

# Russian Civil Code Reform: Spring Rolls

On 7 May, another set of amendments to the Russian Civil Code was signed into law<sup>1</sup>. These amendments affect, *inter alia*, the general rules on transactions, the grounds on which a transaction may be challenged, and the rules governing powers of attorney. The amendments will become effective on 1 September of this year.

The main ideas behind the amendments are reconciling the relevant provisions of the Civil Code (which have remained largely unchanged since the mid-1990s) with court practice that has developed over time, filling in gaps in the law and removing obsolete rules. At the same time, some of the amendments are quite novel.

In this briefing we discuss the principal amendments.

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<sup>1</sup> Please refer to our previous publications spotlighting the Civil Code reform: [The Civil Code Reloaded](#) and [Amendments to the Russian Civil Code: Lower Chamber of the Russian Parliament Adopts First Set of Amendments in the Final Reading](#).

## Rules on challenging vulnerable transactions

Following the approach developed by the court practice, the amendments expressly provide that a person challenging a transaction must be either a party to the transaction or another person that has a statutory right to challenge the transaction.

Furthermore, in order to prevent counterparties from challenging transactions in bad faith on formal or technical grounds, the amendments provide that a claim to have a transaction declared invalid will not be upheld if the party making the claim acted in a way which allowed other parties to treat the transaction as valid. The amendment may be regarded as a type of estoppel restricting the exercise of rights against a party which has been led to believe that they would not be exercised.

The new rules for challenging specific types of transactions are set out below.

### Voidable transactions

For a claim to have a voidable transaction held as invalid, the claimant must prove that the transaction violates the claimant's rights and legitimate interests. This is, in effect, a reflection of the approach developed by the courts in a case where the validity of a transaction is being challenged.

### Void transactions

The amendments provide that only parties to a transaction can claim to have the consequences of invalidity applied to a void transaction and, in cases provided for by the law, by other persons. At the same time a claim to have a transaction held void

without invoking the consequences of such invalidity (such as restitution) may be made by any person who can demonstrate legitimate interest in having the transaction held void.

Under the amendments, the right of a court to nullify a void transaction at its discretion is limited to cases specifically provided for by law as well as cases where the transaction in question infringes what is broadly referred to as the public interest.

## The amendments seek to safeguard transactions from being challenged on frivolous grounds by introducing more robust and commercially oriented criteria for holding transactions invalid and / or applying consequences of invalidity to void transactions.

In addition, the amendments allow a court to refrain from applying the consequences of invalidity to a void transaction should it find that this would be contrary to public order or morality.

### Transactions violating the requirements of law

A new general rule introduced by the amendments is that transactions that violate the requirements of the law or secondary legislation are voidable, rather than null and void *ab initio* as is the case under current law.

However, if a transaction that does not comply with the law infringes the public interest or the rights and

legitimate interests of third persons, it will still be deemed null and void unless other consequences are provided for by law.

### Transactions contrary to public policy

Such transactions will continue to be considered void, but the right of the state to recover everything received by the parties under such transactions will now be limited to cases expressly provided for by law.

### Transactions detrimental to the interests of a legal entity

Under the amendments, a transaction entered into by the CEO of a company acting within the limits of his authority, or a person duly authorised to execute the transaction on behalf of the company, may be challenged by the company or its shareholders if the transaction is found to be detrimental to the company's interests; and (i) its detriment to the company was or should

have been known to a counterparty to the transaction or (ii) the counterparty and the person entering into the transaction on behalf of the company acted in concert to defraud the company.

This is a new ground for the invalidation of transactions to be provided by law. Under the existing regime the courts tend to apply the concept of abuse of rights to set aside such transactions, but until now there were no clear criteria for application of this concept.

