

Besides, the RF Tax Code is uncertain in regard to the remedies to defend the taxpayer's rights in the course of horizontal monitoring. In particular, it not formally provided for that the taxpayer can go to court to appeal the "motivated opinion" of the tax administration (Article 105.30 of the RF Tax Code) and the notification of leaving the motivated opinion without changes adopted in the result of the mutual agreement procedure (Article 105.31 of the RF Tax Code).

5. Challenges ahead

5.1. Further steps

To decrease the tax gap it is necessary to adopt a complex of measures which have to solve the problem at the domestic and foreign markets.

The plan "On Improving Tax Administration" adopted by Decree of the RF Government of 10 February 2014 No.162-r is aimed at the optimization of the system of tax administration and creating the atmosphere of comfortable communication with businesses. According to the Plan (Section I "General Description"), the following directions of improving tax administration are provided for: (1) reduction of time and expenses of businessmen on tax compliance and payment of taxes; (2) improvement of interrelations between taxpayers and tax administrations taking into account the best international practices; (3) harmonization of the rules of tax documentation and accounting rules; (4) increased effectiveness of VAT administration; (5) encouraging the application of electronic documentation by taxpayers and tax administrations; (6) improvement of administration of special tax regimes applied by certain categories of taxpayers. The effective elimination of the tax gap requires coordinated and consistent application of the abovementioned measures taking into account the economic situation and the actual capacity of certain categories of taxpayers in regard to paying taxes.

5.2. National Roadmap "Improving Tax Administration"

In 2014, the Roadmap "Improving Tax Administration" (the Ruling of the RF Government of 10 February 2014 No.162-r) was developed and it focused, in particular, on the following tasks;

(1) — providing for the expanded electronic documentation circulation between the tax administration and taxpayers,

(2) — reduction of time and material costs of the preparation and submission of tax returns to the tax administrations;

(3) — improving tax compliance in cross-border situations (see: section 2 — 3 of the Report).

In the course of the implementation of the Roadmap, a complex of other significant measures has already been completed[39].

5.3. Eurasian Economic Union

Special taxation rules are provided for in the Treaty on the Eurasian Economic Union (EAEU) (signed in Astana, on 29 May 2014). Section XVII of the Treaty regulates the principles of collection of indirect taxes in cross-border situations arising in the EAEU.

It is important that the exchange of information between the tax administrations of the EAEU Member States necessary for securing the full payment of indirect taxes, is carried out in accordance with a special international treaty which also establishes the procedure of the information exchange, the application form on imports of goods and payment of indirect taxes, etc. (see: Article 72 (3) of the Treaty on the EAEU).

Article 73 of the above-mentioned Treaty establishes the peculiarities of the collection of taxes on incomes of individuals in cross-border situations. In particular, in case "*one Member State in accordance with its legislation and international treaties has a right to tax the income of the tax resident of the other Member State in connection with the employment conducted in the first mentioned Member State such income is taxed in the first Member State since the first day of employment at the tax rates provided for such incomes for tax residents of this first Member State*". We may expect further development of the peculiarities of tax compliance rules in the EAEU in the spheres of indirect taxation (the new Customs Code of the EAEU should be introduced in 2017).

[39] It is necessary to mention, in particular, the following laws and regulations:
(1) — Federal law of 29 November 2014 No.382-FZ *established the rights to accept for deduction of VAT in regard to the invoices received before the deadline for submitting VAT return* (taking into account the given amendment, the invoices, also in e-form, received before the moment of submitting the tax return may be recorded in that tax period in which economic operations have been conducted);
(2) — Letter of the RF Ministry of Finances of 27 July 2015 No.03-03-05/4297 allowed *to take into account for tax purposes the original documents in regard to on-going services with a later date than the end of the report period* (the clarification is sent in letter of the RF FTS of 21 August 2015 No.GD-4-3/14815 through the system of tax administrations) (it will allow to use a uniform procedure of taking into account late invoices and the original documents, in particular, acts on providing services);
(3) — The RF Ministry of finances clarified in Letter of 28 August 2014 No.03-03-10/43034 that *minor mistakes in the original documents do not lead to the refusal in recognizing the expenses* which also reduces unnecessary risks in the work of businessmen;
(4) — The RF Ministry of Culture defined the main rules of storing electronic documents (see: Order of 31 March 2015 No.526) (the given procedure includes accounting and tax documents, see: the Clarification of the RF Ministry of finances PZ-12/2015 of 11 September 2015).

5.4. Territorial approach in tax administration vs. "branch principle"

The improvement of the procedures of tax administration is also achieved through organizing the system of tax administrations according to the "branch principle" when tax audit is conducted in respect of the taxpayers of the certain industry (area of economic activities). **Thus,** in 2004, the Russian authorities introduced tax administration of the major taxpayers at the federal level in the interregional inspections of the RF FTS specialized according to the "branch principle" and at the regional level — in the *specialized inter-district inspections* of the RF FTS[40] (As the RF Constitutional Court held, the Russian government has to determine the system of tax authorities and their "specialization" taking into account certain management tasks, the feasibility and cost-effectiveness[41]). However, it is not evident to what extent the "branch principle" may be applicable in cross-border situations (for instance, in regard to the permanent establishments or controlled companies established by non-residents)

[40] P. 2 of the Order of the MTC of 16 April 2004 No.SAE-3-30/290@

[41] RU: RFCC, 13 January 2000, case No.10-O.

SPECIAL ECONOMIC ZONES IN THE RUSSIAN FEDERATION

Ilya A. Rakov
Lecturer at the Department of Tax and Financial Law,
Ural State Law University, Researcher at the BRICS Law Institute

Abstract
This article provides a focused review of special economic / tax zones legal regime in the Russian Federation. In particular, the author describes the Russian domestic special tax zones regulations, the aims for establishing special economic zones and their possible types. The article also analyses the issues of similarities and differences between the concepts of "tax haven" and "special zones".

Keywords: tax law, special tax zones, special economic zones, tax havens, BEPS.

Tax incentives have been the focus of work by international organizations (IOs) for many years[1]. Some kind of them are known as ***special tax or economic zones (STZ).*** The concept of a special tax zone applies to areas where tax regulations are more beneficial than in the generally applicable tax system of the surrounding jurisdiction or country[2].

Under the conditions of implementing the Base Erosion and Profit Shifting Action Plan (BEPS Action Plan), special economic zones are becoming the focus of attention especially in regard to the assessment of the tax regime which they provide for their residents[3].

As referred to in the report to the G-20 Development working group by the IMF, OECD, UN and World Bank "Supporting the Development of More Effective Tax Systems", striking the right balance between an attractive tax regime for domestic and foreign investment, by using tax incentives, for example, and securing the necessary revenues for public spending, is a key policy dilemma. Competition between developing countries for investment can trigger a race to the bottom[4].

---

1 http://www.oecd.org/tax/tax-global/options-for-low-income-countries-effective-and-efficient-use-of-tax-incentives-for-investment-call-for-input.pdf

2 A. Laukkanen. The Development Aspects of Special Tax Zones // 70 Bull. Intl. Taxn. 3 (2016), Journals IBFD.

3 Based on the Final Summary of the Discussion on the Results of the Meeting of the Coordination Committee of the BRICS Law Institute and of the Expert Group on Legal Support to Inter-State Partnership and Integration on Economics, Finance, Taxation and Customs (9-10 June 2016, Yekaterinburg, Russia)// p.3, http://eurasiatax.com/files/Summary.pdf

4 https://www.imf.org/external/np/g20/pdf/110311.pdf

Of course, the risk is recognized that they (special economic zones) may be used in harmful tax competition of jurisdictions and may be used for tax evasion /avoidance in cross-border situations in contradiction to the growing participation or commitment of jurisdictions to automatic exchange of tax information[5].

Nevertheless, STZs and tax havens are different from each other. As resulted from the Collaborative Research[6], the distinction between tax havens and STZs has to be obvious. Despite the main attraction of the STZs, reduced or abolished corporate income taxation and VAT, all other tax haven connotations should be tackled, for example, by providing completely transparent business environment, companies with substantial activity and solid information flow from STZs to foreign tax authorities. In that context, Yariv Brauner (2013) identifies three basic categories of tax incentives: 1) rate reducing, 2) tax base eroding and 3) special zones[7].

1. Special economic zones vs. "tax havens"

According to the Russian domestic legislation, foreign "tax havens" and domestic "special economic (tax) zones" are clearly different legal institutes. At the same time, we can see some similarities in the approaches of the federal legislator to the regulation of tax audit (e.g. in connection with the transfer pricing rules)[8]. The reasons are:

a) reduced rates of taxation: 0% property tax, land tax, tax on transportation;

b) exemption from taxation for a certain period: profit tax/ there are preferential tax rates on profit for residents, including federal tax they make:

— 2% the first five years;

— 7% the next five years;

— 15.5% till 2055.

Taxpayers can use accelerated depreciation with coefficient.

c) customs facilities (e.g. "*Alabuga*" SEZ operates as a free customs zone)

— 0% VAT, import duty.

The Russian STZ residents are exempted from import duties and taxes on foreign equipment if the free custom zone procedure is applied as long as foreign equipment stays in the territory of the STZ till the end period of an investments agreement.

[5] See also p.3 of the Final Summary of the Discussion on the Results of the Meeting of the Coordination Committee of the BRICS Law Institute and of the Expert Group on Legal Support to Inter-State Partnership and Integration on Economics, Finance, Taxation and Customs (9-10 June 2016, Yekaterinburg, Russia)// http://eurasiatax.com/files/Summary.pdf

[6] Reflections on Special Tax Zones, Collaborative Research, unpublished research paper, 4 November 2016, IBFD Academic. P.13.

[7] Yariv Brauner, Miranda Stewart. Tax, Law and development / Edward Elgar Publishing, 2013, ISBN: 9780857930019. P.27.

[8] Reflections on Special Tax Zones, Collaborative Research, unpublished research paper, 4 November 2016, IBFD Academic (Russian part).

2. Aims of Special Economic Zones

At the same time, Special Economic Zones (SEZ, STZ) of the Russian Federation are a large-scale federal project aimed to bring in investments and advanced scientific, manufacturing, and management technologies. According to Article 2 of Federal Law No.116-FZ of 22 July 2005 "On Special Economic Zones in the Russian Federation" (Federal Law / FL No.116-FZ): "…a special economic zone is a part of the territory of the Russian Federation determined by the decision of the Government of the Russian Federation where a special procedure for exercising business activities and a special customs treatment should be applicable".

The zones provide companies with a unique opportunity to use the full range of Russia's investment opportunities while avoiding the typical concerns related to non-market business pressures and inefficient administration[9]. Investing in the Special Economic Zones is the best way to capitalize on Russia's steady economic recovery (estimated 4% GDP growth in 2010)*, the growing consumer activity of one of the world's biggest markets (Russia has a population of 141 million, and the entire FSU region has 281 million people), and the economy that has the third biggest gold and currency reserves ($476 bln in 3Q2010)[10].

3. Types of Special Economic Zones

The relations in special economic zones in the Russian Federation are regulated, on the one hand, by federal laws: **a)** by the Agreement on free (special) economic zones in the framework of the Customs territory of the Customs union and on compliance procedures, 18 June 2010 (hereinafter — the Agreement on SEZs); **b)** by acts of the Eurasian Economic Commission; **c)** by the domestic legislation of the Russian Federation on special economic zones and by tax legislation of the Russian Federation, and, on the other hand, by decrees of the President of the Russian Federation and decisions of the Government of the Russian Federation.

In the Russian Federation, there are different types of special economic zones with different legal and tax regimes:

1) Special Economic Zones directly established by Federal Law No.116-FZ ("general law");

1) the Special Economic Zone established in accordance with Federal Law "On the Special Economic Zone in the Kaliningrad Region";

2) the Special Economic Zone established by Federal law "On the Special Economic Zone in the Magadan Region;

3) the Special Economic Zone provided for by the provisions of Article 2 of Federal Law No.244-FZ of 28 September 2010 "On the Innovation Centre '*Skolkovo*'";

[9] http://eng.russez.ru/investors/

[10] http://eng.russez.ru/investors/

4) the Free Economic Zone introduced by Federal Law No.377-FZ of 29 November 2014 "On the Development of the Crimean Federal District and the Establishment of a Free Economic Zone in the Territory of the Republic of Crimea and the Territory of the Federal City of Sevastopol";

5) the Free Port of Vladivostok was established by Federal Law No.212-FZ of 13 July 2015 "On the Free Port of Vladivostok";

6) the federal legislation provides for opportunities / possibilities for regions to establish supplementary Special Economic Zones at the regional level (and to apply reduced tax rates);

7) Zones of Territorial Development provided for by Federal Law No.392-FZ of 3 December 2011 "On the Areas of Territorial Development in the Russian Federation and on Amending Certain Legislative Acts";

8) Zones of Advancing Social and Economic Development provided for in accordance with Federal Law No.473-FZ of 29 December 2014 "On the Territories of Advancing Social and Economic Development in the Russian Federation";

9) the Special Tax Regime established by Article 284.3 of the RF Tax Code for the exploration of hydrocarbon deposits on the continental shelf of the Russian Federation.

According to Article 3 of Federal Law No.116-FZ "Goals of Setting up Special Economic Zones", special economic zones shall be set up with the objective of developing processing, industries, high-technology industries, tourism, the sanatoria-resort sphere, the harbor and transport infrastructure, process engineering and commercialization of their results as well as of manufacturing novel types of products.

The following types of special economic zones shall be established in the territory of the Russian Federation: 1) industrial-and-production special economic zones; 2) technological-and-innovative special economic zones; 3) tourism-recreational special economic zones; and 4) port special economic zones.

The zones provide companies with a unique opportunity to use the full range of Russia's investment opportunities while avoiding the typical concerns related to non-market business pressures and inefficient administration.

4. Conclusions

1. Developing countries have expressed particular support for a platform to work together on an equal footing with regard to the monitoring and implementation of the BEPS outcomes[11]. In that context, it is clear that effective implementation needs a combined effort.

[11] https://www.pwc.com/gx/en/tax/newsletters/tax-policy-bulletin/assets/pwc-developing-countries-show-interest-in-oecd-beps-recommendations.pdf

The countries of BRICS reflect in their economic systems both the features of developed and developing countries, already for this reason there are grounds to believe that they are a proper international forum for finding an appropriate balance between the regulation of the activities in special economic zones and the implementation of the BEPS[12].

2. The OECD BEPS project, the increased requirements for exchange of information and limitation on benefits (LOB) rules emerging from the United States, and the anti-tax haven attitudes so prevalent in the European Union further diminish the acceptability of tax haven operations and make them subject to more scrutiny. For these reasons, STZs must provide an environment where the development targets are clearly defined, the rules and legislation are transparent and acceptable, and information flows freely from STZs to tax authorities of the investors' country of residence[13].

The regulation in Russia directly complies with the accepted BEPS standards. However, there are priority national interests, which affect the policy on the regulation of relations within special tax (economic) zones. The above does not enable to make the legal regulation more transparent. Besides, the developing of the Russian special tax zones should be in coordination with BRICS member states for economic purposes. Such tasks pose a serious challenge to the legislator.

[12] See hereinafter http://eurasiatax.com/files/Summary.pdf

[13] Antti Laukkanen. Special Tax Zones in Developing Countries and Global Tax Policy // Bulletin for International Taxation, 2016 (Volume 70), No.10.

REFLECTING ON DOMESTIC ECONOMIC POLICY OF THE RUSSIAN ESTABLISHMENT

Vladimir S. Belykh
Professor, Doctor of Law, Head of Entrepreneurial Law Department, Ural State Law University, Yekaterinburg, Russia

Abstract
The article contains a critical analysis of the RF government's Anti-crisis plan. The author makes some general conclusions and recommendations aimed at ensuring stable economic and social development. First of all, the author underlines that the idea of economic modernization is obviously not objectionable and doubtful. Therefore it is necessary to define its spheres, aims, and principles. So far, there are only declarations!

Keywords: modernization of the economy, Anti-crisis plan, Russian GDP, inflation, unemployment level, a new concept of managing national economy, recommendations on drafting new laws in the sphere of economy and entrepreneurship.

The 2009 line for modernization set by the then Russian President Dmitry Medvedev met a mixed reaction in the society. The great majority of Russians remained silent and did not comment on the chosen policy for modernization. That was understandable, as there are more vital things to be concerned about, like real conditions for living, rather than declarative statements of the Head of the State and its "senior dignitaries". There have been many examples in the history of our long-suffering people: from the "construction of a brighter future" to the Gorbachev's *Perestroika*.

Against this background, there were many publications, various articles, compilations, textbooks, and monographs. The range of academic research areas was rather wide: policy, economy, education, culture, and etc. At the same time, there was a unilateral approach (subject and sector oriented) to the research (economic, administrative, legal, etc.) that does not invalidate the quality of the carried research. Thus, L.V. Goloskokov writes about modernization of the Russian law from the point of using informational technologies and tools[1]. S.A. Belyakov examines the modernization of education in Russia from the point of improving

[1] See: L.V. Goloskokov. Modernizatsiia rossiiskogo prava [Modernization of the Russian Law]: Monograph/ ed. by A.V. Mal'ko. Moscow, 2006.

the administration[2]. The authors of the monograph "Modernization of the Russian Education: Resource Potential and Staff Training" focus on the issues connected with the quality of professional education, educational technologies, and the growth of the material and technical base in educational establishments[3]. The multi-authored monograph "Modernization of Russia in Economy and Policy" examines the controversial issues of establishing the rule-of-law and social state, civil society, law in the economic and political spheres as well as innovative processes[4].

At the same time, the proclaimed line for modernization has been 'thick in the air' for long. At present, there is no (as we used to say in the good old days) science-based concept for modernization of Russia at large and national economy inter alia. That is why, there are still many declarations!

Like any idea, the idea of modernization may grasp the minds of people in a voluntary form if people are mature enough to understand and implement it. In the foreseeable future, there is still no required 'turn of brains'. In contrast, there is a great brainwashing in the form of political declarations and emphatic statements. However, the nation's poverty (multiplied by the high rate of unemployment, mortality, etc.) generates poverty in philosophy and opinions.

Russia's socio-economic position before and during the crisis remains unchangeably difficult (multiple indicators show that) as other countries have ensured better control over inflation, diversification of national economies, growth of production, generous social programs, and political stability[5]. For example, the Chinese economic policy during the crisis was oriented at the needs of the domestic market. The above said led to lower dependency on external factors that eventually predetermined its economic growth and development.

The following economic indicators illustrate the said. Thus, according to *Rosstat's* preliminary estimates, Russia's GDP nominal in 2014 was 70 trillion 975 billion rubles; the index of physical volume was 100.6 %. The growth rate of the Russian economy was the weakest since 2009. For example, Russia's GDP grew by 3.4% in 2012, by 4.3% in 2011, by 4.5% in 2010. In the crisis 2009 year, the economy fell by

[2] See: S.A. Belyakov. Modernizatsiia obrazovaniia v Rossii: sovershenstvovanie upravleniia [Modernization of Education in Russia: Improvement of Administration]. Moscow, 2009.

[3] Modernizatsiia rossiiskogo obrazovaniia: resursnyi potentsial i podgotovka kadrov [Modernization of the Russian Education: Resource Potential and Staff Training]/ ed. by T.L. Klyachko. Moscow, 2002.

[4] Modernizatsiia Rossii v ekonomike i politike [Modernization of Russia in Economy and Policy]: monograph. Yekaterinburg, 2012, p.322.

[5] *See*: V.S. Belykh. Modernizatsiia rossiiskoi ekonomiki i predprinimatel'skogo zakonodatel'stva: voprosy teorii i praktiki [Modernization of the Russian Economy and Entrepreneurial Legislation: Issues of Theory and Practice]/ ed. by A.I. Tatarkin. Yekaterinburg, 2011, pp.54-58, 150-165.

7.8%. According to the official estimates of the Economic Development Ministry, the GDP in 2016 amounted to minus 0.6%[6].

The inflation refreshes the records. According to *Rosstat's* estimates, the Consumer Price Index was 102.6% in December 2014, for the period (December 2014 as a percentage of December 2013) it was 114.4%[7]. In 2014, the inflation level was 11.36% at an annual rate. According to Aleksei Uliukaev, Minister of Economic Development, the inflation peak was in March — April of 2015 and amounted to 15 — 17%[8]. The estimates of the Economic Development Ministry for the inflation of 2016 were much better — 5.8%. In short, the forecast of the Economic Development Ministry resembles Schubert's great *Fantasie*. The life has become better and more fun!

We would like to continue by mentioning the rate of *unemployment* in Russia. In February 2009, the overall unemployment was 6.1 million people or 8.1% of economically active population. At an annual rate the total number of unemployed people increased by 1.1 million[9]. However, in March of 2009, the preliminary *Rosstat's* estimates made according to the International Labor Organization standards showed that the number of unemployed people was 7.5 million. During 2012-2014, the unemployment rate in Russia seemed to shrink. In the beginning of 2011, it was 7.85%, and in the beginning of 2014 it was 5.3%. By the end of 2014, the rate of unemployment began to rise. *Rosstat* estimated that, in November 2016, the rate of unemployment was 5.2% and it constituted 4 million people of economically active population.

Economists, lawyers and doctors find it more difficult to secure employment. There has also been a gradual oversupply of IT specialists that were highly demanded even several years ago. At the same time, there is a lack of engineers, workers for production industries, and technologists. The professions of hairdressers, sales assistants and cosmetologists do not lose their popularity. Russian Prime Minister Dmitry Medvedev advised teachers who are unhappy about their economic lot to earn money in[10]. Another popular expression belonging to Prime Minister is: "There's just no money. But you take care!"

The economic situation in Russia has worsened after the USA and European states imposed various sanctions, including financial ones. The sharp decline of oil prices is the most painful for the Russian economy. Russia needs oil at a price not lower than USD 100 per barrel to balance its budget[11]. Currently, one barrel of oil

[6] http://www.interfax.ru/business/525823

[7] http://www.gks.ru/bgd/free/b04_03/IssWWW.exe/Stg/d05/ind-zen26.htm

[8] http://top.rbc.ru/finances/11/02/2015/54db61179a79478025b561aa

[9] Federal State Statistics Service. Information on Social and Economic Situation in Russia — 2009. Employment and Unemployment//www.gks.ru

[10] http://izvestia.ru/news/625391

[11] Source: http://censor.net.ua/n276978

costs USD 45, though some analysts forecast USD 20-25 per one barrel of oil in the short term.

What does the Russian Government do in this situation of immense complexity? It drafts and adopts the so-called "Anti-crisis plan" that sets measures for ensuring a sustainable economic development and social stability in Russia[12]. At present, it contains 60 articles but the drafters indicated that the measures would be changed depending upon the situation.

The Anti-crisis plan has *seven key directions*. They are import substitution, promotion of small and medium-sized businesses, compensation of inflationary expenses to pensioners and large families, and optimization of budget spending. According to the Anti-crisis plan, the greatest proportion of money should be spent on additional capitalization of systemically important banks (1 trillion rubles at the expense of the Agency on Deposit Insurance and 250 billion rubles from the Fund of National Well-Being of Russia). 50 billion rubles go to combat unemployment. The agricultural sector will receive 54 billion rubles. Financing of government programs in the sphere of public health and education will remain the same.

Aleksei Kudrin, former RF Minister of Finance, wrote in his Twitter account: "The Anti-crisis program has a lot of rational things but it offers only partial pain relief and is hardly a cure"[13]. He thinks that the program lacks structural reforms, which are crucial for exiting the crisis and stagnation. However, he thinks that the Anti-crisis plan will be completed by 90%, though the risks of GDP fall will stay at 4%, and the inflation will range from 12% to 15%[14].

The following **general conclusions and recommendations** aimed at ensuring stable development of the economy and social stability in Russia should be formulated. First, it is necessary to differentiate between long-term measures and short-term measures for overcoming the stagnation and crisis phase.

1. The idea of modernization appears undisputed. Though, it is necessary to clearly define its spheres, principles and objectives. Not only does the Russian economy need modernization, but the political system and other segments of society and state as well. So, we need a *holistic concept for modernizing the Russian economy* for a long-term period secured by the system of non-legal and legal means. In particular, we propose that Russian national projects should take the form of federal laws and be under great control of the state and public.

2. Presidential Decree No.478 of 29 April 2012 approved the Charter of the budgetary institution "Russian Institute of Strategic Studies" (RISS). The main task of the RISS is to provide information support to the Administration of the President of

[12] http://government.ru/info/761/

[13] http://top.rbc.ru/economics/30/01/2015/54cbaaa79a79470e77ba1253

[14] http://openrussia.info/4710-kudrin-antikrizisnyy-plan-budet-vypolnen-na-90.html

the Russian Federation, the Federation Council, the State Duma and the Security Council as well as to Government offices, ministries and departments. The RISS provides expert appraisals and recommendations and prepares analytical materials for those bodies. We think that the RISS activities should focus on major projects like modernization of the economy, political system, and national security. There is no centre for legal studies within the RISS structure and there are no expert lawyers. In any case, the RISS needs reforming with due regard to the experience of strategic studies institutes (centres) in the countries of the near and far abroad.

3. On Friday (13 February 2015), the RF President Vladimir Putin gathered high-ranking officials and Heads of the Bank of Russia not to make the Anti-crisis plan become a dead letter. During this meeting, Herman Greff, Head of the RF *Sberbank* proposed a public administration reform. His main idea is to establish a new Centre for Change Management under the RF Government that will deal with the preparation for reforms as the ministries are overloaded with work and have no time to comprehend the reform. And the Centre will be working out general rules and indicators[15]. Herman Greff also proposed to reduce the number of instructions, to create the new system of motivation in the Ministries, indices for the officials and new methods of staff selection. This proposal is rather interesting. With respect to the above, we propose not to establish a new centre, but to place the said functions with the Russian Institute for Strategic Studies.

4. The concept of the Russian economy modernization should mainly focus on the development (with the elements of strong state support and protectionism) of core branches of the national economy system such as machine-building, metallurgical industry, fuel and energy complex, chemical and forest complex, and light industry. These very spheres of economy should be invested in. The economy needs diversification!

Indeed, the years of Putin's presidency are the years of missed opportunities for Russia. The Russian economy has been marking time at best. Anatoly Chubais said: "The unique economic conditions that have developed in Russia over the past 6-7 years could be used much better"[16]. He also stressed that Putin's period in Russia's life was a fantastic coincidence in the economy. The situation with oil was fantastic. But that fantastic situation remained in the history of the Russian state. On 19 December 2014, Russian President Vladimir Putin at the meeting with the leading businessmen encouraged them to participate in the diversification of the Russian economy and promised that the state would help them[17]. But the calls are not likely to help. We need the program and a strong hand!

[15] http://news.rambler.ru/29161643/

[16] http://lenta.ru/news/2005/11/20/chubais/

[17] RIA Novosti http://ria.ru/economy/20141219/1039260750.html#ixzz3SRorwGYJ

5. The thesis that *the market economy has more advantages than the administrative one* does not need specific argumentation. At the same time, the market economy (especially in Russia) is unimaginable without the elements of central management. Methods of state regulation over economic life in Russia must be actively and reasonably implemented. The question about the state interference with the private affairs and economy was very relevant during the global financial crisis. The situation at the stock demonstrated that the state must control the market and be actively involved in these processes. Private property cannot be "a sacred cow", and the state must not play the role of "a night watchman". *Market self-regulation* is not bad but it should be complemented by a state one.

During the transitional period, modern Russia needs *a new concept of national economy management* — a concept of the state socially oriented capitalism. This concept should be taken into account while drafting the concept for the modernization of current legislation (including the sphere of entrepreneurial legislation). The ideology of the modernization process should be looked at within the line of the economic model[18].

6. Large integrated structures should become, on the one hand, the main links in the Russian economy. Together with the state defense enterprises, holdings are able to lead the state economy out of stagnation to the level of progressive development. On the other hand, *small and medium businesses* are an important and necessary element of the market economy. Small and medium businesses play a key role in the stable growth of the national economy and the welfare of the citizens in the developed European countries. "Asian economic miracle" also to a great extend happened due to the small business. Nearly all countries of the South-East Asia (excluding North Korea) provide an unprecedented large-scale support to small business. They three times exceed the European countries in the dynamics of entrepreneurship development and economic growth[19]. These figures are impressive! The Anti-crisis plan states that one of the key directions in the RF Government's actions in the nearest future will be the support to the development of small and medium enterprises by reducing financial and administrative expenses. Let us hope for the said to become true!

7. On 22 August 2012, Russia became the 156th member of the WTO. However, the consequences of this event fell outside the systemic analysis. The negotiation process is known to have been going on in the *four basic directions*: *1) negotiations*

[18] V.S. Belykh. Modernizatsiia rossiiskoi ekonomiki i predprinimatel'skogo zakonodatel'stva: voprosy teorii i praktiki [Modernization of the Russian Economy and Entrepreneurial Legislation: Issues of Theory and Practice]/ ed. by A.I. Tatarkin. Yekaterinburg, 2011, p.78.

[19] *See*: V.A. Semeusov. Maloe predprinimatel'stvo v Rossii [Small Business in Russia]: Study guide. Irkutsk, 2001, pp.11-12.

on tariff issues. The main goal here is to define the maximum level of import duty tariffs which Russia will be able to use after the official WTO accession; *2) negotiations on agriculture.* The key point (excluding tariff) is defining the level of internal support to the agrarian sector; *3) negotiations on entering the services market.* The goal is to harmonize the conditions for foreign suppliers to enter the Russian market; *4) negotiations on systemic issues.* The main goal of negotiations is to define measures that Russia will take in the sphere of legislation and its implementation to perform its obligations as a WTO member[20].

According to the survey, *negative consequences in the short-term period* may affect the enterprises of food, pharmaceutical, and textile industries. Possible decline in the production volume in these sectors may be 0.5 — 2%. But the largest fall is expected in the machine building sector — up to 12% drop of the production — and also in the food, light, and construction materials industries where the drop will be up to 7%. Negative consequences will affect aircraft building and car industry, agriculture, and agrifood sector. For example, due to Russia's commitments, the country will have to reduce tariffs on imported line aircrafts within 7 years. It will pose a serious threat to large-scale aircraft manufacturing projects being implemented by our state. That is hardly contributing to the development of the Russian aircraft companies.

In short, where is the analysis of consequences of Russia's accession to the WTO at the government level? Let us not speed things up and wait for four years. Then, we will be able to say definitely which branches of domestic industries have stood the test of the world market in connection with the WTO accession and which have not done that[21].

At the same time, the RF Government had to organize and carry out a differentiated assessment of the WTO accession within the branches and regions. Without this assessment, all recommendations on curtailing the economy sectors may lead to serious socio-economic consequences.

8. In the modern context, the key issue is Russia's rental income. According to the assessment of academician D.S. Lvov, annual net national economic income of the country is 60-80 billion dollars that 2-2.5 times higher than the present amount of the budget[22]. So, if the retained income is 60-80 billion dollars, then the rent is 45-60 billion dollars. Thus, the greatest part of Russia's income is privatized (e.g. in the

[20] *See*: V.S. Belykh. Ekonomicheskii i pravovoi analiz posledsvii vstupleniia Rossii vo Vsemirnyiu torgovuiu organizatsiiu [Economic and Legal Analysis of Consequences after Russia's Accession to the World Trade Organization]// Business, Management and Law. 2013. No 1, pp.16-17.

[21] This is what Michail Margelov, Chairman of the Russian Federation Council's Committee on Foreign Affairs, thought// http://www.rg.ru/2012/08/22/vto-anons.html

[22] Upravlenie sotsial'no-ekonomicheskim razvitiem Rossii: kontseptsii, tseli, mekhanizmy [Management of Socio-Economic Development of Russia: Concepts, Objectives, Mechanisms]/ Heads of the collective body of authors D.S. Lvov, A.G. Porshnev. Moscow, 2002, pp.13-14.

shadow business, offshore zones, and criminal structures). However, on the fair comment of the economist-scholar, the rental income is not the result of the direct entrepreneurial activity and commercial risks, i.e. it comes from God. So, rental income must belong to everybody. Alexander Yakovlevich Lifshits, former Minister of Finance said: "You have to share!" Even, if not now, then in the foreseeable future.

9. In February 2008, the Stabilization Fund was divided into the Reserve Fund and the Fund of the National Welfare. The latter is a part of the mechanism for pension support of the RF citizens. According to the RF Ministry of Finance, the volume of the Fund of the National Welfare is 5,101,83 billion rubles as of 1 February 2015. Then, the volume reduced and was 4,541,93 billion rubles as of 1 November 2016.

The debts of the present oligarchs to the state and society that incurred as a result of the total privatization of the federal property (read: nationwide) should be repaid. Such repay is only possible by way of transferring the corresponding share in business to the state or by way of donating, or by way of constructing a lot of social facilities and infrastructure. We propose to establish a unified fund that resembles Soros Foundation at the expense of major Russian entrepreneurship.

10. Against the backdrop of the economic crisis and the stagnation of the Russian economy, we propose to draft and adopt the following federal laws: 1) On Entrepreneurial Activity[23]; 2) On Property Administration[24]; 3) On Nationalization and Deprivatization; 4) On Control and Mergers (Acquisition); 5) On Prices and Price Formation; 6) On Financial Instruments; 7) On Foundations of Innovative Activity.

Looking at the investment and innovative policy as a component of the Russia's industrial policy one should: **a)** bring the regimes of legal regulation in the sphere of foreign and national investments (including benefits) closer; **b)** eliminate the conflicts of norms in the Russian investment, tax and customs legislation; **c)** ensure the protection of Russia's national interests from illegal foreign companies.

[23] *See*: V.S. Belykh. Kontseptual'nye predlozheniia po razrabotke tipovogo proekta zakonodatel'nogo akta "O Predprinimatel'skoi Deiatel'nosti" [Concept Proposals on Drafting the Legislative Act "On Entrepreneurial Activity"]// Business, Management and Law. 2013. No.2.

[24] *See*: V.S. Belykh O kontseptsii proekta zakona "Ob upravlenii sobstvennostiu" [On the Concept of the Draft Law "On Property Administration"] //Business, Management and Law. 2009. No.1.

INDEPENDENT AND DISINTERESTED DIRECTORS IN RUSSIAN JOINT-STOCK COMPANIES

Olga A. Makarova
Doctor of Sciences (Law), Associate Professor
Department of Commercial Law
St. Petersburg State University, Russia

Independent—free from outside control;
not subject to another's authority.
Disinterested—not influenced by considerations
of personal advantage.
Oxford Dictionary of English (Oxford University Press, 2005)

Abstract
The approval procedure for related party transactions has recently been amended in the revised version of Russia's Federal Law "On Joint-Stock Companies". The amendments effective from 1 January 2017 replaced the concept of an "independent director" by that of a "disinterested" one. This paper analyses the two concepts and their treatment in Russia's legislation on joint-stock companies. The definitions of the disinterested director and the independent director are provided. The paper also analyses the issue of mandatory inclusion of independent directors in public companies' boards.

Keywords: board of directors, a public company, the independent director, the disinterested director, a transaction affected by a conflict of interests.

The concepts of 'independent' and 'disinterested' directors in Russia's legislation on joint-stock companies. The concepts of the independent director and disinterested director were used in Russia's legislation with regard to the approval of related party transactions (transactions affected by a conflict of interests).

As enacted, Federal Law No.208-FZ "On Joint-Stock Companies" of 26 December 1995 laid down the following procedure to approve a related party transaction: "Where a company has 1,000 shareowners with voting shares or more, the decision to enter into a related party transaction shall be made by the company's board of directors (supervisory board) by a majority vote of *independent directors disinterested in the transaction.*" (p.2 Art.83 as amended in 1999).

The same article also contained the definition of an independent director: "a member of the company's board of directors (supervisory board) who is not acting

as the sole executive authority (director, general director) and is not a member of the collegial executive body (management board), provided his spouse, parents, children, brothers and sisters are not officers in the company's governing bodies". In other words, the cited provision is related both to independent directors and to directors disinterested in a transaction affected by a conflict of interests, taking into account that Art.81 of the Law defined persons interested in a transaction.

As revised on 1 January 2002, Federal Law "On Joint-Stock Companies" adopted the same approach saying that "where a company has 1,000 shareowners with voting shares or more, the decision to enter into a related party transaction shall be made by the company's board of directors (supervisory board) *by a majority vote of independent directors disinterested in the transaction.* In the event all members of the company's board of directors (supervisory board) are recognized as self-interested and (or) are not independent directors, the transaction shall be approved at the general meeting of shareowners" (Art. 83 p.3)[1].

In this respect, "an independent director is a member of the company's board of directors (supervisory board) who is not and has not been for a year before the decision:

1) a person exercising the powers of the company's sole executive authority, including a sole trader exercising the powers of the management company; a member of the collegial executive body; an officer of the management company's governing bodies;

2) a person whose spouse, parents, children, full and half siblings, adoptive parents and adopted children are officers in the said governing bodies of the company or the management company, or act as a sole trader exercising the powers of the management company;

3) the company's affiliated person, with the exception of the member of the company's board of directors (supervisory board)".

Therefore, the concept and criteria of a director's independence were used in conjunction with his lack of interest in the board of directors' approval of a transaction affected by a conflict of interests.

However, a director's self-interest in the company entering into a particular transaction is not connected from whether he is an independent director or not. A director's self-interest essentially means his attitude to the transaction—i.e. his private interest of a material or other nature that runs counter to the interests of the majority of shareowners or the company as a whole[2].

[1] Federal Law No.120-FZ "On Amending Federal Law "On Joint-Stock Companies" of 7 August 2001. Collection of Legislation of the Russian Federation, No.33 (part 1) (13 August 2001), Art.3423.

[2] I.S. Shitkina, ed. Korporativnoe Pravo: Uchebnik [Corporate Law: textbook], 2nd ed. (Moscow: 2015), 810. See also: I.S. Shitkina, ed. Sootnoshenie imperativnykh i dispozitivnykh nachal v kor-

The courts have commented upon the concept of self-interest in their decisions: "the self-interest in a transaction means an interest of a particular person in determining the terms and conditions of a transaction, the choice of contractor and the contract price; this self-interest is underlain by a person's private interest of a material or other nature that runs counter to the interests of the majority of shareowners or the company as a whole. This serves to prevent the possible abuse by interested persons resulting from their position and private interests and, also, to protect the rights of other (disinterested) shareowners"[3].

The independence of a board member is a criterion that characterizes his status in the board of directors and the company as a whole. Ideally, an independent director is a member of the board who is elected by shareowners but does not depend on them—i.e. has neither family nor official (subordination) ties with them. It is these independent directors who should monitor and improve the company's performance, counterbalance the pressure of persons interested in certain transactions, and curb the selfish initiative of the company's affiliates[4].

An independent director has a major mission of maintaining the balance of interests in the board of directors—including protection of the government's interest—and assisting in conflict resolution to the benefit of the company. His other important functions include contributing to the company's strategy and taking part in supervising the management[5].

The Council of Institutional Investors provided a simple and understandable definition of an independent director: "… a person whose directorship constitutes his or her only connection to the corporation"[6].

The Principles of Corporate Governance drawn up by the Organisation for Economic Cooperation and Development (OECD) set forth that the board must be able to exercise objective judgement on corporate affairs in an independent manner, including independence from management. To that end, it is recommended that the boards should consider assigning a sufficient number of non-executive board members capable of exercising independent judgement to tasks (e.g. ensuring the

poravitnom prave: Sbornik statei [Interrelation of Mandatory and Default Rules in Corporate Law: Collected Articles] (Moscow: Statut, 2017), 48.

[3] Ruling of the RF Supreme Court No.303-ES15-17677 of 21 January 2016 in Case No.A51-32494/2013, https://kad.arbitr.ru/Card/4520fad5-021c-4cb2-ba76-0122266dace2

[4] N.V. Bandurina. Nezavisimye direktora v sisteme korporativnogo upravlenia gosudarstvennoi sobstvennost'u [Independent Directors in the System of Corporate Governance of State Property], "Chernye dyry" v rossiiskom zakonodatel'stve ["Black Holes" in Russia's Legislation], No.6 (2011). P.166-169.

[5] A.A. Filatov. Rol' nezavisimykh direktorov v rossiiskikh kompaniyakh [Role of Independent Directors in Russian Companies] — Sobstvennik i menedger: stroim effektivny biznes [Owner and Manager: Building a Successful Business], edited by A.A. Filatov and K.A. Kravchenko (Moscow: 2008). P.59.

[6] http://www/cii/org/independent_director.asp.

integrity of financial reporting and management remuneration) where there is a potential possibility for a conflict of interests[7].

Therefore, the "self-interest" test applies to certain transactions that might be affected by a conflict of interests. Conversely, the "independence" test characterizes the status of a board member.

That is the reason why the concept of an "independent director" was removed from Art.83 (3) of Federal Law "On Joint-Stock Companies" as amended by Federal Law No.343-FZ of 3 July 2016[8] that set out the criteria to ascertain whether a public company's board member is disinterested for the purpose of approving a transaction affected by a conflict of interests.

Art. 83(3) contains the following provision: "In the instances governed by cl.1 of this Article, a decision to enter into a related party transaction is made by a public company's board of directors (supervisory board) by a majority vote (unless a different threshold is laid down in the company's articles of association) of *directors disinterested in the transaction,* who are not and have not been for a year before the decision:

1) a person exercising the powers of the company's sole executive authority, including a sole trader exercising the powers of the management company; a member of the collegial executive body; an officer of the management company's governing bodies;

2) a person whose spouse, parents, children, full and half siblings, adoptive parents and adopted children are officers of the management company, including its governing bodies; or act as a sole trader exercising the powers of the management company;

3) a person controlling the company or the management company (or controlling the sole trader exercising the powers of the management company), which the management company exercises powers of the company's sole executive body; or a person who can give mandatory instructions to the company".

Comparing the previous version of Art.83 (3) relating to independent directors and the latest version of the said Article relating to disinterested directors, we can conclude that the latter uses the same criteria to characterize a director's disinterest as were used by the former to describe a director's independence. The concept of "affiliated persons" is the only exception: in the latest version, it was replaced by "controlling persons".

[7] Organization for Economic Co-operation and Development. Principles of Corporate Governance (Art. V), P.22-23, http://www.oecd.org/corporate/ca/corporategovernanceprinciples/32159669.pdf.

[8] Federal Law No.343-FZ "On Amending Provisions of Federal Law "On Joint-Stock Companies" and Federal Law "On Limited Liability Companies" relating to large transactions and related party transactions" of 3 July 2016. Collection of Legislation of the Russian Federation, No.32 (part 2) (4 July 2016), Art.4276.

Mandatory inclusion of independent directors in public companies' boards. The new provisions relating to the procedure of granting consent to (subsequent approval of) transactions affected by a conflict of interests took effect on 1 January 2017. The amendments removed the director's independence criteria from the law. Does it imply that boards of directors in joint-stock companies — first and foremost, public companies — might include no independent directors at all, since there is no mandatory rule in this regard? Basically, there has never been such a rule, because a director's independence was determined in conjunction with his disinterest for the purposes of approving transactions affected by a conflict of interests.

The Code of Corporate Conduct recommended by the Federal Securities Commission (Order No.421-r of 4 April 2002) mentioned the director's independence criteria and recommended to include independent directors in Russian joint-stock companies' boards of directors[9]. Specifically, the Code says the following: "The effective functioning of the board of directors requires inclusion of independent directors — that is, persons who are not members of the management board, are independent from the company's officials, their affiliates and the company's large contractors; and have no other relations to the company that could compromise their independence".

"The specific requirements to an independent director should be inferred from the fact that such a director must be capable of independent judgement. This implies there are no circumstances that can influence his opinion". The Code of Corporate Conduct provided a list of the director's independence criteria and recommended that independent directors should comprise at least 25% of the board of directors. "In any event, it is advisable for the company's articles of associations to provide for at least three independent directors in the board of directors"[10].

The Code of Corporate Conduct of 2002 was recommended to all joint-stock companies. After 2002, publicly traded companies started to include independent directors in their boards of directors.

In 2014, the Code of Corporate Conduct was replaced by the Code of Corporate Governance recommended by the Bank of Russia that contains similar provisions in relation to public companies[11].

According to the Code of Corporate Governance, "it is advisable that the person recognized as an independent director has sufficient professional competence, experience and autonomy to form his own opinion, and is capable of making objective

[9] http://www.zakonprost.ru/content/base/part/40551.

[10] http://www.zakonprost.ru/content/base/part/40551.

[11] Bank of Russia's Letter No.06-52/2463 "On the Code of Corporate Governance" of 10 April 2014. Vestnik Banka Rossii [Bank of Russia's Bulletin], No.40 (18 April 2014).

and conscientious judgement that is independent from the company's executive bodies, shareowner groups and other interested persons".

"Independent directors should play a key role in preventing corporate conflicts and making decisions that are of major importance for the company".

The Code of Corporate Governance also says: "Though it is impossible to enumerate all possible circumstances that can influence a director's independence, it is advisable to recognize as an independent director (a candidate to be elected to this position) the person who meets the following criteria:

1) has no connection to the company;

2) has no connection to a large shareowner of the company;

3) has no connection to the company's major contractor or competitor;

4) and has no connection to the state (the Russian Federation, a constituent entity of the Russian Federation) or municipal authorities.

The boards of directors in joint-stock companies "are advised to evaluate the compliance of candidates to the board of directors with independence criteria; to perform a regular analysis of current independent directors' compliance with independence criteria; and to ensure immediate disclosure of circumstances compromising a director's independence. The evaluation should place the emphasis on the content rather than the form".

Therefore, the Code of Corporate Governance contains only recommendations on inclusion of independent directors in public companies' boards of directors. Similarly, no mandatory provisions are included in the Bank of Russia's Information Letter No.IN-015-52/66 of 15 September 2016 "On Provisions Regarding the Board of Directors and its Committees in Public Companies"[12] or the Bank of Russia's Information Letter No.IN-06-52/8 of 17 February 2016 "On Disclosure of Compliance with Principles and Recommendations of the Code of Corporate Governance in Annual Reports by Public Companies"[13]. The information letters issued by the Bank of Russia are not universally binding[14].

However, we should mention the "Regulation on Admission of Securities to On-Exchange Trading" No.534-P approved by the RF Central Bank on 24 February 2016[15]. The Regulation lays down the requirements to corporate governance that precondition the listing of securities and sets forth the conditions of failure to

[12] http://cbr.ru/finmarkets/files/common/letters/2016/Inf_sep_1916.pdf.

[13] http://cbr.ru/finmarkets/files/common/letters/2016/Inf_feb_1916.pdf.

[14] Federal Law No.86-FZ of 10 July 2002 (revised on 3 July 2016) "On the Central Bank of the Russian Federation (Bank of Russia)" (with amendments effective from 1 January 2017). Collection of Legislation of the Russian Federation, No.28 (15 July 2002), Art.2790.

[15] The Regulation on Admission of Securities to On-Exchange Trading (approved by the Bank of Russia on 24 February 2016 No.534-P) (registered in the RF Ministry of Justice on 28 April 2016 No.41964). Vestnik Banka Rossii [Bank of Russia's Bulletin], No.45 (12 May 2016).

comply (Appendix 4 to the Regulations). These requirements, *inter alia*, include the presence of independent directors in the company's board. The independence criteria are set by an exchange that takes into account the provisions contained in the Code of Corporate Governance recommended by the Bank of Russia. The independent directors shall comprise at least one fifth of the board of directors and there shall be at least three independent directors in the board.

Independent directors shall comprise the majority in the nomination committee, while the audit committee and remuneration committee shall be entirely comprised of independent directors. In the event that is impossible for objective reasons, independent directors shall comprise the majority in each committee, while the remaining membership of the said committees (nomination, audit and remuneration) may include members of the board of directors who do not exercise the functions of the issuer's sole executive body and are not members of its collegial executive body.

"The Regulation on Admission of Securities to On-Exchange Trading" is a piece of secondary legislation that is binding on issuers of securities — first and foremost, on public companies. Therefore, public companies shall have independent directors in their boards of directors and its committees as a mandatory requirement.

REFORM OF INTERESTED PARTY DEAL REGULATION IN JOINT-STOCK COMPANIES

Maria A. Mazo
Candidate of Law, Master of Jurisprudence (Russian School of Private Law),
Master of Comparative Law, Economics and Finance
(International University College of Turin, Italy)
Leading Legal Adviser of Corporate Relations Department

Abstract
The article focuses on the recent reform of interested party deal regulation in joint-stock companies. The author considers main amendments of Federal Law "On Joint-Stock Companies", theoretical aspects of conclusion and approval of interested party deals, analyses the concept of the conflict of interests as a whole and proposes certain amendments in this respect.

Keywords: interested party deal, corporate approval, conflict of interests, joint-stock company, corporate interest.

On 1 January 2017, provisions amending Federal Law No.208-FZ of 26 December 1995 "On Joint-Stock Companies"[1] in respect of interested party deals came into force[2]. Amended law contains a lot of significant changes regarding the list of interested parties, cases of such deals, the procedure of corporate approval, and challenging these transactions, etc. The article will consider some of these amendments.

Amendments to the List of Persons Deemed to be Interested Parties

Until recently, one of the most important problems of interested party deals regulation was the list of persons who may be deemed to be interested parties according to the relevant provisions of the Law "On Joint-Stock Companies".

On the one hand, this list was too wide since it was referring to the concept of affiliated persons. This reference made the given list almost limitless[3], and, in practice,

[1] Collection of Legislation of the Russian Federation. 1999. No.1. Article 1. Hereinafter referred to as Law "On Joint-Stock Companies".

[2] Federal Law of 3 July 2016. No.343-FZ "On the Introduction of Amendments to Federal Law "On Joint-Stock Companies" and Federal Law "On Limited Liability Companies in Respect of Major Deals and Interested Party Deals"//Collection of Legislation of the Russian Federation. 2016. No.27. Article 4276.

[3] A.V. Gabov. Interested Party Deals in Practice of Join-Stock Companies: Problems of Legal Regulation. M., 2005 // Legal Reference System "ConsultantPlus".

there were a lot of persons deemed to be interested; therefore, there was a large number of transactions requiring special corporate approval as interested party deals.

It is obvious that the legislator intended to cover the maximum number of possible social relations trying to find out the maximum number of entities associated to directors, shareholders and other persons entitled to adopt managerial decisions on behalf of a company. However, it led to the situation when transactions which, in fact, did not include any conflict of interests were formally considered as interested party deals. This, in its turn, made corporate procedures more complicated, impeding business activities of joint-stock companies and increasing its managing costs.

On the other hand, though the mentioned list was quite wide, some situations of the deals with a factual conflict of interests were not covered by the law. In particular, the law did not regulate cases with persons who have not registered their marriage, friends, persons undertaking business activity jointly, formally independent shareholders, which in fact are under control by the same commercial company via offshore firms, and so on. Relations with such persons are relations of business or personal nature or relations of subordination, economic dependence and, therefore, they may lead to a factual conflict of interests which is not provided for by the law.

The latest amendments to the Law "On Joint-Stock Companies" have addressed the given problem in part.

At present time, there is no reference to affiliates in the list of interested parties. Instead, the updated law uses another category. This category is "controllability" with a certain number of clear criteria of the controlling and controlled persons. According to amended Article 81 of the Law "On Joint-Stock Companies", a person shall be deemed to be controlling, if this person directly or indirectly (through his controlled persons) is entitled to control *(by way of participation in the controlled entity and (or) by virtue of the agreement on the fiduciary management of assets and (or) ordinary partnership and (or) suretyship and (or) shareholders agreement and (or) other agreement the subject of which is execution of rights certified by shares of the controlled entity*[4]*)* more than 50 percent of votes in the highest management body of the controlled entity or has a right to appoint (elect) the sole executive body of a company and (or) more than 50 percent of members of the collective managing body of the controlled entity. The controlled person (controlled entity) is a legal entity which is under direct or indirect control of the controlling person.

These changes of approach according to which persons shall be deemed to be interested in a deal will allow to avoid situations when transactions considered as

[4] Italics added.

interested party deals just formally (not containing any conflict of interests in fact) require corporate approval of company management bodies.

However, the above mentioned problem of a factual conflict of interests (not provided for by the law) has not been fully eliminated. As L. D. Ebralidze aptly notes "….impact of factual circumstances on a situation in each case plays an important role. It is not possible to specify the whole infinite set of such circumstances in legal norms. Up to the present time, all attempts of the legislator to "seize the unseizable" have not been successful"[5].

Under such conditions, the list of persons who may be deemed to be interested in a deal shall be made in-exhaustive. In other words, the law shall provide for a possibility to consider a transaction as the interested party deal in other cases when a factual conflict of interests takes place. But it is very important that in this case the burden of proof of a factual conflict of interests shall lie with the plaintiff.

Information Concerning Interest in the Conclusion of a Transaction by a Company. Besides, one more solution to the problem of a factual conflict of interests (not provided for by the law) could be found in requirements to information disclosure. In particular, it is necessary to impose upon the interested person (manager, shareholder, etc.) a duty of identifying a conflict of interests and disclosing information in respect of such a conflict with a possibility to apply sanctions in a case of breach of this duty.

At present, the duty of an interested person to disclose information concerning a conflict of interests to some extent is established by the Law "On Joint-Stock Companies". Interested persons (specified in Article 81 of the Law) shall be obliged to inform the company concerning: legal entities in which they, their spouses, parents, children, siblings and half brothers and sisters, step-parents and step-children and/or their controlled entities are controlling persons or entitled to issue binding directions; legal entities in whose management bodies they, their spouses, parents, children, siblings and half brothers and sisters, step-parents and step-children and/or their controlled entities hold office; transactions known to them to be concluded or proposed in which they may be deemed to be interested persons (Article 82 of the Law).

This article has been slightly amended in respect of the notification procedure and terms for such notification. However, it still deals only with interested party transactions (a formalized conflict of interests) and not with a factual conflict of interests (not provided for by the law); neither does it contain any sanction in a case when relevant notification has not been made. The only consequence in respect of

[5] L.D. Ebralidze. Affiliates as a Legal Institute and Legal Measure to Regulate a Conflict of Interests in Business Activity: Author's Abstract … Cand.Sc.Law. Kazan, 2014. P.28.

the notification is stipulated in Article 84 of the Law "On Joint-Stock Companies" and connected just with a case of recovery of damages (see below). Therefore, this norm to a certain degree has a declarative nature.

Notification Instead of Approval of an Interested Party Deal

Former Article 83 of the Law "On Joint-Stock Companies" provided for quite a complicated procedure for the approval of an interested party deal. Moreover, this approval had to be preliminary. According to the latest amendments, there is no need of such approval. An interested party deal does not require approval before its accomplishment any more. Instead, before an interested transaction is concluded, a joint-stock company shall make obligatory notification in regards to such a deal to the members of a board of directors (supervisory board) of a company, members of the collective executive body of a company or to shareholders (in a case if all the members of the board of directors (supervisory board) of a company are deemed to be interested persons or if the board of directors (supervisory board) has not been formed in accordance with the law or the charter).

Once notification has been made, a proposed interested party deal may be approved in accordance with Article 83 of the Law "On Joint-Stock Companies" upon the demand of a sole executive body of a company, a member of the collective executive body of a company, a member of the board of directors (supervisory board) or a shareholder (shareholders) who has no less than one percent of the voting shares of a company.

At first sight, the new procedure of an interested party deal accomplishment seems to be more effective than the previous one to the extent that it will allow joint-stock companies to avoid approval of many deals which are just formally deemed to be interested party deals, but, in fact, do not include any real conflict of interests.

However, being considered closer, this reduced procedure is fraught with some negative consequences.

Firstly, notification in respect of an interested party deal shall be sent to relevant persons not later than 15 days before the closing date. But the charter of a company may provide for some other period of time for such notification to be made. This means that if the charter of a company stipulates, for instance, just 1 or 2 days period, those relevant persons will simply have no time to direct to a company their requirements of an interested party deal approval before the closing date. Therefore, there will be no possibility of ex-ante control over deals with a conflict of interests. In such a case, there is a high risk that rights and interests of minor shareholders (who have no votes enough to affect the resolution of the charter's amendments) will be violated.

Secondly, there are only two cases when notification concerning an interested party deal shall be directed to shareholders, whereas there are much more cases

when interested party deals have to be approved on the level of shareholders. For example, the decision to approve an interested party deal shall be adopted by the general meeting of shareholders by a majority of votes of all the shareholders not interested in the deal who are owners of voting shares if the subject matter of the deal or several interconnected deals is assets of which the value according to accounting data (the offer price of the asset) makes up 10 and more percent of the balance sheet value of the company's assets according to its financial statements as of the last accounting date. But in such cases, notification in respect of an interested party deal shall not be sent to shareholders. **Thus,** shareholders may not even know about such transactions although it is their level of approval.

Taking aforesaid into account, it may be concluded that updated provisions regarding the procedure of concluding interested party deals intend to be for the benefit of joint-stock companies management and major shareholders, whereas interests of minor shareholders were better protected by the previous version of the law. In order to keep the balance between interests of these two groups, it is proposed to set an imperative term of notification concerning an interested party deal which may not be changed by the charter of a joint-stock company. This term shall be no less than 1 month since the present term of 15 days seems to be too short, bearing in mind how much time is required for a post correspondence. Besides, notification in respect of an interested party deal shall be addressed to shareholders not only in two mentioned cases, but also in all the times when an approval of a proposed interested party deal is under their competence.

Option not to Apply the Provisions in Respect of Interested Party Deals

According to the latest amendments, the charter of private (non-public) joint-stock companies may provide a different procedure of concluding interested party deals than the procedure provided for by the Law "On Joint-Stock Companies" or may stipulate that the provisions of the law concerning interested party deals are not applied to a certain company (such provisions of the charter shall be adopted by resolution of all shareholders of a company).

It appears that such a dispositive (discretionary) approach is not a proper measure for the purpose of regulating any relations complicated by a conflict of interests on the whole.

Discretionary nature is one of the main features of the method of civil law regulation. The discretionary approach is most widely used in relations with participation of business entities, including joint-stock companies. However, such discretion conferred on corporations needs to be limited since, if one person has unbounded discretion, it automatically leads to violation of the interests of the other. Therefore, the law shall establish a certain balance between dispositivity and

imperativeness as well as reasonable grounds which allow receding from this balance in some cases.

In particular, imperative regulation shall be aimed to provide the equal status for persons with different economic or physical positions or, at least, to minimize consequences of such inequality. This is the reason for use of imperative regulation in relations including a conflict of interests.

For instance, according to the law, members of regulatory bodies of a joint-stock company must, when exercising their rights and performing duties, operate in the interests of a company. This means that activity of members of regulatory bodies should be completely geared to the company's interests and shall not be intended to serve their own interests or interests of any third party. Regulatory bodies shall prevent a conflict of interests in their activity and if it arises they have to act wholly for the purposes of a company.

In such a way, the law establishes the priority of the common corporate interest. As it might appear at first sight, establishment of such a priority of the common corporate interest over individual interests of members of regulatory bodies contradicts the principle of legal equality. However, such contradiction is necessary and reasonable. It is intended to adjust the status of a joint-stock company as a person at law since a legal entity, being to a certain extent artificial person, has no opportunity to exercise its rights and realize its interests directly (corporate interest can be realized only indirectly by specially set-up corporate bodies) and, therefore, it is initially in a "losing position" in comparison with an individual. Imperative norms in this case are aimed to allow corporate interest to be realized fully and properly in civil circulation.

Necessity to adjust the status of a legal entity determines that the discretion in regulation of relations including a conflict of interests shall be applied in strictly limited volume.

The above is equally applicable to the regulation of interested party deals. A joint-stock company (including non-public joint stock companies) is a pooling of capitals. Number of stockholders of this legal entity is not limited by law. It is not possible to leave such a company otherwise than by selling its shares. Shares of some joint-stock companies are part of a quick turnover; they could be sold many times. In these circumstances, it is highly important to secure common corporate interest (interest of a company itself) as well as interests of its future investors. In this light, the option not to apply the legal provisions in respect of interested party deals tends to be a potential hazard of violation of the rights of a company and its investors.

Although not to the full extent, but the provisions regarding interested party deals allow revealing conflicts of interests, suspending an interested person from a transaction and, thus, preventing potential losses of the interested party deal. In the

absence of these provisions, if any damages are caused by the interested party deal a company may just claim for damages and it is not possible to hold a deal invalid and give assets back to a company. However, bearing in mind Russian judicial practice of the damages' recovery and lack of the development of managers' liability insurance, the way of recovering damages unlikely could be considered to be fruitful[6].

Challenging the Interested Party Deals and Recovery of Damages

Special defensive legal mechanisms applied in respect of the relations with a conflict of interests are declaration of the avoidable interested party deal as invalid and recovery of damages from the interested person.

In order to declare the interested party deal invalid, it is necessary to prove not only existence of a conflict of interests itself but also harm the company's interests. According to the former version of the law, both of these facts had to be proved by the plaintiff. Such apportionment of the burdens was wrong and unfair and has been highly criticized in academic literature[7]. If the undisclosed and unapproved conflict of interests has been proven by the plaintiff, harm to the company's interests has to be presumed. This presumption should be overcome by the other party.

In terms of the current system of legislation, the absence of such a presumption practically brings to nothing the motivation to use the given special defensive mechanism as long as there is general norm of part 2 of Article 174 of the Civil Code of the Russian Federation[8] which may be used in order to declare a deal violating the company's interests invalid. This general norm does not require proving any conflict of interests. Therefore, the application of this article seems preferable from the point of simplicity of the proof process.

The presumption of harm to the company's interests (if there is a deal with a conflict of interests) has been established by the latest amendments of the Law "On Joint-Stock Companies" (updated Article 84). These amendments shall be considered as reasonable and fair.

Besides, the legal norm, according to which an interested person shall bear responsibility to a company in the amount of losses caused by him, has been amended. The important changes have concerned the presumption of guilt of the interested person if harm to the company's interests has occurred. At present, guilt of the interested person on damages has to be presumed if this person has broken his

[6] For more details of the principles of regulating relations with a conflict of interests, see: M.A.Mazo. Conflict of Interests in Joint-Stock Companies (Civil Law Aspect). Cand.Sc.Law. Yekaterinburg, 2016, pp.91-109.

[7] A.A. Kuznetsov. Challenging Major Deals and Interested Party Deals: General Comments // Newsletter of the Supreme Arbitration Court of Russian Federation. 2014. No.2. Pp.14 — 15.

[8] Civil Code of the Russian Federation. Part One.// Collection of Legislation of the Russian Federation. 1994. No.32. Article 3301.

obligation to notify a company concerning circumstances, according to which this person may be deemed to be interested in a deal. In compliance with the above logic in respect of the presumption of harm in the interested party deal, this amendment seems to be proper as well.

Scope of Regulation of the Relations Complicated by a Conflict of Interests

In conclusion, one crucial problem should be pointed out. This problem goes beyond the scope of interested party deals. The case is that the concept of a conflict of interests is outside the framework of civil law deals as such. It means that a conflict of interests could also arise in respect of other legal facts. A conflict of interests could be observed, for instance, in concluding labor contracts, agreements of lawsuit, confession of an action, abandonment of an action, resolutions of corporate meetings (shareholders or board resolutions). As early as in 2014, some of these facts were officially mentioned in the Resolution of the Plenum of the Supreme Arbitration Court of the Russian Federation[9]. However, they still have not been provided for by the law in the context of a conflict of interests.

To this extent, the provisions of the Code of Corporate Governance[10] regarding its approach to the conflict of interests seem to be more effective in comparison with the provisions of the law. According to Article 128 of this document, a conflict of interests is understood as any contradiction between interests of a company and personal interests of a member of board of directors or a member of collective executive body of a company or a sole executive body of a company (any direct or indirect personal interests or interests for the benefit of a third party including interests connected with business, friendship, family and other social relations, positions in other legal entities, possession of shares of other legal entities, contradictions between duties in a company and duties in respect of another person). These provisions have more general nature and could be applied to all situations where a conflict of interests (whether factual or formalized, whether in respect of the deal or not) could take place. However, the Code of Corporate Governance and its provisions are advisory rather than mandatory.

Taking all the aforesaid into account, it must be said that the concept of a conflict of interests in general and, in particular, interested party deals, need further doctrinal consideration.

---

[9] Resolution of the Plenum of the Supreme Arbitration Court of the Russian Federation of 16 May 2014 No.28 "On Some Aspects of Challenging Major Deals and Interested Party Deals"// Newsletter of the Supreme Arbitration Court of the Russian Federation. 2014. No.6.

[10] Letter of the Bank of Russia of 10 April 2014 No.06-52/2463 "On the Code of Corporate Governance" No.40.

THE ALGORITHM OF INVESTOR RIGHTS PROTECTION ACTION CLASSIFICIATION AT STOCKS AND BONDS

Marina A. Rogaleva
Independent Lawyer

Abstract
An algorithm aimed at classification of civil action proceedings can be developed. The elements of the legal action (cause of action, subject of action, litigants (plaintiff and defendant)) form four groups of features necessary and sufficient to form the basis of juridical classification of civil cases.

Keywords: legal cause of action, actual cause of action, subject of action, claim for compensation (for enforceable judgment), claim for declaration of right (sans enforceable judgment), plaintiff, defendant.

Classification is a kind of "intellectual technology" which makes it possible to replace intuitive judgments with certain algorithms (or the rules of problem solving)[1].

Legal (juridical) classification consists of relating a particular case to a suitable general provision in order to deduce the solution[2].

The general theory of crime classification by V.N. Kudriavtsev works in criminal procedure science. It describes the algorithm (operating procedure) for crime classification by law enforcement machinery and criminal court. An analogous theory for civil cases classification has not been developed yet, although the general theory of classification must be intersectoral, or more exactly, a general legal phenomenon.

V.N. Kudriavtsev assumed that every criminal case has a unique legal qualification[3]. It is undeniably correct for civil proceedings, too.

Unlike criminal proceedings, in which all the questions are solved by preliminary investigation authorities, the public prosecutor's office and the criminal court, in civil proceedings a tentative legal classification is performed by litigants and the final legal classification is carried out by the civil court.

Legal classification has legal grounds.

[1] Bell D. Griadushchee postindustrial'noe obshchestvo. Opyt social'nogo prognozirovaniia [Forthcoming Postindustrial Society. Experience of Social Forecasting] M.: Academia, 2004. P.39.

[2] Petrazhickij L.I. Teoriia prava i gosudarstva v sviazi s teoriei nravstvennosti [Theory of Law and State in Connection with Morality Theory] St.P.: Izdatel'stvo Lan', 2000. P.193.

[3] Kudriavtsev V.N. Obshchaia teoriia kvalifikatsii prestuplenii [The General Theory of Crime Classification] M.: Jurist, 2006. P.44.

A great achievement of criminal law science is the discovery of the uniform structure of all kinds of crimes; this structure becomes the basis of *corpus delicti* which contains four main groups of features: the object of crime, the criminal, the objective element in crime, and the mental element in crime. The *corpus delicti* structure is important for classification because it gives an opportunity to create some general classification principles[4].

Is it possible to discover a uniform structure in the infinite variety of civil cases? Can this structure become the basis for classification?

Legal action consists of the following elements — the cause of action, the subject of action, and litigants (plaintiff and defendant). In practice, these elements are means of individualization, as they help to distinguish between actions[5].

In our opinion, the elements of action (the cause of action, the subject of action, plaintiff and defendant) group four necessary and sufficient features to classify all civil cases.

Substantive basis of division is chosen for the civil procedure classification by an analogy with the criminal procedure. Indeed, the substantive type of cause and subject of action is unquestionable[6]. Litigants (in civil and arbitration proceedings) presumably are parties to a litigious substantive relationship, unless the contrary is proved in the course of proceedings.

Each of the four features helps to classify cases and differentiate them[7]. Therefore, every element is the basis for differentiation. Civil cases can be differentiated using one of them, two, three or all the elements (integrated differentiation).

In criminal proceedings, the object of analysis carried out by the classifying subject is crime itself. In civil proceedings, the object is the litigious substantive relationship which presumably links litigants; it is identical with the actual cause of action.

1. Cause of action

The actual cause of action is the bench mark of the procedure; it conditions plaintiff's claims, defendant's answers, and legal investigation of this civil case.

[4] Kudriavtsev V.N. Obshchaia teoriia kvalifikatsii prestuplenii [The General Theory of Crime Classification] M.: Jurist, 2006. P.59-60.

[5] Osokina G.L. Grazhdanskii protsess. Obshchaia chast' [The Civil Process. General Part] M.: Norma, 2008. P.499-500.

[6] Zheroulis I.A. O sootnoshenii material'nogo i protsessual'nogo v iske [On the Correlation between Substantive and Procedural Aspects in the Claim]/ I.A. Zheroulis// Formy zashchity prava i sootnoshenie material'nogo i protsessual'nogo v otdel'nykh pravovykh institutakh: Mezhvuzovskii tematicheskii sbornik [Forms of Law Protection and the Correlation between Substantive and Procedural Aspects in Separate Law Institutes: Inter-University Collection on the Subject] Kalinin, the Kalinin State University, 1977. P.15.

[7] Kudriavtsev V.N. Obshchaia teoriia kvalifikatsii prestuplenii [The General Theory of Crime Classification] M.: Jurist, P.62.

Classifying subjects' (litigants and court) reasoning consists of "recognition" of the actual cause and establishment of the correspondence between the actual cause and legal cause of action[8].

Cause of action is the main basis for classifying and differentiating civil action proceedings, which certainly does not exclude the significance of the other elements of action (subject and litigants).

As a rule, personal right is based not on a single juridical fact, but on their totality; it means, that cause of action includes a certain combination of juridical facts[9].

Legal cause of action forms circumstances in proof[10], as well as influences on allocation of burden of proof between litigants, conditions the choice of the defendant, jurisdiction of the case, limitation period, security for a claim.

Therefore, tentative legal classification plays a key role in the course of proceedings, and neither the plaintiff nor the defendant can read a case without it. Litigants are obliged to define a legal cause of action due to the permissive foundation of civil and arbitration proceedings.

Infringements of investor's rights are connected with ownership of security or the right provided in security[11]. As far as securities circulate through the equity market, cause of action is always based on investment relations connected with equity market. The legal cause of action is the property rights embodied in substantive law; the actual cause of action is the fact of infringement of these rights.

2. Subject of action

The legitimate interest of litigants concerns the subject of action: what the plaintiff can claim and what the defendant must endure.

So long as equity market is the system of liabilities, investors have the right to sue in case of a contract breach.

Indeed, in order to protect rights of claim, which constitute the substance of a security, actions may be taken in case of the contract breach. Legal actions for restitution are taken to protect the ownership of securities.

---

[8] A legal norm itself can become an object of classification: the classifying subject relates a specific norm with a general norm (or with an institution, a branch of law). The branch of law that a norm belongs to should be determined primarily on the basis of its content and optionally on the source of its fixation.

[9] Grazhdanskii protsess [Civil Proceedings]/ edited by V.V. Yarkova. — M.: Volters Kluver, 2009. P.271.

[10] Puchinskii V. Otsenka dokazatel'stv v rossiiskom grazhdanskom i arbitrazhnom protsessual'nom prave// Hoziaistvo i pravo [The Assessment of Evidence in the Russian Civil and Arbitration Procedural Law. //Economy and Law]. 2005. No.6. P.35-36.

[11] Zashchita prav investorov v sfere rynka tsennykh bumag [The Protection of Investors' Rights in the Sphere of Securities Market]/ edited by M.K. Treushnikova. M.: Izdatel'skii Dom Gorodets, 2009. P.45-46.

However, in order to protect the ownership of securities, property suits and tort suits are initiated too. Therefore, it is important to classify cases and differentiate them at the same time.

The subject of action is the method of defense chosen by the plaintiff; a pecuniary claim of the plaintiff to the defendant, based on a litigious substantive relationship[12]. Protection of civil rights can be exercised only by methods explicitly stated by substantive civil law (Art.12 of the RF CC). The plaintiff can choose the method[13] that, in his opinion, will repair the breach of his subjective civil right or legal interest.

It is impossible to choose the method of defense arbitrarily or to substitute one method by another randomly. Firstly, the method of defense can be directly specified in the applicable substantive law. Secondly, this method can be stipulated in the contract concluded by the litigants. Thirdly, the choice of a method is conditioned by the actual cause of action.

Most methods of investors' rights protection can "boil down" to those provided in Art.12 of the RF CC, except those embodied in the equity market laws.

The subject of action forms the basis for procedural classification. All methods of defense can be divided into two groups: claims for compensation (with executive power) and claims for declaration of the right (without executive power). In turn, the subject of action to compensation calls forth special features of execution.

3. Litigants

Litigants as an element of action define the case concerning the prosecuting and defending parties in the action[14].

All actions connected with the equity market can be divided into individual actions and class actions. The ground for classification is the question whose rights and interests are protected in court[15].

Individual action is always initiated and prosecuted by the substantive plaintiff (holder of securities, investor).

[12] Vershinin A.P. Vybor sposoba zashchity grazhdanskikh prav [The Choice of a Remedy of Protecting Civil Rights] St.P.: Spetsial'nyi iuridicheskii fakul'tet po perepodgotovke kadrov po iuridicheskim naukam Sankt-Peterburgskogo gosudarstvennogo universiteta [Special Law Faculty on Retraining the Specialists in Legal Sciences of the St.Petersburg State University], 2000. P.16; Grazhdanskii protsess. P.269; Osokina G.L. Grazhdanskii protsess. Obshchaia chast' [Civil Proceedings. General Part]. P.500; Sakhnova T.V. Kurs grazhdanskogo protsessa: teoreticheskie nachala i osnovnye instituty [The Course of Civil Proceedings: Theoretical Basics and Major Institutions] M.: Volters Kluver, 2008. P.295.

[13] Vershinin A.P. Vybor sposoba zashchity grazhdanskikh prav [The Choice of a Remedy of Protecting Civil Rights] P.22-23.

[14] Osokina G.L. Grazhdanskii protsess. Obshchaia chast' [Civil Process. General Part]. P.507.

[15] Grazhdanskii protsess. P.277.

Class action is commenced and prosecuted by the procedural plaintiff (sans his own interest in the case outcome). Class actions are sued for the plaintiff's substantive rights protection; the standing of the procedural plaintiff is connected with his executive discretion or by-laws.

Derivative action is commenced to protect a joint-stock company. The substantive plaintiff is absent in structure of actions for indeterminate group protection as well as in that of actions for public interest protection.

Therefore, along with the cause of action, the procedural status of the substantive plaintiff is the main feature.

The special status of the defendant may also become an essential feature for some cases. For example, if the defendant is a bidder in stock exchange, he must have a valid license. In case of initiating a derivative action, the defendant is a sole or joint authority of a joint-stock company.

ROLE OF A WARRANTY PERIOD FOR THE LEGAL ENSURING OF THE QUALITY OF THE GOODS SUPPLIED UNDER A CONTRACT

Albina S. Panova
PhD (Law), Associate Professor,
Head of the Civil and Entrepreneurial Law Department,
Kazan Innovative University named after V.G. Timiryasov (IEML),
Kazan, Russia

Abstract
The article is devoted to the aspects of a warranty period. Its significance is shown for the legal ensuring of the quality of goods supplied under a contract.

Keywords: goods quality, delivery contract, warranty bond, warranty period, standard, technical regulation.

The compliance of the delivered product to the sales contract is a presumption in a majority of national legal systems. Such presumption is stipulated in the Civil Code of the Russian Federation (further — the RF CC) (clause 1 Art.469)[1]. This presumption is supported by a rule that a seller (supplier, producer) has a right to provide a warranty of the goods quality, which is in the form of a warranty bond. Within the warranty bond, the seller must provide the compliance of the goods with the terms of the contract concerning its quality, and in case of revealing defects in the product (breach of warranty) the seller must remove the defects, or replace the goods of improper quality by the ones complying with the terms of the contract. The existence of a warranty bond is determined by a certain time period — the warranty period. There is no common approach to interpreting the warranty period in the Russian juridical science. Some authors interpret the warranty period as the prolonged period for revealing latent defects (Kh.E. Bakhchisaraytsev[2], E.A. Fleyshits[3]). Other scholars

[1] Civil Code of the Russian Federation. Part 2 / Federal Law of January 26, 1996 No.14-FZ (as amended on 23 May 2016) // Collection of Legislation of the Russian Federation. 1996. No.5. Art.410; 2016. No.22. Art. 3094.

[2] Bakhchisaraytsev Kh.E. Pravila o garantiinykh srokakh i povyshenie kachestva promyshlennoi produktsii// Sovetskoe gosudarstvo i pravo [Rules on Warranty Periods and Increasing the Quality of Industrial Production // Soviet State and Law]. 1963. No.1. P.114.

[3] Nauchno-prakticheskii kommentarii k osnovam grazhdanskogo zakonodatel'stva Soyuza SSR i soyuznykh respublic [Scientific-Practical Comment to the Fundamentals of the Civil Law of the USSR and the Union Republics]// edited by prof. S.N. Bratus' and prof. E.A. Fleyshits. Moscow: Gosyurizdat, 1962. P.213.

state that the warranty period is a period for reclamation (R.O. Khalfina[4]). What both positions have in common is the retrospective aspect of interpreting "the warranty period". Actually, in the retrospective way the warranty period is interpreted by S.G. Khinoy[5], V.F. Yakovleva[6], S.D. Pokrevskaya[7], L.I. Broslavskiy[8] and other scholars[9].

Another viewpoint is that warranty periods are time periods during which a producer (supplier) guarantees the good quality of the product (on the condition of proper storing and using). In this case, the emphasis is made on "positive interpretation" of the warranty period. Thus, according to M.N. Semyakin, the essence of the warranty period is that it is connected with the occurrence of the secured (guarantee) liability, where the most essential are the guarantee liabilities of a producer (supplier) for the proper level of the product quality[10]. V.S. Shelestov highlights that the warranty period of exploitation is a time period during which, under certain regimes and conditions of exploitation, a producer provides reliable functioning of technical equipment[11]. N.A. Yakhnina states that the warranty period should be defined as a time period during which a producer guarantees non-failure functioning of the item, i.e. as the warranty liability of a producer to provide the stable quality characteristics of the product during a certain time period[12]. A fault of definition by N.A. Yakhnina is that it actually identifies the notions of "the warranty period" and the "the warranty bond". However, "the warranty period" is one of the conditions of the warranty bond existence, whereas "the warranty bond" itself is a

[4] Khalfina R.O. Pravovoe regulirovanie postavki produktsii v narodnom khoziaistve [Legal Regulation of Products Delivery in People's Economy] Moscow: Academy of Sciences of the USSR, 1963. P.201.

[5] Khinoy S.G. Rol' garantiinykh srokov v povyshenii kachestva produktsii. V kn.: Aktual'nye voprosy sovetskogo grazhdanskogo prava. [Role of the Warranty Periods in Increasing the Production Quality. From the book: Topical Issues of Soviet Civil Law]. Moscow: Yurid.lit., 1964. P.102–104.

[6] Dogovory v sotsialisticheskom khoziastve [Contracts in Socialistic Economy] / O.S. Ioffe, N.V. Rabinovich, V.F. Yakovleva et al. / exec. editor O.S. Ioffe. Moscow: Yurid.lit., 1964. P.162.

[7] Pokrevskaya S.D. Garantiinyi srok kak uslovie dogovora roznichnoi kupli-prodazhi i prava pokupatelei [Warranty Period as a Term of Retail Sales Contract and the Consumers' Rights]// Scholarly Notes of All-Union Scientific-Research Institute for Soviet Legislation. Iss.28. Moscow, 1973. P.215.

[8] Broslavskiy L.I. Otvetstvennost' predpriiatii za narushenie standartov [Liability of Enterprises for Violation of Standards]. Moscow: Izd-vo Standartov, 1988. P.121.

[9] See: Soviet Civil Law: textbook / edited by D.M. Genkin and Ya.A. Kunik. Moscow: Higher School, 1967. P.301; Ring M.P. Dogovory na nauchno-issledovatel'skie i konstruktorskie raboty [Contracts for Scientific-Research and Development Works]. Moscow: Yurid.lit., 1967. P.128.

[10] Semyakin M.N. Grazhdansko-pravovye formy (sredstva, sposoby) upravlenia kachestvom produktsii v sisteme khoziastvennogo mekhanizma [Civil-Legal Forms (Means, Techniques) of Managing the Product Quality in the System of Economic Mechanism]: Doctoral (Law) Thesis. Sverdlovsk, 1991. P.314–315.

[11] Shelestov V.S. Garantiinye sroki v dogovorakh postavki // Pravovedenie [Warranty Periods in Delivery Contracts // Law Studies]. 1965. No.3. P.44.

[12] Yakhnina N.A. Znachenie garantiinykh srokov v povyshenii kachestva produktsii// Sovetskoe gosudarstvo i pravo [Role of Warranty Periods in Increasing the Production Quality // Soviet State and Law]. 1966. No.7. C.94.

civil legal relation, presupposing execution of a certain set of rights and liabilities. I.N. Petrov suggests interpreting the warranty period as a condition of the goods quality, according to which a producer (supplier) guarantees (under the conditions of proper storing and exploitation of the supplied goods) the compliance of its quality with the requirements of the State Standard, technical conditions or the contract during the time period defined by them[13]. A similar opinion on the essence of the warranty period is shared by L.T. Kuklin[14], M.B. Emelyanova[15], L.M. Rutman[16], I.V. Eliseev[17].

There are viewpoints uniting the "retrospective" and "positive" aspects in defining the essence of the warranty period. Thus, O.S. Ioffe wrote that a warranty period has a dubious juridical meaning. On the one hand, it is the period of operating, i.e., the time period during which a consumer is guaranteed the standard functioning of the item under proper storing and using. On the other hand, it is the period for revealing the defects in the supplied items and reclamations to a supplier[18]. Similar opinion is shared by V.P. Gribanov[19], V.A. Yazev[20].

The RF CC (clause 2 Art.470) interprets the "warranty period" as a special time period of implementing civil rights. By the conception of the RF CC (§1 Ch.30 "General Provisions on Sales"), the warranty period is the time stipulated in the contract, according to which the goods must comply with the requirements stipulated by Art.469 of the RF CC. This interpretation of the warranty period is typical, first of all, for the relations of supply. The definition of a "warranty period"

[13] Petrov I.N. Reglametatsia garantiinykh srokov kachestva produktsii// Sovetskoe gosudarstvo i pravo [Regulation of the Warranty Periods of the Production Quality // Soviet State and Law]. 1968. No.11. P.81.

[14] Kuklin L.T. Rol' garantiinogo sroka v povyshenii kachestva produktsii / Iz. sb.: Pravovye problemy upravlenia kachestvom produktsii na baze standartizatsii i meteorologicheskogo obespechenia [Role of the Warranty Period in Increasing the Production Quality / From a collection of works: Legal Issues of Production Quality Management Based on Standardization and Meteorological Provision]. Sverdlovsk, 1979. P.278.

[15] Emelyanova M.B. Standarty i kachestvo produktsii (pravovoi aspekt problemy) [Standards and Quality of Products (Legal Aspect)]. Moscow: Izd-vo Standartov, 1971. P.120–121.

[16] Rutman L.M. Garantiinye sroki i otvetstvennost' za kachestvo produktsii pri kooperirovanykh postavkakh / Iz. sb.: Pravovye problemy upravlenia kachestvom produktsii na baze standartizatsii i meteorologicheskogo obespechenia [Warranty Periods and Liability for the Production Quality in Cooperated Delivery / From a collection of works: Legal Issues of Standardization, Metrology and Quality of Products. Works of All-Union Scientific-Practical Conference (November 15–17, 1971). Moscow: Izd-vo Standartov, 1972. P.193.

[17] Grazhdanskoe pravo: Uchebnik [Civil Law: Textbook]. Part II / edited by A.P. Sergeev, Yu.K. Tolstoy. Moscow: Prospekt, 1998. P.27.

[18] Ioffe O.S. Obiazatel'stvennoe pravo [Law of Obligations]. Moscow: Yurid.lit., 1975. P.257–258.

[19] Gribanov V.P. Osushchestvlenie i zashchita grazhdanskikh prav [Implementation and Protection of Civil Rights]. 2nd stereotyped edition. Moscow: Statut, 2001. P.274.

[20] Yazev V.A. Otvetstvennost' prodavtsa za nadlezhaschee kachestvo prodannykh tovarov [The Seller's Liability for Improper Quality of the Sold Goods]. Moscow: Yurid.lit., 1964. P.21.

contained in Federal Law of the Russian Federation of 7 February 1992 No.2300-1 "On Consumers' Rights Protection" (further — the Law on Consumers' Rights Protection) (clause 6 Art.5)[21], is of protective character. According to the Law on Consumers' Rights Protection, this is a period during which, in case of revealing a defect in the product (service), the producer (supplier), seller, authoritative organization, or importer are obliged to satisfy the demands of the consumer stipulated in Articles 18 and 29 of the Law. Such demands include exchanging the goods for the goods of the same brand and/or nomenclature; exchanging the goods for the goods of another brand and/or nomenclature with the corresponding recalculation of the purchase price; commensurate reduction of the purchase price, etc. Actually, the same protective interpretation of the warranty period is typical for the European consumer law: within the warranty period, a seller or producer (supplier) is obliged to reimburse to the consumer the purchase price or to exchange or fix the consumer goods if they do not comply with the specifications stipulated in the warranty statement or corresponding advertisements[22]. We believe that the emphasis on the protective character of the "warranty period" is due to the fact that legislation on consumers' rights protection is aimed at ensuring the priority of consumers' interests in their relations with producers (sellers, executors)"[23]. Consumer legislation is characterized by enforcement of "legislative protection of the interests of citizens-consumers"[24]. The European legislator proceeds from the assumption that "stable consumer demand for goods, works and services is one of the most important incentives of the market economy

[21] Law of the Russian Federation of 7 February 1992 No.2300-1 "On Consumers' Rights Protection" (as amended on 3 July 2016) // Bulletin of the Council of People's Deputies and the Supreme Court of the Russian Federation. 1992. No.15. Art.766; Collection of Legislation of the Russian Federation. 2016. No.27 (part 1). Art.4198.

[22] Directive 1999/44/EC of the European Parliament and of the Council of 25 May 1999 on certain aspects of the sale of consumer goods and associated guarantees // Official Journal L 171, 07/07/1999 P. 0012-0016; The Sale and Supply of Goods to Consumers Regulations 2002 (UK)// http://www.legislation.gov.uk/uksi/2002/3045/regulation/5/made.

[23] Sherstobitov A.E. Yuridicheskie garantii okhrany prav potrebitelei v dogovornykh otnosheniiakh/ Iz.kn.: Sfera uslug: grazhdansko-pravovoe regulirovanie: sbornik statei [Juridical Warranties of Consumers' Rights Protection in Contract Relations / from the book: Services Sphere: Civil-Law Regulation: Collection of Works] / A.V. Asoskov, A.V. Barkov, A.A. Boger et al.; edited by E.A. Sukhanov, L.V. Sannikova. Moscow: Infotropik Media, 2011. P.32; Ibid. Grazhdanskoe zakonodatel'stvo Rossiiskoi Federatsii i zakonodatel'stvo o zashchite prav potrebitelei: sootnoshenie i problemy primenenia/ Iz.kn.: Osnovnye problemy chastnogo prava. [Civil Law of the Russian Federation and Legislation on Consumers' Rights Protection: Correlation and Problems of Application / from the book: Basic Issues of Private Law]. Collection of works for the jubilee of Doctor of Law, Professor Aleksandr L'vovich Makovskiy/ exec.editors V.V. Vitryanskiy, E.A. Sukhanov. Moscow: Statut, 2010. P.374.

[24] Puginskiy B.I. Kommercheskoe pravo Rossii: uchebnik [Commercial Law of Russia: Course book]. Moscow: Yurait-Izdat, 2009. P.177.

growth. That is why the reliability of legal provision of the consumer's party is one of the most important incentives of the preservation and increasing the demand"[25].

During the warranty period stipulated by the delivery contract, the parameters and properties of the goods should be preserved which characterize their ability to perform the required functions in certain regimes and conditions of exploitation (storing, transportation). These parameters and properties are usually stipulated in the contract by citing the standards or technical conditions (further — TC) of a manufacturing plant. The interconnection of the warranty period and reliability is obvious. Specialists correctly underline several aspects of the reliability problem: technical, economic and legal. The technical aspect of the problem is setting the requirements for reliability, content and general rules of reliability requirement[26], and the order of calculating reliability[27]. The economic aspect is the economic substantiation of these requirements and indicators, taking into account the expenditures for production, exploitation and maintenance which provide the optimal reliability, on the basis of physical deterioration and moral obsolescence. The legal aspect of the problem is in attributing legal authority to the optimal, technically and economically grounded requirements and indicators of reliability, methods of their determination and checking by duly stipulating them in normative-technical documentation[28]. A producer takes into account the achieved level of science, technology, material production, and, based on that level, defines the indicators of the product reliability, including non-failure operation, fatigue life, etc.

Certainly, the warranty period should be a technically grounded term of non-failure operation of the goods proving the reliability of the item; it may perform the function of an incentive as a means of influencing the technical progress. However, it is wrong to connect the warranty period exclusively with the reliability of the goods. By giving the guarantee, a producer (supplier, seller) warrants, first of all, the absence of any latent defects in the goods at the set time. For example, the defects in the item's design, the defects connected with the clearance increase, corrosion, poor coloring due to poor observance of the coloring technique, breaches of thermal conduction, etc. The guarantee of the compliance of the goods quality with the

[25] Grazhdanskoe i torgovoe pravo zarubezhnykh stran: uchebnik [Civil and Trade Law of Foreign Countries: coursebook / edited by V.V. Bezbakh and V.K. Puchinskiy. Moscow: MTsFER, 2004. P.46–47.

[26] State Standard 27.003-90. State Standard of the USSR. Reliability of technical equipment. Content and general rules of setting the requirements to reliability (adopted and enforced by Determination of the State Standardization Agency of the USSR of 29 December 1990 No.3552). Moscow: Izd-vo Standartov. 1991.

[27] State Standard 27.301-95. International standard. Reliability of technical equipment. Calculation of reliability. Main provisions (enforced by Determination of the State Standardization Agency of the Russian Federation of 26 June 1996 No.430). Minsk, 1996.

[28] Emelyanova M.B. Standarty i kachestvo produktsii (pravovoi aspect problemy) [Standards and Quality of Products (Legal Aspect)]. Moscow: Izd-vo Standartov, 1971. P.124.

contract is supported by the liability of a producer (supplier) to remove the defects revealed during the warranty period. The breach of this guarantee results in unfavorable property consequences for the producer (supplier), while granting the buyer a possibility to employ one of the legal protective means stipulated by legislation. Thus, the warranty period has a non-homogeneous (regulative and protective) character, with the priority of the protective aspect.

Under the market economy, the warranty period may serve as a means stimulating the competition between producers, as a marketing tool providing easier marketing of the products. Alongside with that, using the institution of the warranty period should not mislead the buyers as to the quality of goods or limit the buyers in their rights.

Before Federal Law of 27 December 2002 No.184-FZ "On Technical Regulation" was enacted[29], in case of regulation of the warranty period by the state standards, the parties had the right to change the fatigue life of such periods by increasing them. At present, the parties to a delivery contract possess a high level of discretion in solving the question of setting the warranty period and its duration. When setting such periods, the contract parties usually take into account the provisions of the standards. They may also take into account the information contained in TC, technological instructions (maps), and receipts. The parties have a right (but are not obliged) to stipulate in the contracts the warranty periods longer than those stipulated in the standards. In such a case, a supplier (producer, seller) may put a question of increasing the contract price. At present, we do not consider as a breach of legislation the cases when the parties stipulate in the contract the warranty periods shorter than those stipulated in the standard requirements. The parties may include into the contract the term of the warranty period, if there are no provisions as to it in the standards. The warranty periods are not stipulated directly in the technical regulations. Some technical regulations state the necessity to include information on the warranty periods as to the goods, as well as the goods marking[30]. The lists of standards, promoting the implementation of requirements of technical regulations, may include the standards containing information about the warranty periods[31]. Thus, in some

[29] Federal Law of 27 December 2002 No.184-FZ "On Technical Regulation" (as amended on 5 April 2016) // Collection of Legislations of the Russian Federation. 2002. No.52 (part 1). Art.5140; 2016. No.15. Art.2066.

[30] See, in particular, "TP TC 007/2011. The Technical Regulation of the Customs Union "On Safety of Products Intended for Children and Adolescents" (adopted by the decision of the Customs Union Commission of 23 September 2011 No.797) (as amended on 10 June 2014) // Official website of the Customs Union Commission http://www.tsouz.ru/, 30.09.2011; the Technical Regulation of the Customs Union "On Safety of Explosives and Products Based on Them" (adopted by the decision of the Eurasian Economic Commission of 20 July 2012 No.57) // Official website of the Eurasian Economic Commission http://www.tsouz.ru/, 20.07.2012; TP TC 009/2011.

[31] Thus, State Standard P 51068-97 "Children's Latex Nipples. Technical conditions" stipulates the producer's warranty, the warranty period of retention and exploitation of nipples (the standard is

cases, the provisions of standards on the warranty periods are directly connected with the norms of technical regulations, the delivery contract parties strive to implement these provisions making them binding. The duration of warranty periods stipulated by the standards may differ depending on the category (type) of the goods. For example, State Standard No.3251-91 "Underlying rubber-fabric oilcloth. Technical conditions" (the standard is included into the List of Standards for the Technical Regulation of the Customs Union 007/2011 "On Safety of Products Intended for Children and Adolescents") stipulates that the warranty retention cycle of type A oilcloth is 24 months, of type B it is 26 months since the date of manufacture (clause 5.2); the warranty operation life of type A oilcloth is 1 month in healthcare establishments and 6 months if used individually, of type B — 2 months in healthcare establishments and 8 months if used individually since the day of delivery to the consumer (clause 5.3)[32]. The standard norms on the warranty periods may also refer to other standards and provide an opportunity to take into account the opinions of the consumer (buyer) on the duration of the warranty period.

The rules of calculating the warranty periods are stipulated by the RF CC (Art.471). The parties have the right to change the code provisions by their consent. By the general rule, the warranty period starts from the moment of delivery of the goods to the buyer (Art.457 of the RF CC). For example, it can be stipulated in the contract that the warranty period for the equipment, delivered by the contract, starts since the date of signing the act of equipment starting-up and adjustment. In our opinion, of great significance is the proposal that the warranty period for machines and equipment, for which the indicator of productivity is essential, should be calculated not since bringing the item into exploitation, but since achieving the nameplate capacity of the equipment. As a result, the responsibility of developers and producers for the quality of the developed and produced equipment will increase[33]. If a buyer is deprived of an opportunity to use the goods, for which the quality warranty is provided, due to the circumstances depending on the seller, the course of the warranty period should be broken until the moment of removal of such circumstances by the

included into the List of Standards the voluntary application of which provides the observance of the requirements of the Technical Regulation of the Customs Union "On Safety of Products Intended for Children and Adolescents" (TP TC 007/2011); State Standard 21982-76 "Industrial explosives. Protective waterproof ammonites. Technical conditions" stipulates the producer's warranty, the warranty period (the standard is included into the List of Standards the voluntary application of which provides the observance of the requirements of the Technical Regulation of the Customs Union "On Safety of Explosives and Products Based on Them" (TP TC 028/2012).

[32] State Standard 3251-91 "Underlying Rubber-Fabric Oilcloth. Technical conditions" (enacted on 1 January 1993). Moscow: Izd-vo Standartov, 1992.

[33] Belykh V.S. Ischislenie garantiinykh srokov pri postavkakh mashin i oborudovaniia // Standarty I kachestvo [Calculation of Warranty Periods in Machines and Equipment Delivery // Standards and Quality]. 1985. No.6. P.63–64.

seller. The warranty period is extended for the time during which the goods could not be used properly due to the defects revealed in it, if the buyer informs the seller about the defects (according to the rules of Art.483 of the RF CC "Terms of Revealing the Defects in the Delivered Product").

The warranty period for a component is equalled to the warranty period of the main item, and starts simultaneously with it. If during the exploitation period the component fails due to the revealed defects (latent defects), the warranty period of the same duration will be enacted for the new component. The warranty period for the new component starts from the beginning. In practice, there are cases when a supplier includes into the contract the condition, according to which the non-payment for the goods in the period stipulated in the contract leads to the removal of the warranty from the delivered goods. The contract term on the previous cessation of the warranty period due to the non-payment for the goods is null and void, as there is no interconnection between the warranty bond and the liability to pay for the goods; in other words, the existence of the warranty bond cannot be dependent on the fact of a buyer's performance of their obligation to pay[34]. A buyer cannot exercise their rights according to the warranty bond, unless the technical conditions which stipulate the warranty period for a product are ascertained by a seller (director of a manufacturing plant) at the moment of signing a delivery contact. Accordingly, such technical conditions cannot alter the terms of a contract signed prior to their adoption, and the guarantee validity will not be extended to such products[35].

Taking the abovementioned into account, a warranty period can be defined as a specially qualified period, within which a warranty bond is valid, i.e. the guarantee of a producer (supplier, seller) for the non-failure operation of the goods item, product, as well as for the absence of latent defects in the goods. A part of this guarantee is the liability to remove the defects in the product revealed during the warranty period. The parties to a delivery contract have the right to set the warranty periods and their duration *ad libit*. However, when agreeing upon these terms, the supplier and the buyer must take into account the provisions of technical regulations and standards.

[34] Determination of Federal Arbitration Court of North-West district of 21 March 2008 on case No.A42-9963/2003. URL: http://ras.arbitr.ru.

[35] Determination of Federal Arbitration Court of North-West district of 25 May 2009 on case No.A56-22287/2008. URL: http://ras.arbitr.ru.

ELIMINATION OF ACCUMULATED ENVIRONMENTAL HARM IN THE ARCTIC ZONE OF THE RUSSIAN FEDERATION: WHAT RULES SHOULD BE APPLIED?

Inna A. Ignatyeva
Doctor of Law, Professor
Department of the Environmental and Land Law, Law Faculty,
Lomonosov Moscow State University, Russia

Abstract
The new legal norms on the elimination of accumulated environmental harm in the Law on Environmental Protection came into force on 1 January 2017. Now the basic legal concepts were defined in the legislation, related to the liquidation of the harm, the accounting treatment of objects of accumulated environmental harm, regulatory requirements to the implementation of the liquidation operations. But these rules are far from being exhaustive and integrated; there are many gaps in the legal regulation. At the same time, there is another legal regulation which is used for a number of objects in the Arctic. Thus, the new legislative regulation has given rise to many practical problems and issues, the answers to which should come as soon as possible in law additions, in the regulatory legal acts of a sub-level and also interpretations of courts.

Keywords: accumulated environmental harm, accumulated environmental damage, liquidation of accumulated environmental harm, environmental legislation, Law on the Environmental Protection, the Arctic Zone of the Russian Federation.

A substantial part of territories are experiencing a negative impact of environmental harm as a result of the past activities the in the Arctic zone of the Russian Federation (further — the Arctic, the Russian Arctic). The need to eliminate this type of harm (or damage) is manifested most clearly in the aspect of ongoing and future intensification of economic and other activities in the Russian Arctic. It is necessary to solve the problem due to environmental and economic reasons: "The territories contaminated in the past are a deterrent to economic growth, the reason for reducing the environmental ratings of the territories and, as a consequence, a barrier to foreign and domestic investment"[1].

[1] Kharitonova G.N. Problema ochistki morskogo poberezh'ia rossiiskoi Arkticheskoi zony ot istoricheskikh zagriaznenii // Strategiia morskoi deiatel'nosti Rossii i ekonomika prirodopol'zovaniia

The task of eliminating such damage is consistently formulated in the official documents. The solution of the task is scheduled and implemented for quite a long time in accordance with various programs, strategies and other similar documents: the Strategy of Development of the Arctic Zone of the Russian Federation and providing national security for the period until 2020, approved by the President of the Russian Federation on 20 February 2013[2], the State Programme of the Russian Federation "Environmental Protection for 2012-2020"[3], the Action Plan to implement the Strategy for the Development of the Arctic Zone of Russian Federation and providing national security for the period until 2020, approved by the Government of the Russian Federation on 30 August 2016[4], etc.

The State Programme of the Russian Federation "The Socio-Economic Development of the Arctic Zone of the Russian Federation for the Period till 2020"[5] plans repairing the damage resulting from the implementation of the past economic activities on the *Franz-Joseph Archipelago* (collection and disposal of barrels, land recultivation) and implementation of measures on the liquidation of consequences of the past economic activities of the oil and gas producing complex in the *Delta of the Pechora River* in the territory of the state natural reserve "Nenetsky".

The State Report "On the State and Protection of the Environment of the Russian Federation in 2015" lists the necessary works on the elimination of the accumulated environmental damage in the *Murmansk region* (vessels dumps), the *Arkhangelsk region* (rehabilitation of the land, contaminated by petroleum products), the *Republic of Sakha (Yakutia)*, the *Kamchatka region* (rehabilitation of the Avacha Bay), the *Yamalo-Nenetsk Autonomous District* (the former railway station Chircha), in the *state natural reserve "Nenetsky"* and others. Some liquidation works on a number of the identified objects of the accumulated damage have already started or already completed.

The absence of legal regulation in this area has been especially evident against the background of a wide range of tasks to eliminate the accumulated damage to the environment in the Russian Arctic. Therefore, the Federal Law "On Amendments to Some Legislative Acts of the Russian Federation"[6] is so long-awaited and topical.

v Arktike. IV Vserossiiskaia morskaia nauchno-prakticheskaia konferentsiia: materialy konferentsii [Kharitonova G. N. The Problem of Cleaning the Seacoast of the Russian Arctic Zone from the Historic Contamination // Strategy of Maritime Activities of Russia and Economics in the Arctic. The IV All-Russian Maritime Theoretical and Practical Conference: Papers of the Conference]. Murmansk, 7 — 8 June 2012. P.156.

[2] The document was not published. Here and further in the article the texts of normative legal acts were used with information support of the "ConsultantPlus" company.

[3] Government Decree of 15 April 2014 No.326.

[4] Available at: http://www.government.ru.

[5] Government Decree of 21 April 2014 No.366.

[6] Federal Law of 3 July 2016 No.254-FZ.

The amendments made to the Federal Law "On the Environmental Protection"[7] (further — the Law on the Environmental Protection) enable to resolve at least such issues as:

1) the uniform terminology in this sphere;

2) the definition of the concepts of the "accumulated environmental harm", "objects of accumulated environmental harm";

3) the designation of specially authorized federal government bodies, government bodies of the subjects of the Russian Federation, municipal authorities, which must (or are entitled to) organize activities to eliminate the accumulated environmental harm;

4) the establishment of procedures for the elimination of the accumulated environmental harm, etc.

The relevant amendments to the Law on the Environmental Protection came into force on 1 January 2017.

According to Article 1 of the Law on the Environmental Protection, the accumulated environmental harm is the environmental harm which emerged as a result of the past economic and other activities; the obligation to eliminate them have not been implemented or were not implemented in full. **Objects of the accumulated** environmental harm are the territories and water areas where the accumulated environmental harm was identified, and objects of capital construction and waste disposal facilities, which are the source of the accumulated environmental harm.

However, the new definitions from Art.1 of the Law on the Environmental Protection are incomplete, as they contain not all the signs of the accumulated harm that follow from the legal provisions of the new chapter XIV.1 of the Law on the Environmental Protection. For example, according to Art.80.1 of the Law on the Environmental Protection, capital construction facilities and waste disposal facilities must be **ownerless** to identify them as the objects of the accumulated environmental harm. But at the same time, Article 1 of the Law on the Environmental Protection does not mention the characteristics associated with the concept of ownerless items at all.

According to Art.225 of the Civil Code of the Russian Federation, *a thing that has no owner or the owner of which is unknown or if otherwise is not provided by law, the right of ownership to which the owner has refused is an* ***ownerless thing***. Unfortunately, the Law of the Environmental Protection did not solve such questions as:

— at what stage, after what period of time the owner can refuse the objects that are the source of the accumulated environmental damage?

[7] Federal Law of 10 January 2002 No.7-FZ.

— how, legally speaking, it can be explained that the case when the duty to eliminate the environmental damage was not met or was not implemented in full took place at all?

— how much time should pass since the economic and other activities, that have caused the environmental harm, were carried out in this case?

Obviously, the indication of ownerless facilities in the Law on the Environmental Protection generates quite practical questions. In accordance with the legislation, individuals and legal entities are obliged to compensate for the environmental harm they have caused. Pursuant to Article 77 of the Law on the Environmental Protection, claims for the compensation for the environmental harm caused by the violation of environmental legislation may be submitted within twenty years. Therefore, the compensation for the environmental harm is provided by a possibility of legal proceedings and by the defendant's obligation to compensate for the harm by the court during this period.

At the same time, as I. V. Suzdalev rightly points out, "it would be wrong to describe the past damage simply as damage caused before a specific date"[8]. Definition of the accumulated environmental harm (damage) should contain a number of clarifications that allow to differentiate this concept from the concept of "the harm to the environment", which is subject to compensation under the general rules ***as the imposition of legal liability on the offender***. Accordingly, in this case it is necessary to determine the conditions that enable to establish unequivocally when the harm to the environment is to be called "accumulated".

Thus, an indication of the period of causing harm as an event before the privatization property could bring some clarity to this issue[9]. Among other proposals to clarify the investigated concept, there was the description of the situation when the accumulated damage causer "is currently unavailable or is not easily subject to legal liability as the causer of damage which has stopped business activities at the site of damage was liquidated or simply is unknown"[10].

Ownerless real estate shall be registered by the authority that is responsible for the state registration of the right to real property, according to the statement of local authority in whose territory it is located (p.3 Art.225 of the Civil Code of the Russian Federation). In addition, after one year from the date of putting the ownerless real

[8] Suzdalev I.V. Perspektivy pravovogo regulirovaniia proshlogo ekologicheskogo uscherba v Rossiiskoi Federatsii // Pravovye voprosy stroitel'stva [Prospects of Legal Regulation of the Past Environmental Damage in the Russian Federation // Legal Issues of Construction]. 2013. No.2. P.6-8.

[9] See: Vasil'yeva M.I. O yuridicheskikh napravleniyakh natsional'noi ekologicheskoi doktriny // Ekologicheskoe pravo Rossii. Sbornik materialov nauchno–prakticheskikh konferentsii [On the Legal Directions of National Environmental Law Doctrine // Environmental Law of Russia. The Collection of Materials of Scientific-Practical Conferences]. Vol.3 / edited by A.K. Golichenkov. M., 2002. P.16.

[10] Suzdalev I.V. Op. cit.

estate on record, the authority managing municipal property may apply to the court to declare the recognition of the municipal ownership of the real estate. The question — how it is necessary to combine the rules of the Civil Code on ownerless property with the new provisions of the Law on the Environmental Protection — does not have the answer in the current legislation.

Chapter XIV.1 of the Law on the Environmental Protection, first and foremost, refers to a set of certain administrative procedures and powers in the field of environmental management. The implementation of legal provisions on the accumulated harm depends on the fulfillment of the functions of planning, accounting, control and financing of environmental protection measures. It is also associated with the implementation of a wide spectrum of organizational measures (assessment, classification, and others.). Thus, according to p.1 Art.80.1 of the Law on the Environmental Protection, detection of objects of the accumulated environmental harm is carried out by means of inventory and inspection of territories and waters, on which the past economic and other activities were carried out and (or) on which there are ownerless objects of capital construction and waste disposal facilities.

The provisions of the Law on the Environmental Protection on the identification of objects of the accumulated harm on their assessment and on subsequent organization of works for liquidation of the accumulated harm with respect to activities of public authorities of subjects of the Russian Federation and local authorities are partially impaired by the use of phrases like this: "the authorities are entitled…" (p.3 of Art.80.1, p.2 of Art.80.2). Thus, "the bodies of state power of the subjects of the Russian Federation or local authorities are entitled to carry out the identification and assessment of objects of the accumulated environmental harm" and "the bodies of state power of the subjects of the Russian Federation and local authorities are entitled to carry out the organization of works on elimination of the accumulated environmental harm". Such an approach will ultimately affect the overall effectiveness of processes to eliminate the accumulated environmental harm. Therefore, it turns out that detection or, conversely, disregard for elimination of the accumulated environmental harm, vigorous activity in the field or, on the contrary, passive expectation is equally valid for regional authorities and local authorities concerning elimination of the accumulated harm, if they rely on the wording "…are entitled".

From a practical viewpoint, the emergence of such wordings can be explained by a lack of clarity on the issue of financing relevant activities at the stage of drafting a normative legal act. The Law on the Environmental Protection has not solved the issues of financing the works related to the liquidation of the accumulated environmental harm either.

This situation is more understandable if we assume using the method of public-private partnership in this area. Such a method requires an individual approach to the solution of a particular case, which may vary significantly depending on the circumstances.

And besides, since the adoption of the analyzed amendments to the Law on the Environmental Protection, Government Decree of 13 August 2016 No.790[11] introduced additions to the state programme of the Russian Federation "On the Environmental Protection" for 2012-2020. As a result, Section I of this state programme was supplemented by a reference to the Rules of granting and distributing subsidies from the federal budget to the budgets of the Russian Federation subjects to support regional projects in the field of waste management and elimination of the accumulated environmental damage that are given in Appendix No.4 to the state programme "On the Environmental Protection". Thus, to some extent, the problem of financing the activities of the Russian Federation subjects to eliminate the accumulated environmental harm is solved through the use of the mechanism of subsidizing regional projects for elimination of the accumulated environmental harm from the federal budget.

Along with this, the Law on the Environmental Protection provides for the situation where detection and assessment of objects of the accumulated environmental harm are carried out only by the federal bodies of executive power. Such cases, according to p.3 of Art.80.1 of the Law on the Environmental Protection, must be set by the Government of the Russian Federation.

Objects of the accumulated environmental harm should be included in the state register of objects of the accumulated environmental harm. The Russian Ministry of Natural Resources under the existing draft[12] should become that federal executive body which conducts the state register.

At this stage of work with the objects, there was a comparison of their impact on environmental safety in order to substantiate the sequence of works on liquidation of the accumulated harm. But it is known that some of the objects that are the source of the accumulated environmental harm, have already been highlighted in one way or another by various legal acts. For example, according to the subprogramme "Development and Use of the Arctic" of the federal target programme "World Ocean", measures for the implementation of the large-scale integrated project "Environmental Security in the Arctic" were planned and now they are implemented (Sec.III). One of the main goals of the project is "the restoration of the environment disturbed as a result of the past activities in the Russian Arctic"[13].

[11] Government Decree of 13 August 2016 No.790.

[12] Available at: http://regulation.gov.ru/projects#npa=53382.

[13] Government Decree of 10 August 1998 No.919.

Such objects for which measures to eliminate the accumulated harm are already carried out in accordance with a variety of programmatic documents and individual acts are the priority in its own way in relation to other objects of the accumulated environmental harm as well. But ***their priority is determined*** *in another* ***manner*** *than the* ***priority*** *that* ***is introduced by the Law on the Environmental Protection***. In these circumstances, it is especially important for the liquidation activities in the Arctic to establish a transition period and transition rules from one order to another. But they are not stipulated by the Law on the Environmental Protection. As a result, it is not clear whether it is necessary to put into the inventory, assess, and incorporate in the state register all of these Arctic objects anew or not.

From a practical point of view, it would be important to continue the started works in the former order. But legally speaking, the order of liquidation of the accumulated harm as it was defined by the Law on the Environmental Protection is the priority now.

Thus, a number of specific practical issues remains unresolved in the Law on the Environmental Protection. It only partly solves a task to eliminate the accumulated environmental harm — mainly for the newly identified objects. Applied to the Arctic objects of the accumulated environmental harm, this situation can, first of all, adversely affect the timing of the completion and comprehensiveness of the required liquidation activities.

RESTRICTIONS ON FOREIGN INVESTMENT IN RUSSIAN AND CHINESE LAW

Aleksandr P. Alekseenko
LLM, Senior Lecturer of the Department of Civil Law Disciplines
Vladivostok State University of Economics and Service

Wei Chengyuan
LLM, Manager for CIS and Baltic
Angel Yeast Co., Ltd

Abstract
The major quantity of countries allows foreign investors to enjoy national treatment. But in some cases, for example, in order to protect national economic security, states use restrictive exceptions from national treatment. This article examines Chinese and Russian legislation on this issue. Based on the analysis of national laws, the classification of restrictive exceptions was made. The main criteria of restrictions division are territory; the sphere of economic activity; objects of civil rights which allowed as investments; corporate management and establishment of foreign invested legal persons. This article argues that Chinese restrictions on foreign investments are stricter than Russian ones. The authors conclude that restrictive exceptions from national treatment are necessary but only if they are justified.

Keywords: foreign investments, restrictions, joint ventures, Chinese law, exceptions from national treatment, strategic business entities.

Introduction

In order to examine foreign investments properly, it is very important to study the treatment applied to foreign investment and exceptions from it. Today the People's Republic of China is among leading countries attracting foreign investments[1]. Thus, the Chinese experience in the sphere of its legal regulation is highly interesting.

Though Russian and Chinese law proclaims that foreigners and foreign investments enjoy national treatment, any state not only has a right, but should pursue efficient and adequate economic policy and use thereto different restrictions. As Russian Professor Vladimir Belykh said, "the place and the role of a state in the economy of any country is determined by the effectiveness of the measures it takes,

[1] 月全国吸收外商直接投资情况 // URL: http://www.mofcom.gov.cn/article/tongjiziliao/v/201601/20160101238883.shtml

by the methods and instruments of legal regulation which can be used for solving social, economic and other questions"[2].

The restrictive exceptions from national treatment can be divided into a number of criteria: the territory where investments are allowed; the sphere of economic activity; the objects of civil rights which allowed as investments; the corporate management and establishment of foreign invested legal persons.

1. Territorial (geographic) restrictions

The Russian Federation includes some territories where foreign investors don not have a right to establish a legal person without special permission from the state body. These territories are called closed cities — ZATO. In accordance with par.2, 4, 5 of the Governmental Provision "On Establishment and Activities Organizations with Foreign Investments in a Closed City", a foreign investor should ask a confirmation from the public body (Ministry of Defense, *Rosatom*) to establish a company. Moreover, the application for company registration is checked by the Federal Security Service.

The restrictive exceptions are virtually applicable to the stage of company promotion in a ZATO, but when a company is established, it enjoys the treatment close to a national.

In the People's Republic of China, territorial restrictions are closely connected with economic activities. For example, foreign investors are not allowed to invest in the sphere of retail in the county towns.

2. Restrictions in the sphere of economic activities

Russian law maintains restrictions concerning the right of the foreign investor to make a contract. These restrictions depend on the sphere of economics where the investor realizes his activities.

In accordance with p.2 Art.2 of the Federal Law "On Foreign Investments in the Business Entities of Strategic Importance for National Defense and Security of the State" (FZ-57), foreign investors are prohibited to make contracts entailing their control over strategic business entities which are defined as the companies carrying out the activities mentioned in Art.6 of the Law.

In order to invest in a strategic business entity, the foreign investor should inform the Federal Antitrust Service and take permission from the Governmental Commission on foreign investments. It is obvious that above mentioned restrictions are highly important, because they prevent the state from the situation when

[2] Belykh V.S. Gosudarstvennoe regulirovanie predprinimatel'skoi deiatel'nosti v RF // Rossiiskii juridicheskii zhurnal [State Regulation of Business Activity in the Russian Federation // Russian Law Journal]. 2007. No.1. P.39.

foreigners have control over key entities and threaten the economic security of the state.

Art.7 of the FZ-57 lists transactions which are allowed but need a prior approval. For example, transactions which entail foreign investors' right of direct or indirect control more than 50% of strategic business entities' voting shares (stakes), transactions which entail the situation when the foreign investor (or a group of foreign investors) can define decisions of the company bodies and managers, etc. Moreover, Russian courts say that the contracts which contain provisions about future or indirect ownership of strategic companies' shares (stakes) are equal to above mentioned transactions[3].

Thus, the Russian legislation substantially restricts foreign investors' possibility to invest in Russian companies counted as strategic business entities. We can see that there is no freedom of contract, and that the state has a right to prohibit or abolish any transaction named in the FZ-57.

Some federal laws contain restrictions on the quantity of a business entity's shares (stakes) which a foreign investor is allowed to hold. We can find these restrictions in the following spheres: gold mining, life insurance, air transport, etc.; particularly, p.2 Art.61 of the Russian Air Code reads as follow: a company engaged in the air transportation can be established as a joint venture but a foreign investor is not allowed to hold more than 49% of the company's shares.

The Chinese legislation also has a lot of restrictive exceptions from national treatment which depends on certain economic activities. Chinese scholar Ling Wang believes that the amount of capital invested as well investments pattern should be controlled by China...[4] So this point of view is widespread among Chinese scholars and politicians as well as it is embodied in the legal acts.

In the People's Republic of China, the spheres of business activities restricted or prohibited for foreign investors are named in the Catalogue for the Guidance of Foreign Investment Industries. Activities, which are not listed in it, are considered to be permitted to foreign investment. The analysis of the Catalogue shows that the provisions of this document are designed not only to protect the national security of the PRC but also underpin national business.

Russian lawyer M. Doraev notes that in the PRC the procedure of foreign investments approval is very strict and includes the estimation of investments impact on sustainable economic growth, its influence on the political regime, and national security[5]. Therefore, there is a list of business activities where foreign investors are

[3] See: The decision of the Moscow Arbitration Court of 28 June 2010 No.A40-40521/2010.

[4] 林婉. «TRIM's协议» 与中国外商投资 法律制度的完善// Sun Yatsen University Forum. 2004. Vol. 24. No.1. P.99.

[5] Doraev M.G. Dopusk inostrannykh investorov v strategicheskie otrasli ekonomiki (pravovye osnovy) [The Admission of Foreign Investors in Strategic Sectors of Economy (Legal Basis)]. Moscow: Infotopic Media, 2012.

allowed to establish only joint ventures with a Chinese party. In some cases, the Catalogue requires the Chinese party to hold 50% or more of the shares. Apparently, these restrictions are made because of willingness of the Chinese Government to create a situation when national enterprises (as a rule, state-owned companies) have an opportunity to borrow foreign experience, techniques and methods of management.

In order to prevent evasion of rules on the establishment of foreign invested companies by buying shares of business entities which have already been created, the Government of the PRC adopted special Provisions on the Merger and Acquisition of Domestic Enterprises by Foreigners. [6] This legal act urges investors to conform to all requirements which are obligatory at the stage of the company establishment. Chinese researchers note that although Provisions mentioned above have some defects, they allow maintaining the stability of the economy, making market relations more predictable[7].

The Ministry of Commerce of the People's Republic of China pays special attention to a procedure of investing in state owned companies. In 2002, Interim Provisions on Restructuring State-owned Enterprises with Foreign Investment were adopted[8]. This legal act empowers additional requirements which are concerned M&A which are obligatory for the foreign investor who is willing to buy shares of a state-owned enterprise.

Thus, unlike the Russian legislation, the Chinese one has established a lot of restrictions and prohibitions on foreign investments. They depend on the sphere of business activities where the foreign business is willing to make investments. The core feature of these restrictions is that foreigners are obligated to establish joint ventures with a Chinese party. Moreover, in certain cases they are allowed to invest if they are minority shareholders, but the Chinese partners will be major shareholders. In Russia, such requirements for foreign investors do not exist. The Russian legislation limits only freedom of contract and this limitation is applied if a transaction is aimed at purchasing Strategic companies' shares.

3. Ownership restrictions

In Russia, some objects of civil rights are not granted to foreign investors. It means that investors may not use these objects as investments. In accordance with p.3 Art.15 of the Russian Land Code, foreigners may not owe land plots located in border

[6] 关于外国投资者并购境内企业的规定// URL: http://www.mofcom.gov.cn/article/b/f/200907/20090706416939.shtml

[7] 朱秀云. 对«关于外国投资者并购境内企业的规定»的解读 // 河南纺织高等专科学校学报. 2007. Pp. 36.

[8] 利用外资改组国有企业暂行规定// URL: http://www.safe.gov.cn/

areas. The Federal Law "On Sea Ports" prohibits foreigners to hold land plots within the boundaries of a sea port. Similar restrictions we can find in the Federal Law "On Agricultural Land Transactions".

The foreigners do not have a right of land ownership in the People's Republic of China; therefore, investors may not use a land plot for investing.

4. Organizational restrictions

First of all, it should be noted that under organizational restrictions the authors understand different limitations concerning corporate management, a company's structure and a business entity establishment. In the PRC, these restrictions apply to all foreign invested companies, regardless of the territory or the sphere of business activities. In Russia, such organizational restrictions do not exist.

As professor Lutz-Christian Wolff notes, the Government of the PRC uses a lot of different means in order to control investments[9]. First of all, Chinese legislation requires permission of foreign invested company's establishment. Art.3 of the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures reads as follows: "The joint venture agreement, contract and articles of association signed by the parties to the venture shall be submitted to the competent authorities of foreign economic relations and trade (hereafter referred to as approval authorities), and the approval authorities shall, within three months, decide whether to approve or disapprove them. In the case of approval, the joint venture shall register with the state competent authorities of administration for industry and commerce to obtain a license to do business and start operations"[10]. If the joint venture agreement, contract and articles of association are signed by the parties, but not approved, these documents will be counted as invalid [11].

Furthermore, the following restrictions are named in Art.4 of the cited Law: first, a joint venture should take the form of a limited liability company; second, the proportion of the investment contributed by the foreign joint venture(s) should generally not be less than 25% of the registered capital of a joint venture. The same requirements are formulated by other legal acts [12]. Settled time limit on making investments by the public body is one of the most difficult in the process of the enterprise establishment.

---

[9] Lutz-Christian Wolff. Mergers & Acquisitions in China: Law and Practice. Hong Kong: CCH Hong Kong, 2008. P.312.

[10] Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures // URL: http://www.fdi.gov.cn/1800000121_39_2447_0_7.html

[11] 最高人民法院关于审理外商投资企业纠纷案件若干问题的规定 // URL: http://www.court.gov.cn/fabu-xiangqing-1454.html

[12] 中华人民共和国中外合资经营企业法实施条例 // URL: http://www.law-lib.com/law/law_view.asp?id=15261

So, it seems that these measures make it impossible to freely attract investments, but create a convenient mechanism of foreign investment administration by the state. On the one hand, measures mentioned above are necessary because they protect Chinese socialistic market economy, but on the other hand, they put the brakes on the economy. This conclusion is confirmed by the World Bank statistics [13].

Another distinctive feature of Chinese law on foreign investments is that it sets foreign invested company's structure and competence of its bodies. The Company Law of the People's Republic of China specifies that the organizational structure includes the General meeting, the Board of Supervisors, the Board of Directors and the Manager. At the same time, in accordance with Art.5, 30 of the Regulations for the Implementation of the Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment[14], the General meeting and the Board of Supervisors are default. Art.33 of the Regulations sets a closed list of the Board of Directors' functions. Therefore, competence of this body may not be regulated by the articles of association. As for the Company Law of the PRC, it says that domestic companies can specify functions and powers of the Board of Directors in the articles of association. No wonder that Chinese scholar Liu Jun Hai noted that business entities with foreign investments had less freedom in determining the content of its local regulations[15]. So, this point of view should be unanimously supported.

Conclusion

The comparative analysis of foreign investment restrictions has shown the following core features of foreign investment's legal regulation in Russia and the PRC.

First of all, unlike Russian legislation, Chinese law knows organizational restrictions. Chinese law sets a special procedure of a company establishment which includes approval of articles of association by the state body. The *second* one is that law contains regulations concerning the enterprise structure which are different from the rules applied to domestic companies. It means that foreign investors do not enjoy national treatment in the PRC when we are talking about company management and establishment.

The territorial (geographic) restrictions, restrictions in the sphere of economic activities and restrictions of ownership are valid both in Russia and China. In the case of the Russian Federation, they are strongly connected with national security. But in the PRC these restrictions exist not only for protecting security, they help to

[13] See: Economy Rankings. URL: http://www.doingbusiness.org/rankings

[14] 中华人民共和国中外合作经营企业法实施细则 // URL: http://www.mofcom.gov.cn/article/swfg/swfgbl/201101/20110107351598.shtml

[15] 刘俊海.现代公司法. 下册. 北京：中国法律出版社. 2015. P.1066.

control the economy. Why does the Chinese Government do so? The answer is that China is the country which opens its national market with care.

Understanding the place of the state in the legal regulation of investments is crucial. The analysis of Chinese legislation shows that exceptions from national treatment do not push away foreign investments. Thus, the Russian legislator should not just "open the country" for foreign investments, but protect national interests. It means that restrictions on foreign investments are necessary, but only if they are justified. At the same time, in order to attract foreign investments into Russia with a glance at Chinese experience in taxation, administration of special economic zones and anti-corruption drive, the Russian Federation should take measures which will ensure investors to do business in this country.

MECHANISMS OF PROTECTION OF MINORITY SHAREHOLDERS UNDER ENGLISH LAW

Asset Bazekov
LLM, Lancaster University, Practicing Lawyer
Astana, Kazakhstan

Abstract
The article focuses on the mechanisms of protection of minority shareholders. The author tries to highlight the main remedies of protection of minority shareholders' interests and evaluate whether they adequately protect the interests of minority shareholders.

Keywords: minority, protection of interests, Companies Act, shareholders, derivative claim, petition, losses.

The general principles of the law in the UK, concerning commercial affairs, are that majority prevails in controlling the company; simply, it could be stated that when it comes to decision-making, the principle of "a majority rule" is to be applied. Of course, it is absolutely logical in the decision-making process that majority shareholders prevail. However, there is a possibility that majority shareholders could abuse their power and prejudice minority shareholders' interests. Minority shareholders could be oppressed and prejudiced in different ways both in public companies and private companies. To some extent, shareholders of public companies are in a better position than shareholders of private companies, because they can withdraw from the company just selling their shares on the stock market. Also, listed companies are subject to stock market control. In contrast, minority shareholders of unlisted companies cannot find such an easy way out. Even if minority shareholders of an unlisted company could find someone who would purchase their shares, it does not mean that they would get "a fair price" for their shares. Furthermore, it should be taken into account that there could be some restrictions in the Statute of the company for shareholders to transfer their shares[1].

For the protection of their interests, minority shareholders may resort to court. One of the ways to protect shareholders' interests is offered by Part 11 of the 2006 Companies Act[2]. It provides minority shareholders with the right to bring a derivative action on behalf of the company and for the damage recovery of the company if

[1] S.H. Goo. Minority shareholders' protection (London: Cavendish Publishing Limited, 1994), 1.
[2] Companies Act 2006, Part 11.

certain terms are met[3], as an exception to the principles that underlain in the rule of *Foss v Harbottle*[4]. The rule states that if any harmful action is committed to a company, only the company can go to court for enforcing its rights against those who committed the offense against it[5]. This rule is crucial if we consider it from the practical perspective because minority shareholders should know that there are three large grounds coming from this rule for the court to dismiss the case. First of all, the court could refuse to consider the claim, because the claim could involve it in disputes over the business policy of the company. Secondly, it could resolve that disputes among shareholders should be decided by shareholders themselves at the general shareholders' meeting where majority shareholders should have the say. And thirdly, if there is "a fear of multiplicity of claims", the court could withdraw proceedings[6].

According to the procedure, minority shareholders could bring a derivative claim against the director of the company or another person (or both) in regard to negligence, default, breach of duty or breach of trust by a director of the company[7]. If the company is controlled by wrongdoers, who could be directors or majority shareholders, basically, the company will not take an action. In such a situation, minority shareholders are left only to bring a derivative action on behalf of their company and they would refer to the "fraud on the minority" exception. Until recently, it could be considered that if minority shareholders could determine that the harm committed to the company constituting a fraud on the minority and the company is under the control of wrongdoers, they would be permitted to bring a derivative action. To date, it is enough to bring an accusation against the director's act or omission causing negligence to start a derivative proceeding. After a derivative proceeding has been initiated, a shareholder must seek permission of the court before it could be continued[8]. It appears that such kind of an action involves what has been acknowledged as "a two-stage test". At the first stage of the permission process, the application and the evidence filed by the shareholder must disclose a *prima facie* case on an "*ex parte* basis", the failure of disclosing it could result in dismissing the claim according to section 261(2)[9]. If a *prima facie* case has been satisfied, the court may order the company to provide the evidence constituting why the claim should be dismissed. At the second stage,

[3] Ibid.

[4] *Foss v Harbottle* (1843) 2 Hare 461; 67 E.R. 189.

[5] A. Keay and J. Loughrey. Derivative Proceedings in a Brave New World for Company Management and Shareholders' [2010] JBL, 3, pp.151-178, pp.151-152.

[6] D. French, S.W. Mayson and C.L. Ryan. Company Law (Oxford: Oxford University Press, 32nd ed., 2015), p.557.

[7] Companies Act 2006, s.260(3)

[8] A. Keay and J. Loughrey, n.5 above

[9] A.M. Gray. The Statutory Derivative Claim: an Outmoded Superfluousness? [2012] Company Lawyer, 33(10), 295-302, 295-296 and also see Companies Act 2006, s.261(2)

permission to proceed could be refused under section 263(2)[10]. According to section 263(2), it could be refused if a person acting under the duty to promote the success of the company would decide to refuse from continuing the claim or if the act or omission under consideration has been authorized or ratified[11]. As it can be seen from the case *Iesini v Westrip Holdings Ltd*[12], the court refused permission for continuing the derivative claim. In this case, a shareholder claimed a derivative action concerning the act or omission causing negligence, default, breach of duty or breach of trust by a director[13]. There was a two-stage procedure held. At the first stage, the applicant succeeded in disclosing a *prima facie* case. However, at the second stage, it was not enough just to establish a *prima facie* case, under the circumstances sections 263(2) (a) and 263(3)(b) of the Act had to be considered by the court in *Iesini v Westrip Holdings Ltd*[14]. It was discovered that the board of directors followed the advice of eminent professionals and specialists on the matter that was considered by the court; therefore, there was no doubt that the directors acted in accordance with section 172 of the Act[15]. And the claim was obviously so weak that no director acting in compliance with section 172 would seek to continue the proceedings[16]. So, as the result, the court refused permission to continue the derivative claim.

Also, it is necessary to mention about a ratification issue. It is an important question whether permission will be given to start a derivative proceeding or not, if an act that has, or could be, ratified is wrongful[17]. Under section 263(2)(c), the court has to refuse permission if the cause of action arises from an act or omission that has been ratified by the company[18]. In case it has not taken place, the court proceeds further and in considering whether to give permission, the court must take into account whether the act or omission is likely to be ratified by the company[19]. In this situation, the court relies on section 263(3)(c) of the 2006 Companies Act to exercise its discretion. The statutory derivative regime continues applying the common law rules that some definite wrongs are incapable of being ratified as indicated in section 239(7) of the 2006 Companies Act. A *Franbar Holdings*[20] case is a good example of that the Act does not change the common law position and keeps following the rule

[10] Companies Act 2006, s.263(2)
[11] A.M. Gray, n.9 above
[12] *Iesini v Westrip Holdings Ltd* [2009] EWHC 2526 (Ch)
[13] Companies Act 2006, s.260(3)
[14] Ibid, s.263(2)(a) and s.263(3)(b) and also see [2009] EWHC 2526 (Ch)
[15] Companies Act 2006, s.172
[16] *Iesini v Westrip Holdings Ltd*, n 12 above
[17] A. Keay and J. Loughrey, n 5 above, 161-162
[18] Companies Act 2006, s.263(2)(c)
[19] A. Keay and J. Loughrey, n 5 above, 161-162
[20] *Franbar Holdings Ltd v Patel* [2008] EWHC 1534 (Ch); [2008] B.C.C. 885

that certain wrongs are unratifiable[21]. And it could be considered that unratifiable wrongs are those acts, which could be recognized as a fraud against the company. However, in this statutory regime, the court has to refuse permission to bring a derivative action if all the directors would not seek to continue the proceedings or it must dismiss the claim where the act has been ratified even if it is a wrong relating to negligence or even some other substantial breach[22].

Furthermore, in considering whether to give permission, the court must take into account the following issues, defined by section 263(3)(a)-(f) of the Act:

"(a) whether the member is acting in good faith in seeking to continue the claim;

(b) the importance that a person acting in accordance with section 172 (duty to promote the success of the company) would attach to continuing it;

(c) where the cause of action results from an act or omission that is yet to occur, whether the act or omission could be, and in the circumstances would be likely to be —

(i) authorized by the company before it occurs, or

(ii) ratified by the company after it occurs;

(d) where the cause of action arises from an act or omission that has already occurred, whether the act or omission could be, and in the circumstances would be likely to be, ratified by the company;

(e) whether the company has decided not to pursue the claim;

(f) whether the act or omission in respect of which the claim is brought gives rise to a cause of action that the member could pursue in his own right rather than on behalf of the company"[23].

There are six issues that the court should take into account before making its discretion in accordance with section 261(4) of the 2006 Companies Act as to whether give permission to continue the claim[24]. And sometimes it can be concluded that a claimant has to meet all the factors before getting permission to proceed[25]. As it can be observed in *Kiani v Cooper*[26], where the court gave its permission to pursue the derivative claim because the claimant, being a shareholder in the company, had been acting in good faith and a director of the company acting in compliance with section 172 of the Act gave his consent to continue the claim. In fact, the defendant failed to disclose any evidence to defend himself. Although the applicant could pursue a petition under section 994 of the Act instead of bringing a derivative action, it was

[21] A. Keay and J. Loughrey, n 5 above, 161-162

[22] L. Talbot. Critical Company Law (Abingdon: Taylor & Francis Group, 2nd ed., 2015), 172

[23] Companies Act 2006, s.263(3)

[24] A.M. Gray, n 9 above

[25] L. Talbot, n 22 above, 175

[26] *Kiani v Cooper* [2010] 2 BCLC 426

obvious that alternative remedy was just one factor for dismissing a derivative action. But the court gave its permission only to pursue the action for disclosing the documents that defendant possessed[27]. As a matter of fact, the court concluded that the claimant should be indemnified for her costs; however, she should have no indemnity regarding a potential adverse costs order. That means that pursuing the action, applicants must be aware of the fact that they could be required to assume part of "the risk of the litigation"[28]. This is one of significant limitations for bringing a derivative action. It could be noticed that it does not matter how strong a claim and aggrieved a shareholder is if a shareholder does not have enough financial support to pursue a derivative claim. Furthermore, if a shareholder fails, he or she might be required to make compensation not only for litigation expenses but also for legal expenses of the defendant. So, as a result, the derivative claim as the mechanism of protecting minority shareholders could be considered as not efficient if we take into account these substantial "financial disincentives"[29].

Another limitation of the availability of derivative action is that minority shareholders are prohibited from claiming "reflective loss". That means that if a company has a loss due to managerial misconduct, a shareholder also may have a personal loss that bringing to a reduction in share values. According to *Prudential Assurance Co Ltd v Newman Industries (No.2)*[30], where the company, as well as a shareholder, suffers from wrongdoing that causes a loss for both, a shareholder cannot bring a personal action to recover the loss, because the shareholder's loss is reflective of the company's[31]. So, the proper way to recovery is to pursue the derivative action on behalf of the company expecting that recovery will be gained for shareholders by way of an increase in the value of shares[32].

The final substantial reason for limiting a derivative action is the pursuing an alternative way of protecting minority shareholders. A shareholder could continue an action in his or her own right, rather than seeking the possibility of bringing a derivative action on behalf of the company. As a good example, we could take *Franbar holdings*[33], where even a *prima facie* case was successfully disclosed, the claimant was required that he should pursue in his own right rather than on behalf of the company.

[27] L. Talbot, n 22 above, 175

[28] *Kiani v Cooper*, n 26 above cited in L. Talbot, n 22 above, 175

[29] J. Tang. Shareholder Remedies: Demise of the Derivative Claim?'[2012] UCL Journal of Law and Jurisprudence, 1(2), 178-210, 201-202

[30] *Prudential v Newman* (No.2) [1982] 1 All E.R. 354

[31] A.M. Gray, n 9 above, 297

[32] K. Raja. Majority Shareholders' Control of Minority Shareholders' Use and Abuse of Power: a Judicial Treatment [2014]. International Company and Commercial Law Review, 25(5), 162-185, 173

[33] *Franbar Holdings Ltd v Patel*, n 20 above

Definitely, this fact could be behind when the court determines whether to give or not its permission on the continuation of a derivative action process[34].

Another way of protecting minority shareholders' interests is a petition that shareholders could apply to the court on the ground that the company's affairs have been conducted in a manner that is unfairly prejudicial to the interests of members or that an act or omission of the company would be prejudicial[35].

Before sections 994-996 (former sections 459-461)[36], the old remedy, which was available to minority shareholders, was section 210 of the 1948 Companies Act that, as Bourne stated, had certain serious defects:

a) an order could only be made if a winding-up order could have been made on the just and equitable ground;

b) a single act was insufficient to found a petition;

c) the petitioner had to show that the conduct was oppressive;

d) a petition could not be based on omissions or on future conduct; or

e) probably personal representatives could not present a petition.

Under what are now ss.994-996, all of these defects are remedied. In particular, a petitioner needs now to demonstrate unfair prejudice and does not need to show oppression"[37].

In most cases, minority shareholders are unfairly prejudiced by a controlling majority of shareholders and, therefore, the sought remedy is to oblige the majority to purchase their shares at a price reflecting the proportion of the company's value[38]. Of course, it is unusual for shareholders, who have shares in listed companies, to seek an unfair prejudice remedy, because they can invoke an opportunity to sell their shares in the market. So, this remedy is good for minority shareholders in private companies, which shares are not listed on the stock market.

To succeed in applying a petition of unfairly prejudicial conduct, shareholders have to show that the conduct must be both "prejudicial" and "unfair", causing prejudice or harm to the relevant interests of the shareholders or part of the shareholders of the company[39]. As an example, we can take *Re Saul D Harrison*[40] case into consideration, where a minority shareholder applied a petition under section 459 of the 1985 Companies Act (now section 994 of the 2006 Companies Act) complaining that the company was a loss-making venture because the majority shareholders and

[34] L. Talbot, n 22 above, 177

[35] Companies Act of 2006, c.994(1)

[36] Companies Act of 2006, ss 994-996 and Companies Act of 1985, ss 459-461

[37] N. Bourne. Bourne on Company Law (Abington: Routledge, 6th ed., 2013), 243-244

[38] D. French, S.W. Mayson and C.L. Ryan, n 6 above, 577

[39] E. Ndzi. Shareholders' Dilemma Regarding Excessive Directors' Pay and Unfair Prejudicial Conduct [2016] *Company Lawyer*, 37(1), 3-7, 3

[40] *Re Saul D Harrison & Sons plc* [1995] 1 B.C.L.C. 14

directors paid themselves excessive remuneration. In turn, the majority shareholders claimed to strike out the petition as it did not disclose any substantial cause of action. In this case, the court took the defendants' side and dismissed the petition. Lord Hoffman held that although the conduct was not in accordance with the article, he dismissed the petition arguing that so trivial or technical infringements were not intended to be a ground for raising a petition under section 459 (now section 994 of the 2006 Act)[41].

Notwithstanding the evidence that the shareholder's right was breached and the court decided that the conduct was "unfair", however, Lord Hoffman stated that it was not unlawful and as a result in *Re Saul D Harrison,* the court took the resolution that the claimant failed to establish the fact that the act was conducted in "unfairly prejudicial" manner[42]. And it could be considered that an unfairly prejudicial conduct goes beyond unlawful conduct[43]. It could be observed further in his decision in *O'Neill v Phillips*[44], as Raja suggested that Lord Hoffman made an emphasis on "the adoption of a more preventive, restrictive and principled approach to the scope of unfair prejudice"[45]. The point of this case for Lord Hoffman is that the unfair prejudice petition must be based on the ground of the rational principles. These principles could be called as "the equitable considerations category" or following Lord Hoffman's judgment, it could be considered as "the legitimate expectations category"[46]. It shows that an unfair prejudice petition under section 994 of the Act[47] could succeed if there is a strict breach of legal rights or if the conduct is unfairly prejudicial that abuses legal rights of oppressed shareholders[48].

However, the unfair prejudice petition is an attractive remedy for minority shareholders, because the interpretation of section 994 is more flexible rather than the cautious and restrictive interpretation of derivative claims. Also, due to section 996, the court lodged with powers to grant "an order as it thinks fit for giving reliefs"[49], which plays a substantial role in acknowledging the unfair prejudicial petition as the remedy of choice of most minority shareholders[50].

---

41 *Ibid* cited in Robin Hollington Q.C. Shareholders' Rights (London: Sweet & Maxwell Limited, 4th ed., 2004), 133-135

42 *Ibid*

43 K. Raja, n 32 above, 182

44 *O'Neill v Phillips* [1999] 1 WLR 1092

45 K. Raja, n 32 above, 182

46 D. Kershaw. Company Law in Context (Oxford: Oxford University Press, 2nd ed., 2012), 689

47 Companies Act of 2006, s.994

48 K. Raja, n 32 above, 184

49 Companies Act of 2006, s.996

50 J. Tang, n 29 above, 206

Such cases like *Clark v Cutland*[51] and *Gamlestaden Fastigheter AB v Baltic Partners Ltd*[52] make an emphasis on "the concessionary attitude" of the court in relation to granting corporate relief in unfair prejudice petitions[53]. In *Clark v Cutland*, the claimant had brought both the derivative claim and the unfair prejudice petition that were subsequently consolidated. It was not a pure unfair prejudice petition, but an application involving elements of unfairly prejudicial conduct and wrongdoing more appropriate for bringing a derivative action. The court granted corporate relief to the company on the unfair prejudice petition. Lowry supposed that the application of section 996 in such kind of a way would approximately give a mechanism for broadening the relief granted by section 996, including the procedure to direct that profits and damages to be counted in the benefit of the company itself[54]. However, he suggested there should be "an established statutory basis" for such relief, but not just a precedential mechanism[55]. This case shows that before granting corporate relief on the unfair prejudice petition, there should be mixed grounds, including unfairly prejudicial conduct and corporate wrong. Although it is not difficult for skilled lawyers to find the existence of unfairly prejudicial conduct in "clear-cut cases" of corporate wrongs[56], it could be found in past cases that the courts have been inclined to think that the reasons for establishing unfairly prejudicial conduct could be breaches of directors' duties[57]. The flexibility of the court's attitude to evaluating the existence of unfairly prejudicial conduct could be an effect of their judicial proceedings under section 994 which has "an elastic quality which enables the courts to mould the concepts of unfair prejudice according to the circumstances of the case"[58].

As it could be seen from the case practice, section 996 grants power to the court to create the remedy that benefits petitioners as even those who are seeking corporate relief or those who are seeking relief in order to induce the majority shareholders to sell their shares to the minority shareholders, as it has been considered in *Re Brenfield Squash Racquets Club Ltd*[59]. Surely, the unfair prejudice petition, as Gray suggested, is undoubtedly an attractive option for minority shareholders, who are seeking relief for redress[60].

[51] *Clark v Cutland* [2003] EWCA Civ 810, [2004] 1 WLR 783

[52] *Gamlestaden Fastigheter AB v Baltic Partners Ltd* [2007] UKPC 26, [2007] Bus LR 1521

[53] J. Tang, n 29 above, 206

[54] *ibid* and also see John Lowry. Reconstructing Shareholder Actions: a Response to the Law Commission's Consultation Paper (1997) 18 *Company Lawyer* 247, 255.

[55] *ibid*

[56] J. Tang, n 29 above, 207

[57] *Re a Company (No. 008699 of 1985)* [1986] BCC 99024 cited in J. Tang, n 29 above, 207

[58] *Re Macro (Ipswich) Ltd* [1994] 2 BCLC 354, 404 cited in J. Tang, n 29 above, 207

[59] *Re Brenfield Squash Racquets Club Ltd* [1996] 2 BCLC 184

[60] A.M. Gray, n 9 above, 301

In line with the abovementioned mechanisms of the protection, there is another remedy that is available for minority shareholders, and it is a petition for winding-up the company. Minority shareholders can pursue the winding-up petition if it is applied on the just and equitable ground as indicated in section 122(1)(g)[61]. So, as a petitioner seeking to cease the operation of the company and, consequently, the company would be liquidated, this remedy could be counted as an option of last resort[62]. One point is that to pursue the petition on the ground of just and equitable winding-up is less in usage after the appearance of the unfair prejudice remedy. And also, the procedure of securing a winding-up order is delicate[63]. As an example, let us take *Re Quiet Moments Ltd*[64] case into consideration. In the case, the court refused to give permission for a winding-up order on the just and equitable ground, because it decided that the first respondent could not be blamed for the breakdown of trust and confidence within the company[65]. And the other point is that if there is another remedy that a petitioner could also pursue, the court could consider that a petitioner is acting unreasonably in seeking to have the company wound up instead of pursuing that other available remedy[66]. It could be observed in *Re Woven Rugs Ltd*[67] case, in which the petitioners pursued granting a decision to wind up the first respondent company, but the court decided to dismiss the application, because the petitioners' allegations amounted, in substance, to allegations of unfair prejudice. Thus, the petitioners had an alternative remedy, and there was no solid prospect of granting a winding-up petition[68]. So, the availability of relief under section 994 of the 2006 Companies Act had set some limitations for pursuing the winding-up petition.

However, just and equitable winding-up could be granted in various situations. One of these situations is exclusion from management[69]. In *Re A & BC Chewing Gum Ltd*[70], the petitioner had invested his money in the company and held one-third of the company's equity and had been promised a say in the company management, but the obligation of an entitlement to management participation was broken. So the petitioner had been granted the winding-up petition because the entitlement

[61] Insolvency Act of 1986, s.122(1)(g)
[62] A.M. Gray, n 9 above
[63] D. Milman. Shareholder Law: Recent Developments in Practice [2015] *Company Law Newsletter*, 378, 1-5, 4-5
[64] *Re Quiet Moments Ltd* [2013] EWHC 3806 (Ch) cited in D. Milman, n 63 above
[65] *ibid*
[66] Insolvency Act of 1986, s.125(2)
[67] *Re Woven Rugs Ltd* [2008] B.C.C. 903
[68] *ibid*
[69] N. Bourne, n 37 above, 241
[70] *Re A & BC Chewing Gum Ltd* [1975] 1 All ER 1017

obligation was so fundamental that, if broken, the association had to be dissolved[71]. Other situations could be such as "destruction of the stratum of the company"[72], cases where a "deadlock" occurs[73], "director's lack of probity"[74], "breakdown of trust and confidence"[75] and the categories are not closed[76].

Following the court's decision in *Ebrahimi v Westbourne Galleries*[77], winding-up could be granted on any ground that it would be just and equitable. Especially, it is applicable if a company is, in essence, a partnership[78]. So, it might be seen that the remedy of just and equitable winding-up is available for minority shareholders in a broad range of circumstances. However, it should be underlined once again that its popularity has decreased since the advent of the unfair prejudice remedy under sections 994-996 of the 2006 Companies Act and, also, to wind a company up would mean to obtain a discounted price for the company's assets, which is not an attractive prospect for any of the shareholders[79]. And it is not a fact that after the company would have been wound up that the realized earnings from the company's assets would be used to fund the claim of minority shareholders if there were any other first-priority creditors.

Briefly, it can be stated that there are three main mechanisms, which are available for minority shareholders; surely, each of them offers different methods of protection. As a matter of fact, minority shareholders have the option of pursuing either a derivative action or an unfair prejudice petition. Alternatively, as "an option of last resort", they may be able to pursue the just and equitable winding-up petition.

As Sykes mentioned, the 2006 Companies Act is revolutionary in that minority shareholders no longer have to prove any fraud in bringing a derivative claim whereas it is enough to demonstrate negligence, default, breach of duty, or breach of trust

[71] *Ibid* cited in N. Bourne, n 37 above, 241

[72] *Re German Date Coffee Co* (1882) 26 Ch. D. 169 cited in N. Bourne, n 37 above, 242. In this case, the company's main purpose had failed, so the company could not carry out its objectives for which it had been formed. The court granted the petition, because it was just and equitable that the company should be wound up.

[73] *Re Yenidje Tobacco Co Ltd* [1916] 2 Ch 426 cited N. Bourne, n 37 above, 242. If there is a deadlock and there is not any resolution of breaking up the deadlock using the remedy clauses in the articles or if the company's management fails in reaching a decision, then a winding-up petition could be granted. And also see *Re Brand and Harding Ltd* [2014] EWHC 247 (Ch), but in this case, the deadlock was not the only reason for the winding-up petition to be granted.

[74] *Re Bleriot Manufacturing Aircraft Co* (1916) 32 TLR 253 cited in N. Bourne, n 37 above, 242.

[75] *Re Zinotty Properties Ltd* [1984] 1 WLR 1249 cited N. Bourne, n 37 above, 242

[76] N. Bourne, n 37 above, 244

[77] *Ebrahimi v Westbourne Galleries* [1973] AC 360

[78] *Ibid*

[79] N. Bourne, n 37 above, 243

from the act or omission committed by a director of the company[80]. So, the derivative claim under Part 11 of the 2006 Companies Act has increased minority shareholders' ability to monitor directors. However, the strict guidelines of the two-stage procedure, perhaps, could mean lengthy litigation for minority shareholders, whereas the costs of pursuing a derivative claim and no personal recovery for the claimant, in the result, outweigh its benefits[81]. In contrast, the unfair prejudice remedy has become an attractive remedy for minority shareholders seeking personal relief. If a shareholder succeeds to establish that the conduct has been both unfair and prejudicial, the court will grant the unfair prejudice petition. Also, as the main reason calling this remedy as the remedy of the minority shareholders' choice could be flexibility of the court in decision-making, because the court may be able to make such an order as it thinks fit for giving relief in relation to the matters complained of. And as an alternative to these abovementioned remedies, the just and equitable winding-up remedy may be pursued. This alternative remedy remains as the option of last resort, so any of shareholders would pursue this remedy after all the others, because if there are any other remedies that minority shareholders could pursue, the winding-up petition would be refused by the court. So, one could arrive at the view, on the ground of the arguments, which have been made in the article, that the just and equitable winding-up remedy entails disadvantages for all shareholders.

From the effectiveness and availability perspective, the most common remedy that minority shareholders would pursue to redress infringement of their rights is the unfair prejudice remedy. Moreover, it should be taken into account that minority shareholders, pursuing this remedy, do not need any permission of the court as they need in the derivative action as well as there is room for obtaining personal recovery[82].

[80] J. Paul Sykes. The Continuing Paradox: a Critique of Minority Shareholder and Derivative Claims under the 2006 Companies Act [2010] C.J.Q. , 29(2), 205-234, 221

[81] J. Tang, n 29 above, 210

[82] J. Tang, n 29, 209

CROSS-BORDER INSOLVENCY OF INDIVIDUALS IN RUSSIAN AND CHINESE LAW

Tatyana Yu. Kareva
Ph.D. in Law, Associate Professor
Civil Law and Civil Litigation Department, School of Law, FEFU

Vadim V. Sonin
Ph.D. in Law, Research Associate
Constitutional and Administrative Law Department, School of Law, FEFU

Abstract
On the basis of the Russian and Chinese legislation, judicial practice and special literature, this article discusses the possibility of applying the provisions of the Federal Law "On Insolvency (Bankruptcy)" of 26 October 2002 to the Chinese nationals registered as individual entrepreneurs. The article also reviews the Chinese legal regulation and offers recommendations on the enforcement of court judgments on bankruptcy and collection of debts from the PRC nationals. The cross-border insolvency of the Chinese nationals encounters obstacles at three levels. Firstly, the awards of the Russian arbitration courts have not been practically executed in the PRC due to inadequate notification of the Chinese party in the case. Secondly, Chinese courts in principle are extremely reluctant in recognizing foreign judgments on bankruptcy, and such cases are exceptional. Thirdly, there is no personal bankruptcy institution in the PRC, while bankruptcy of individual private enterprises, close to it, is not applied in reality, and there are no legislative prospects for the personal bankruptcy in the nearest future.

Keywords: cross-border insolvency, personal bankruptcy, bankruptcy of individuals, China, People's Republic of China, recognition of the court judgments.

Economic cooperation between Russia and China evolves both at the top level of the state-owned corporations and private companies, and at the ground level of individual entrepreneurs conducting day-to-day commercial transactions. A lot of Chinese citizens are engaged in the entrepreneurial activity in the territory of Russia, often sustaining losses and finding themselves unable to meet the claims of creditors. After introduction of the Personal Bankruptcy Institution in Russia, the question has arisen in practice regarding a possibility of applying this bankruptcy institution to foreigners, in particular, to the nationals from the jurisdictions not familiar with the said institution, including the People's Republic of China.

1. Recognizing the Chinese Nationals as Bankrupts in the Territory of Russia

According to Article 25 of the Russian Civil Code[1] (hereinafter referred to as the RF CC), "a citizen who is incapable of meeting the claims of creditors in respect to monetary obligations and (or) fulfilling the liability with regard to obligatory payments, can be recognized insolvent (bankrupt) according to the arbitration award". It is stated in Part 3, Article 1 of the Federal Law "On Insolvency (Bankruptcy)"[2] that the relations associated with insolvency (bankruptcy) of citizens, including individual entrepreneurs, are regulated by this Law. Article 2 of the said Law provides the definition of a debtor: "it is a citizen, including individual entrepreneurs, or a legal entity, who proved to be incapable to meet the demands of creditors in respect to monetary obligations, on making the severance payment and (or) remuneration of labor for the persons who are working or have worked under a labor contract, and (or) fulfill the liability with regard to compulsory payments within the time period specified by the present Federal Law". Therefore, the cited rules tie up the bankruptcy procedure with the status of a citizen.

The definition of a citizen is contained in Article 5 of Federal Law No.62-FZ of 31 May 2002 "On Citizenship in the Russian Federation", according to which "the citizens of the Russian Federation are considered to be the persons having the citizenship of the Russian Federation on the date of the entry into effect of this Federal Law, as well as the persons, who have become citizens of the Russian Federation in accordance with the present Federal Law"[3]. At the same time, in accordance with Part 3, Article 62 of the RF Constitution[4], foreign citizens in the Russian Federation exercise rights and incur obligations equally with the citizens of the Russian Federation, except for the cases established by a federal law or by an international treaty of the Russian Federation. This principle of the national regime is confirmed by Article 4 of Federal Law No.115-FZ of 25 July 2002 "On the Legal Status of Foreign Nationals in the Russian Federation"[5] and Article 1196 of the RF CC. Part 1, Article 13 of the Federal Law "On the Legal Status of Foreign Nationals in the Russian Federation" fixes the right of foreign citizens to pursue entrepreneurial activity: "Foreign nationals exercise …the right for free use of their abilities and property for entrepreneurial and other economic activity not

[1] Grazhdanskii kodeks Rossiiskoi Federatsii (chast' pervaia) [The Civil Code of the Russian Federation (Part One)]: Federal Law No.51-FZ adopted by State Duma on 30 November 1994. In the version of 7 February 2017] // Sobranie zakonodatel'stva RF [Collection of Legislations of the Russian Federation] of 5 December 1994, No.32, Art.3301.

[2] Sobranie zakonodatel'stva RF [Collection of Legislation of the Russian Federation]. 28 October 2002, No.43, Art.4190.

[3] Collection of Legislation of the Russian Federation. 3 June 2002, No.22, Art.2031.

[4] Collection of Legislation of the Russian Federation. 4 August 2014, No.31, Art.4398.

[5] Collection of Legislation of the Russian Federation. 29 July 2002, No.30, Art.3032.

prohibited by law taking into account the limitations provided for by the federal law".

Thus, the provisions of Federal Law No.127-FZ of 26 October 2002 "On Insolvency (Bankruptcy)" should not be applied to foreign nationals only in the instance when there is a direct prohibition in the existing legislation. Federal Laws "On Insolvency (Bankruptcy)" and "On the Legal Status of the Foreign Nationals in the Russian Federation" do not specify any limitations or prohibitions for carrying out the bankruptcy procedure with respect to the foreign nationals registered in the Russian Federation as individual entrepreneurs. Moreover, Part 6, Article 1 of the Federal Law "On Insolvency (Bankruptcy)" allows cross-border insolvency, which also confirms the possibility of bankruptcy of foreign nationals -individual entrepreneurs — in accordance with the international treaties, as well as on the principles of reciprocity.

By the term "cross-border insolvency (bankruptcy)", the international private law implies the insolvency of the debtor residing within the legal order other than his assets and (or) creditors. Recognition of foreign bankruptcy involves spreading the legal consequences of initiating, conducting and (or) completing the bankruptcy proceeding arisen in the territory of one country to the territory of another country, where the assets and creditors of the debtor are located, in the form, in which these consequences would have arisen in the country, the court of which had initiated the bankruptcy case[6].

Thus, the existing Russian legislation allows recognizing foreign nationals as bankrupts. The provisions on the cross-border insolvency also apply to them. In the absence of a special international treaty on mutual recognition of the decisions on bankruptcy, the principle of reciprocity is applicable, and the realization of this principle is considerably dependent on the national legal regime of bankruptcy adopted in the respective country.

2. Bankruptcy of Individuals in the People's Republic of China

The Law on Bankruptcy of 2006 drafted on the basis of the "businessmen bankruptcy" doctrine is presently in effect in the PRC, and it provides only for corporate bankruptcy. During the drafting of this Law, the possibility of introduction of the Personal Bankruptcy Institution was discussed (at least, for the individual entrepreneurs and members of partnerships); however, the lawmakers decided that the conditions had not been ripe for that yet[7]. *First of all*, at that time consumption

[6] Sobina L.Y. Priznanie inostrannykh bankrotstv v mezhdunarodnom chastnom prave [Recognition of Foreign Bankruptcy in Private International Law]. Moscow, 2012, p.19-39.

[7] Zhu Hongxia. Lun woguo de geren pochan zhidu [On the Personal Bankruptcy System of China] (in Chinese) // Yunnan daxue xebao faxueban [Law Edition Journal of Yunnan University]. 2009, No.2, p.90.

on a credit basis was not common among the Chinese (as was the case in the USA and other developed countries); therefore, the credit burden did not threaten the solvency of citizens. *Secondly*, by the time of enactment of the Law "On Bankruptcy", there was no system for registration of the property of individuals as well as no creditability ratings necessary for the introduction of the individuals' bankruptcy. *Thirdly*, in the banking sector, there were no integrated databases of debtors and an information exchange system[8]. It was thought that under these conditions permission of the bankruptcy of individuals would lead to abuses on the part of debtors and a widespread evasion of debt payment[9].

Operation of the PRC's "Corporate Bankruptcy Law" according to Article 2 applies only to the enterprises that have the status of a legal entity[10]. According to the clarifications of the Supreme People's Court of the PRC, the bankruptcy and liquidation procedure stipulated by the Chinese "Corporate Bankruptcy Law" can also be applied by an analogy in case of inability of an individual private enterprise to fulfill the obligations, the deadline for execution of which has already come, when the property of the debtor is not sufficient to repay all his liabilities. After these procedures are completed, the creditor of an individual private enterprise is entitled to make a claim to the founder of an individual private enterprise about the compensation of the remaining debt[11]. In this case, according to Article 2 of the PRC's law "On Individual Private Enterprise" of 30 August 1999, an individual private enterprise is recognized to be an economic entity, established in accordance with this law in the territory of the PRC by the sole founder — an individual, whose property constitutes the property of the founder, and the full responsibility for the

[8] Sun Ying. Lun woguo geren pochan falv zhidu de goujian [On Establishing an Individual Bankruptcy Regime in China] (in Chinese) // Xiandai faxue [Modern Law Science]. 2016, No.3, p.91.

[9] Li Shuai. Lun woguo geren pochan zhidu de lifa jincheng — yi dui geren pochan "tiaojian bu chengshu lun" de pipan er zhankai" [On Progress in Legislation on Personal Bankruptcy System — Starting from Criticism to the "Theory of Immature Conditions"] // Shangye Yanjiu [Commercial Research]. 2016, No.3, p.24.

[10] Zhonghua renmin gongheguo qiye pochanfa [Enterprise Bankruptcy Law of the People's Republic of China]. You zhonghua renmin gongheguo di shi jie renmin daibiao dahui changwu weiyuanhui di ershisan ci huiyi yu 2006 nian 8 yue 27 ri tongguo : Zhonghua renmin gongheguo zhuxiling di 54 hao [Adopted on 8 August 2006 at the 23rd meeting of the Standing Committee of the People's Republic of China National People's Congress of 12: approved by Decree No.54 of the Chairman of the People's Republic of China]. // Available at: pkulaw.cn.

[11] Zuigao renmin fayuan guanyu geren duzi qiye qingsuan shifou keyi canzhao shiyong qiye pochanfa de pochan qingsuan chengxu de pifu [The Supreme People's Court's Reply on whether the individual-owned enterprise liquidation can refer to the application of bankruptcy law of bankruptcy liquidation procedures]. 2012 nian 12 yue 10 ri you zuigao renmin fayuan shenpan weiyuanhui di 1563 ci huiyi tongguo. fashi (2012) 16 hao [Adopted on 10 December 2012 at 1563rd meeting of the People's Supreme Court Judicial Committee. No Fashi (2012) 16] // Available at: pkulaw.cn.

liabilities of whom is borne by the founder, by his personal property[12]. Thus, the application of bankruptcy to the property sphere of a citizen is theoretically possible in case of an individual private enterprise bankruptcy; however, in practice this scheme is not used due to social tension, which can be provoked by a massive default on obligations by the citizens under the conditions of the lending boom. After exhaustion of the property of the individual private enterprise in the course of bankruptcy procedure, further collection of debts from its founder is carried out in accordance with the ordinary civil law procedures.

Thus, the bankruptcy institution is not applied currently to the individuals, although theoretically it may affect their property sphere during the bankruptcy process of an individual private enterprise. Yet, there are other factors, which determine the possibility of implementing a cross-border insolvency of the Chinese nationals on the stage of recognizing the awards made by the Russian arbitration courts.

3. Recognition of the Decisions on Bankruptcy of Individuals in the PRC

In accordance with the provisions of Article 265-267 of the PRC Code of Civil Procedure, a party or a foreign court may apply to the Chinese Intermediate People's Court for recognition and execution of the decision or ruling of the foreign court that has become effective on the basis of the international treaty entered into between the PRC and a foreign country or on the basis of the reciprocity principle. If such a decision is not in conflict with the main principle of the PRC's legislation, and is not in violation of the national sovereignty, security and public interest, then a respective people's court will recognize its legal force, and, if necessary, will issue a writ of execution. Article 5 of the Chinese "Corporate Bankruptcy Law" provides an analogous rule for recognition of "decisions and rulings on the matters of bankruptcy related to the property of the debtor in the territory of the PRC passed by foreign courts and which became effective". Such judicial acts are subject to recognition and execution in accordance with an international treaty or the reciprocity principle, if they do not contradict the fundamentals of the PRC's legislation, national sovereignty, security and public interest, and are not in violation of the lawful rights and interests of the debtor staying in the territory of the PRC.

In reality, the cases of recognition by the Chinese courts of foreign bankruptcies are rare and belong to history. Thus, in 2001 the Foshan court, on the basis of the

[12] Zhonghua renmin gongheguo geren duzi qiyefa [Law of the People's Republic of China on Individual Proprietorship Enterprises]. You zhonghua renmin gongheguo di jiu jie quanguo renmin daibiao dahui changwu weiyuanhui di 11 ci huiyi yu 1999 nian 8 yue 20 ri tongguo [Adopted at the 11th meeting of the Standing Committee of the People's Republic of China 9th National People's Congress on 20 August 1999] // Available at: pkulaw.cn.

Chinese-Italian treaty on legal assistance with regard to civil cases[13], recognized the judgment of the Milano Court (Italy) on the bankruptcy of the Italian limited liability company *E.N. Group S.P.A.* based on the application of the Italian company *B&T Ceramic Group S.R.L.*[14] The reason for application was unlawful alienation by the bankrupted company of 98% of its Chinese subsidiary in favor of the third-party Hong Kong company, whereas according to the judgment of the Italian court all the property of E.N. had already passed into the ownership of B&T[15]. That decision was the first instance of recognition by the Chinese court of the foreign judgment on bankruptcy. In this case, and later in the PRC's "Corporate Bankruptcy Law", the Principle of Limited Universalism was fixed, in accordance with which the Chinese court recognizes the judgments and rulings of a foreign court, made as part of the main proceedings on the matter of bankruptcy in the country of the debtor domicile[16]. Even recognition of the judgments made by Hong Kong courts on bankruptcy (Special Administrative Region Xianggang (Hong Kong) remains a relatively autonomous jurisdiction) faces in the PRC considerable obstacles[17].

Recognition of the Russian arbitration awards on bankruptcy (including the bankruptcy of individuals) has no precedents in the PRC so far; however, it is even hypothetically associated with many general and specific problems.

A common problem is concerned with recognition in China of all the awards made by the Russian courts of arbitration. In accordance with Article 16 of the *Treaty on Legal Assistance Regarding Civil and Criminal Cases* concluded between our countries, dated June 19, 1992 (hereinafter referred to as "the Treaty"), "The parties are liable to recognize and execute on their territory court judgments on civil cases and awards of the arbitration court made on the territory of another Contracting

[13] Zheng Weiwei. Zhongguo yingdui kuaguo pochan wenti de celve xuanze [China's Strategic Choice in Dealing with the Legal Problems of Transnational Bankruptcy] (in Chinese) // Pochanfa [Bankruptcy Law]. 2012, No.1. P.126.

[14] B&T Ceramic Group S.R.L. youxian gongsi shenqing chengren he zhixing yidali fayuan pochan panjue an [The case of B&T Ceramic Group S.R.L. Co., Ltd. applied for recognition and enforcement of the Italian court bankruptcy decision] // Available at: http://www.pkulaw.cn/Case/pfnl_118269646.html?match=Exact

[15] Shi Jingxia. Recent Developments in Chinese Cross-Border Insolvencies // International Insolvency Institute. March 2001. Available at: www.iiiglobal.org.

[16] Arsenault Steven J. Leaping over the Great Wall: Examining Cross-Border Insolvency in China under the Chinese Corporate Bankruptcy Law // Ind. Int'l & Comp. L. Rev. 2011, Vol. 2 1:1, p.20.

[17] See: Lee, Emily. Comparing Hong Kong and Chinese Insolvency Laws and their Cross-Border Complexities (March 16, 2015) // The Journal of Comparative Law, Vol.9(2) 2015, pp.259-280; University of Hong Kong Faculty of Law Research Paper No.2015/009. Available at SSRN: https://ssrn.com/abstract=2588442; Lee, Emily. Problems of Judicial Recognition and Enforcement in Cross-Border Insolvency Matters between Hong Kong and Main-land China // The American Journal of Comparative Law. 2015, vol. 63, p. 439-466.

Party"[18]. According to Article 18 of the Treaty, the recognition shall be made by a respective Chinese intermediate court based on the application of the litigant by way of considering the compliance of the award subject to recognition with the Treaty requirements. The main obstacle for recognition of the judgments made by the Russian arbitration courts is p.3 Article 20 of the Treaty, under which "the recognition of the court judgment can be denied, if the summons to court has not been served in accordance with the legislation of the Contracting Party, whose institution has made a judgment, to the Party not participating in the judicial proceeding".

In accordance with p.3 Article 253 of the Russian Arbitration Procedure Code, in the instances when the foreign persons participating in the proceeding considered by the arbitration court in the Russian Federation, are staying or residing outside the Russian Federation, such persons shall be notified about the court proceeding by the ruling of the arbitration court by way of forwarding an instruction to the justice agency or another competent body of a foreign state. Therefore, the Russian arbitration court may notify the Chinese party participating in the proceedings in the territory of Russia about the court proceedings, only by way of sending an instruction to the Ministry of Justice of China, and such form of notification is an exceptional one. Thus, the Supreme People's Court of the PRC clarified in 2005 that reference to proper notification of the party about the time and date of the court session contained in the award of the Russian arbitration court of Ulyanovsk region is non-specific and does not allow to find out whether or not this notification was in compliance with the requirements of the Treaty on the legal assistance[19]. Therefore, if the Russian arbitration court has not notified the Chinese party through the Ministries of Justice of the RF and PRC, the Chinese court will definitely deny the recognition of the arbitration award. In such cases, actual time of executing such notification may reach half a year, which in no way corresponds to the periods for consideration of cases provided for by the Arbitration Procedure Code of the RF.

As we have already found out, a special problem of recognition of the Russian decisions on the bankruptcy of individuals in the PRC lies in the absence in the PRC's legislation of the Personal Bankruptcy Institution, whereby a reservation clause

[18] Dogovor mezhdu Rossiiskoi Federatsiei i Kitaiskoi Narodnoi Respublikoi o pravovoi pomoshchi po gra-zhdanskim i ugolovnym delam [Agreement between the Russian Federation and the People's Republic of China on Legal Assistance in Civil and Criminal Cases]. Signed in Beijing on 19 June 1992. Ratified by Decision of the Russian Federation Supreme Council from February 26, 1993 No. 4560-1 // Sobraniye zakonodatel'stva RF [Collection of Legislation of the Russian Federation]. February 18, 2013, No.7, Art.612.

[19] Zuigao renmin fayuan guanyu dui fuerjia diniebo hangyun gongsi shenqing zhixing eluosi lianbang wuli-yangnuofusikezhou zhongcai fayuan caijue chuli jieguo de qingshi de fuhan [Reply of the Supreme People's Court on the Request for the Application of the Decision of the Arbitration Court of Ulyanovsk oblast of the Russian Federation concerning Volga-Dnepr Airfreight Company]. Adopted on September 25, 2005 by the Decision No.33 (2005)// Available at: pkulaw.cn

about public order provided for in p.5, Article 20 of the Treaty and Article 5 of the PRC's Corporate Bankruptcy Law can be applied to the Russian awards.

Conclusion

The cross-border insolvency of the Chinese nationals faces obstacles at three levels. *Firstly*, the awards of Russian arbitration courts have not been practically executed in the PRC due to inadequate notification of the Chinese party in the case. It is necessary to change the manner of delivering notifications specified by the international Treaty, or accelerate the Justice Ministries' work in both countries, or change the Chinese judicial practice. *Secondly*, the Chinese courts are extremely reluctant to recognize foreign judgments on bankruptcy in principle; such cases are exceptional even with regard to closely connected (Hong Kong) or economically important (USA) jurisdictions. In this respect, we can only hope for the development of the Chinese bankruptcy institution and a civil turnover on the whole, which is limited by ideological considerations and concerns about undermining social stability. *Thirdly*, there is no Personal Bankruptcy Institution in the PRC, while similar to it, bankruptcy of individual private firms is not applied in practice, and there are no prospects that personal bankruptcy will be introduced in the near future. Therefore, when conducting the bankruptcy procedure for the Chinese nationals in the Russian territory, one can only count on their property located on this side of the border.

ARBITRAL LEGISLATION
NEW ARBITRAL LEGISLATION IN RUSSIA

Sergey A. Kurochkin
Candidate of Law, Associate Professor
Department of Civil Procedure
Ural State Law University, Yekaterinburg, Russia

Abstract
Since December 2013, Russia began working over arbitration enhancement. The new Federal Law on domestic arbitration adopted in December 2015, numerous amendments to legislation on international commercial arbitration, to the Civil Procedure Code of the Russian Federation and the Commercial Procedure Code of the Russian Federation became a result of intensive work. Drafting the amendments, the lawmaker took into account leading achievements of Russian and foreign jurisprudence as well as considerable experience accumulated since 1992 when the first "Provisional Regulations on Arbitration Courts for Economic Disputes Resolution" were adopted as a statute. The fruitful work executed by leading domestic experts entailed the new high-level Russian arbitral legislation.

Keywords: arbitration, arbitral law, arbitrability, corporate disputes, arbitration agreement, arbitral tribunal, arbitral proceedings, interim measures, arbitral award, recognition and enforcement of foreign arbitral award

A growing number of private disputes are dealt in arbitration worldwide. Advantages of arbitration as an alternative dispute resolution method have been recognized by businessmen. Among such advantages are: confidentiality of the procedure, awareness of arbitrators as domain experts, a possibility to determine rules governing the arbitral proceedings, neutrality of the dispute resolution forum, inadmissibility of appeal concerning the arbitral award, wide possibilities to enforce the award abroad. Today, resolving a dispute in arbitration is a widely accepted and advanced method of civil dispute resolution based on the freedom of the contract principle.

The year of 2016 became a year of extensive modernization of arbitral law in Russia. September 1, 2016 was the date when the new Arbitral Law, that is, Federal Law No.382-FZ "On Arbitration (Arbitral Proceedings) in the Russian Federation", came into effect. Amendments to the Russian Law "On International Commercial Arbitration" also became effective on this date. Sections of the Civil Procedure Code of the Russian Federation and the Commercial Procedure Code of the Russian

Federation, governing issues of supervision of domestic arbitral awards and international arbitral awards were fully renovated. Due to the reform, some federal laws of the Russian Federation, including laws on insolvency, joint-stock companies, the status of judges, official registration of real property titles and transactions therewith and official registration of legal entities, were also amended.

In Russia, the right to submit civil disputes to arbitration is based on the provisions of the Constitution of the Russian Federation which guarantees the freedom of economic activity and fair competition, provides an individual right of easy use of personal faculties and paraphernalia for any business or legitimate economic activity. This issue has been especially mentioned by the Constitutional Court of the Russian Federation by stating that arbitration of disputes which arise or may have arisen between parties in respect of a definite legal relationship shall remain an alternative form of remedies and shall not convert arbitration into original court proceedings; neither does it cause legal consequences other than provided by law exactly for the arbitral award which is made by the tribunal on their own behalf, the mentioned award being binding for the parties on the voluntary fulfillment basis and can be enforced by state courts and court officers beyond arbitral proceedings[1].

Constitutional foundations underlie the arbitration reform launched by the Russian legislator. Obviously, the UNCITRAL Model Law became a framework for the new arbitral law in Russia. The legislator consistently developed legal constructions held in the Model Law. As a result, modern Russian arbitral legislation could be considered as progressive, competitive and effective.

The reform left separate legal regulation of domestic and international commercial arbitration intact. **Basic conditions and the legal procedure of constitution of the arbitral tribunal and composition of permanent arbitral institutions in Russia as well as domestic arbitration are governed by** Federal Law No.382-FZ "On Arbitration (Arbitral Proceedings) in the Russian Federation" adopted on 29 December 2015. The Russian Law "On International Commercial Arbitration" No.5338-1 adopted on 7 July 1993 (as amended on 29 December 2015) applies to international commercial arbitration seated in Russia.

Actually, all spheres of arbitration were amended. Arbitrability provisions were substantially modified. The Federal Law "On Arbitration (Arbitral Proceedings) in the Russian Federation" determines that only disputes between parties of civil legal relationships may be submitted to arbitration upon the parties' agreement. Disputes

[1] Constitutional Court Ruling of 26 May 2011 No.10-P upon an Application to the Supreme Commercial Court on Constitutionality of Some Provisions of the Civil Code of the Russian Federation, Federal Law "On Arbitration Courts in the Russian Federation", Federal Law "On Official Registration of Immovable Rights and Transactions", Federal Law "On Mortgage" // The Russian Federation Constitutional Court Review. 2011. No.4.

which have arisen or which may arise on the basis of official (administrative) or public relationships, as well as cases of special proceedings which do not satisfy conventional attributes of issues of law may not be submitted to arbitration.

The list of disputes to be submitted to international commercial arbitration was also amended. In order to make it, the legislator applied legal mechanisms of objective and subjective arbitrability. The new legislative provisions determine that disputes may be submitted to international commercial arbitration, should they result from contractual and other civil law relationships arising in the course of foreign trade and other forms of international economic relations, provided that the place of business of at least one of the parties, the place of fulfillment of most of obligations or the place closely connected with an object of the dispute are situated abroad.

Investment disputes with foreign investors related to foreign investment in Russia or Russian investment abroad may be referred to arbitration if it is allowed by special legal rules based on the international treaty of the Russian Federation or on the Russian Federation law. For instance, disputes between the state and investors related to execution, termination or validity of agreements on output partition may be submitted to arbitration[2].

General provisions related to arbitrability were amended in order to define disputes to be submitted to arbitration. The cases listed below may not be submitted to arbitration:

(1) insolvency cases (bankruptcy cases);

(2) cases related to the denial of official registration or evasion of official registration of legal entities and individual entrepreneurs;

(3) disputes on the protection of intellectual property rights with the participation of organizations conducting joint management of copyright and adjoining rights, and disputes referred to the jurisdiction of the Intellectual Property Rights Court;

(4) cases arising from administrative and other public relations;

(5) cases concerning the establishment of legally significant facts;

(6) cases on a compensation claim for a violation of the right to a fair trial within a reasonable period or the right to enforcement of a court decision within a reasonable period;

(7) cases on the protection of rights and legitimate interests of a group of persons (an analogue of class actions);

(8) certain corporate disputes;

(9) cases related to state or municipal property privatization;

[2] Federal Law No.225-FZ "On the Agreements on Output Partition" adopted on 30 December 1995, Art.22 // Collection of Legislation of the Russian Federation. 1996. No.1. Item 18.

(10) disputes arising from relations of procurement assets and services for state and municipal needs governed by the Russian law;

(11) environment harm compensation claims;

(12) cases of special proceedings;

(13) disputes arising from family relations, including disputes arising from relation concerning management of a ward's assets by custodians and guardians, except for partition of family assets between a married couple;

(14) labour disputes;

(15) disputes arising from hereditary relations;

(16) personal injury and death claims;

(17) disputes concerning the eviction from living quarters.

Direct legal rules on non-arbitrability is a great stride toward predictability of court practice development, a pledge for uniform understanding of an arbitral tribunal's competence.

During the reform of 2016, the lawmaker defined a list of corporate disputes which may be submitted to arbitration. Corporate disputes are cases concerning the foundation of a legal entity, its management or participation in a legal entity which is a commercial organization as well as in a non-commercial partnership, association (union) of commercial organizations, other non-commercial organizations joining commercial organizations and individual entrepreneurs, self-regulating non-commercial organizations. Corporate disputes may be referred to arbitration seated in Russia if the arbitration is administered by a permanent arbitral institution which has already affirmed and published special arbitration rules on corporate disputes. Some corporate disputes may not be submitted to arbitration. These are:

(1) disputes on convening a general meeting of a legal entity's participants;

(2) cases related to the exclusion of founders, members and participants in a legal entity;

(3) cases related to actions of a notary public on certifying transactions with limited liability companies' shares in their registered capital;

(4) disputes on challenging non-statutory legal acts, decisions and actions (omissions) of state agencies, municipal bodies or legal entities authorized to act as a state agency and officials on issues related to disputes on the acquisition and buyout of outstanding shares by public joint-stock companies, and to acquiring of more than 30 percent of a public company's shares.

Other corporate disputes which have arisen between a legal entity and its participants may be submitted to arbitration if two conditions are met. *First*, the legal entity, all participants of the legal entity and other persons acting as a claimant or a defendant must conclude an agreement to submit the specified disputes to arbitration. *Second*, the arbitration should be seated in Russia and the proceedings should be

administered by a permanent arbitral institution which has special arbitration rules on corporate disputes.

A significant evolution may be traced in the arbitration agreement regulation. Today, the arbitration agreement is uniformly considered similar to the UNCITRAL Model Law as an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not.

Provisions concerning the form of an arbitration agreement were unified. Since now, regardless of a type of arbitration, the requirement that an arbitration agreement should be in writing is made by a separate document drawn up and signed by the parties, by an exchange of letters, telegrams, telexes or other documents, including an exchange of statements of claim and defense in which the existence of an agreement is stated by one party and not denied by the other. An appropriate reference in the Rules of Organized Biddings or Clearing Rules duly registered with the Russian Central (State) Bank (a federal executive body within the financial market scope) shall also constitute a valid arbitration agreement. In Russia, an arbitration agreement is considered valid due to the form if it is concluded by an electronic communication with an indispensable condition that documents' complier can be verified. It is evident that information contained therein should be accessible so as to be useable for subsequent reference. Specified legal provisions form the basis for intensive online arbitration development.

During the reform, special requirements were established for an agreement to submit to arbitration corporate disputes which have arisen or which may arise between a legal entity and its participants. Such an arbitration agreement may be included in the charter of the company as a special clause. The arbitration agreement incorporated in the company's charter binds the third party of a dispute arising between the legal entity and its participants if this party has directly expressed the will to arbitrate the dispute due to this agreement.

The new law determines rules of interpretation of the arbitration agreement, of defining its scope, limits and legal destiny. In cases where replacement of persons in an obligation occurs, the arbitration agreement binds both original and new creditors by its obligation as well as original and new debtors.

Main approaches to the composition of the arbitral tribunal, occurring of arbitrators' powers and their termination and challenge procedures were upgraded. The composition of the arbitral tribunal may be made by the parties directly or via appointing persons (authorities) to whom the parties delegated their appropriate rights by their agreement. Failing the parties' agreement on the procedure of appointing an arbitrator in an arbitration court with three arbitrators, each party shall appoint one arbitrator, and the two arbitrators thus appointed shall appoint the

third arbitrator. If a party fails to appoint the arbitrator within one month or if the two arbitrators fail to agree on the third arbitrator within one month of their appointment, the appointment shall be made, upon the request of either party, by the state court. In arbitration with a sole arbitrator, if the parties are unable to agree upon the arbitrator, he similarly shall be appointed, upon the request of either party, by the state court.

The Law defined mandatory personal and qualification requirements to arbitrators in order to guarantee high quality dispute resolution. Modern Russian legislation has perceived innovative achievements made by the international professional community in the sphere of impartiality and independence of arbitrators.

Updated legislative requirements to arbitrators differ according to the type of arbitration. Provisions of the Russian Law "On International Commercial Arbitration" are an example of an extremely tolerant approach; there are no limits for a person to act as an arbitrator except his independence and impartiality. Parties to arbitration are free to agree on supplementary qualifying requirements for an arbitrator. For domestic arbitration, the Law defines minimal mandatory requirements related to personality and qualification. Only a capable person aged 25 and more is permitted to act as an arbitrator. Some public officials specified by law — judges, military men, employees of law enforcement organs, customs officials, notaries, etc. — are precluded from acting as an arbitrator due to their public status. Sole or presiding arbitrators must have legal education (either Russian or foreign one that is duly recognized in Russia).

During the reform, special emphasis was made on the issues of foundation and work of arbitral institutions. An original legal structure of a permanent arbitral institution appeared in Russia which was a subdivision of a non-profit entity established to administrate arbitration on a regular basis. It should be mentioned that a permanent arbitral institution is an autonomous body, independent from the parent organization.

The Federal Law "On Arbitration (Arbitral Proceedings) in the Russian Federation" rules on issues of foundation of permanent arbitral institutions in Russia, design of their work, cessation of existence of a permanent arbitral institution in certain cases related to serious infringement of rights and legal interests of civil turnover participants. The lawmaker took some significant steps towards prevention of a conflict of interest in the work of the permanent arbitral institution established in Russia, and regulated issues of liability of the non-profit organization which established the permanent arbitral institution. General requirements were established which are applied to the rules of arbitration and rules of functioning for arbitration management. Legal rules of the Federal Law "On Arbitration (Arbitral Proceedings) in the Russian Federation" related to permanent arbitral institutions have to be

applied not only to domestic arbitration, but also to international commercial arbitration seated in Russia.

Statutory rules governing the arbitration proceedings were modernized in the course of the reform. The scope of parties' autonomy to define rules governing the procedure was substantially expanded. A segment of dispositive, supplementary legal rulings increased. There appears a new category of "direct agreement" which is, in fact, an agreement whereby parties may define the rules being in general priority to the provisions of arbitration rules. Only using a direct agreement, the parties may refuse to conduct oral hearings or eliminate the court's power to resolve some issues of assistance (appointment of arbitrators and challenge procedures, arbitrator's authority termination) and to decide matters of lack of competence of the arbitral tribunal. An exclusion agreement may also be only a direct one. After the reform, an exclusion agreement is allowed both in domestic arbitration and international commercial arbitration.

Conservatory and interim measures in arbitration have also been updated, but the revised UNCITRAL Model Law provisions related to interim measures have not been implemented. Prior to the arbitration reform of 2016, legal practices of applying provisional measures were not uniform. Scientists also expressed diametrically opposed positions on this issue[3]. As a result, various ambiguous approaches to the application of provisional measures in arbitration were revealed. Today, not only arbitral tribunals but also permanent arbitral institutions can grant provisional measures. Parties may state by a manifest agreement or by reference to arbitration rules that before the formation of the arbitral tribunal, a permanent arbitral institution may be entitled to order the provisional measures they deem to be necessary. Thus, a legal platform for effective application of provisional measures ordered by an emergency arbitrator was formed.

However, parties are still free to apply to the state courts for conservatory and interim measures (*inter alia* preliminary conservatory measures). It is generally accepted that "the principle that the courts and arbitrators have concurrent jurisdiction to take provisional or protective measures is increasingly recognized in modern arbitration law"[4]. In Russia, the concept of "concurrent jurisdiction" has also been assimilated.

Legal rules related to award and settlement evolved earnestly. Unification of approaches to domestic and international arbitral awards, theirs composition and

[3] Commentarii k Federal'nomu Zakonu No.102-FZ "O treteiskikh sudakh v Rossiiskoi Federatsii" [Commentary to the Federal Law of the Russian Federation No.102-FZ "On Arbitration Courts in the Russian Federation"] by *Valeev D., Zaitsev A., Fetyukhin M.* M., 2015. P.86-100. *Skvortsov O.* Commentarii k Federal'nomu Zakonu "O treteiskikh sudakh v Rossiiskoi Federatsii" [Commentary to the Federal Law "On Arbitration Courts in the Russian Federation"]. M., 2003. P.190.

[4] Fouchard P., Gaillard E., Goldman B. On International Commercial Arbitration. Hague. 1999. P.710.

correction came out from the arbitration reform. At present, issues of renewal (remission) of arbitral proceedings are regulated uniformly.

The Federal Law "On Arbitration (Arbitral Proceedings) in the Russian Federation" governs the application of the mediation procedure to a dispute submitted to arbitration. New legislative provisions may be taken into account by multimodal arbitration agreement's drafters. Mediation is allowed at any stage of arbitration. After the decision to mediate the dispute has been made, a party informs arbitrators about it. The arbitral tribunal orders on this issue and names the exact term of mediation agreed by the parties. Arbitral proceedings should be adjourned within this period. If parties settle the dispute referred to arbitration successfully by mediation procedures, their final agreement may be confirmed as an arbitral award on agreed terms upon the request of all parties of arbitration. Now, the results of any settlement in domestic arbitration are formalized by a consent award unlike a simple ruling at previous time.

Grounds for termination of the arbitral proceedings were unified with the UNCITRAL Model Law. Arbitration is terminated by the tribunal's order when the claimant withdraws his claim unless the defendant objects thereto and the tribunal recognizes a legitimate interest on his part in obtaining a final settlement of the dispute, or when the parties agree on the termination of the proceeding or the arbitral tribunal finds that the continuation of the proceedings has for any reason become unnecessary or impossible. Continuation of the proceedings becomes worthless when the tribunal establishes that there exists a judicial act of a commercial court, of a court of general jurisdiction or an arbitral award, delivered in a dispute between the same persons, on the same subject matter and on the same grounds.

Important modifications were applied to the Russian procedural legislation. Legal rules of the Civil Procedure Code of the Russian Federation and the Commercial Procedure Code of the Russian Federation, governing issues of court assistance and supervision, were filled by new substance. State courts henceforward are allotted by authorities to render assistance to arbitral tribunals — to appoint arbitrators, to decide challenge issues, to obtain evidence, to issue an interim measure, etc. During the reform, the Russian procedural legislation was expanded by several sections which govern the procedure of court assistance in matters related to arbitral tribunals. At present, courts are competent to perform such functions as appointment of arbitrators, challenging an arbitrator, termination of the arbitrator's authorities. Parties' requests on these issues must be decided by court within one month. Moreover, in arbitration administered by a permanent arbitral institution the arbitral tribunal or the party with an approval of the arbitral tribunal may request assistance from a competent court in taking evidence.

The court's procedures of challenging the awards of arbitral tribunals, recognition and enforcement of internal and foreign arbitral awards have been modernized during the reform. However, the attitude to arbitration is maintained amicable and needs further development. Recourse to a court against the domestic arbitral award and the international arbitral award rendered in Russia may be made by an application for setting aside the award filed by parties of arbitration, by persons whose rights and duties are affected by the award, and by the public prosecutor (with certain conditions). Such innovative provisions became a result of the summarized court practice. An application for the issuance of a writ of execution for the enforcement of an arbitral award (a procedural form of recognition and enforcement of the arbitral award) may be filed only by a party of arbitration in whose favour the award was rendered. Applications for setting aside or for issuance of a writ of execution must be considered by court within one month at most, from the day of its receipt. Grounds for setting aside of the award, for refusing recognition and enforcement of internal and foreign arbitral awards remained mainly the same.

Arbitral foundations incorporated at the New York Convention of 1958 were widely adopted and developed during the reform. The Russian Federation properly recognizes arbitral awards and enforces them in accordance with the rules of procedure, under the conditions of the New York Convention. Final foreign arbitral awards are objects for recognition and enforcement in Russia. Only final awards and awards on agreed terms are considered to be the object of such recognition. As well as in many other countries, recognition and enforcement of acts of international arbitral tribunals (referred to either as "orders" or "awards") decided during or after merit-based arbitral proceedings which cannot be qualified as a final arbitral award is not allowed in Russia. Moreover, orders of the technical character issued by arbitrators and procedural awards (including interim measures, jurisdiction rulings, decisions concerning costs and fees) cannot be enforced in the Russian Federation[5] due to the procedure mentioned above.

During the reform, the legislator included several provisions in procedural codes which clarify conditions and the procedure of application of Article VI of the New York Convention concerning the adjournment of a decision on the enforcement of the award if an application for setting aside or suspending the award has been made. The Russian Procedural Codes were enriched by rulings related to a foreign arbitral award that does not need to be enforced. Foreign arbitral awards which are not required to be enforced are recognized in Russia without any proceedings, except for cases when the interested party duly raises objections to the recognition.

[5] Ruling of the Supreme Commercial Court No.6547/10 of 5 October 2010, case No.A56-63115/2009.

The list of amendments could be continued, yet another aspect needs to be especially mentioned. Arbitration courts play a significant role in the private sphere evolution process. Private individuals' relationships on the constitution of the arbitral tribunal and resolving disputes by it are based upon merely private interests of the individuals mentioned above. Arbitration is a special instrument of the social governing, private in its origin. At the same time, domestic and international commercial arbitration will remain to be a form of law enforcement and a significant part of the civil justice system. As such, arbitration must be subordinated to basic principles of social government regardless of its distinctive features and it should not be disregarded by the State. The Russian lawmaker has already created almost all legal conditions for effective dispute resolution by means of arbitration.

Regardless of the fact that the legal regulation duality is maintained, the reform of arbitration became a major step toward the integration of domestic and international commercial arbitration in Russia. Legal framework for domestic and international commercial arbitration has been constructed on a common theoretical footing and now seems to be comprehensive. Unification of arbitral legislation is aimed to form the integral insight of arbitration origins; it will assist the successful application of the legal provisions held in sources of domestic and international commercial arbitration by civil circulation participants.

A fair wind attends the development of arbitration in Russia!