### Transactions entered into under material misrepresentation or mistake

According to the amendments, a transaction entered into following misrepresentation or mistake is vulnerable to challenge only if such misrepresentation or mistake is material and the party which has been misled would not have concluded the transaction had it known the actual state of affairs. The amendments extend the list of cases when misrepresentation or mistake is deemed material to include, among others, cases when (i) a party made an obvious mistake in the document or (ii) a party is mistaken as to the identity of the counterparty or a person which is relevant to the transaction.

At the same time, the amendments allow the parties to preserve the transaction under the terms which the party which had been misled believed to be applicable. The terms of such saved transaction must be set out in the court decision.

### Transactions entered into by fraud

Under the amendments, intentional failure by one party to inform its counterparty of circumstances of which a party acting in good faith would be expected to inform its counterparty in the course of normal business dealings, will be treated as fraud. At the same time, in case of a fraud by a third party, the aggrieved party will be entitled to challenge the transaction only if the other party to the transaction or the beneficiary thereof knew or should have known of such fraud.

### Limitation periods

The amendments introduce a final 10-year term in addition to the existing 3-year limitation period for enforcing

one's rights through the court. In addition, under the amendments, the limitation period does not commence until the aggrieved party identifies the proper defendant against whom the action can be brought in court. Carve-outs from this rule may be established by law.

As regards limitation periods for challenging transactions, the existing limitation periods for setting aside a voidable transaction (1 year) and applying the consequences of invalidity to a void transaction (3 years) have not changed.

At the same time, the amendments establish separate rules on how the period during which a third party may claim application of the consequences of invalidity to a void transaction must be determined. The limitation period for third party claims will be 3 years and will start from the date when a third party became aware of or should have become aware that the performance of the transaction had started (under the current rule this period commences from the date when the performance of the void transaction started), but will be limited to a maximum of 10 years from the date when the performance of the transaction actually started.

### Framework rules for transactions subject to consent

The amendments introduce general rules governing the granting of consent to a transaction where the law requires that such consent is obtained from a third party, state or municipal authority or a corporate body of a legal entity, as well as the consequences of failure to obtain the consent (which were unclear in the absence of such rules).

The general rules set out in the Civil Code apply unless different rules are established by law.

The amendments distinguish between (i) a preliminary consent to and (ii) subsequent ratification of a transaction. Silence is not deemed to constitute consent to a transaction unless the law provides otherwise.

Under the general rule a transaction that is subject to consent is voidable in the absence of such consent unless the law provides otherwise. Where the law so provides, other consequences may be stipulated in the agreement with the person whose consent is required.

The right to challenge a transaction entered into in the absence of consent, and the list of persons that can challenge such transactions are limited in a way to protect a good faith counterparty and to prevent bad faith conduct of the person whose consent is required.

### Rules for taking and challenging decisions taken at meetings

The amendments introduce general rules for taking, and grounds for challenging, decisions of meetings which have legal consequences for a person who was entitled to participate in the meeting. The rules set out in the Civil Code apply unless other rules are provided for in another law or pursuant to it.

That said, such rules should not apply to shareholders' meetings in a joint stock company or participants' meetings in a limited liability company or any other meetings to the extent they are regulated by special laws.

Among others, under the general rules introduced by the amendments,

a decision taken at a meeting will be binding for all persons entitled to participate in the meeting (even if they were not present at the meeting). Also, the amendments establish grounds on the basis of which decisions of meetings may be challenged or are deemed void.

### Agency (power of attorney)

The following are the principal changes that affect Russian law powers of attorney ("PoA"):

#### Fewer formalities

Pursuant to the amendments, authority may be delegated not only under a PoA as a separate document, but can also be embedded in an agreement or a corporate resolution.

The amendments expressly allow a PoA to be granted by several persons or in favour of several persons. In the latter case each person will be entitled to act individually, unless the PoA expressly requires them to act jointly.

A PoA granted by a legal entity will no longer require the affixing of a stamp of the legal entity and PoAs issued by way of sub-delegation will no longer require certification by a notary.

#### No restrictions on the PoA term

The amendments lift the current restriction on the maximum term of a PoA (3 years) thus allowing a PoA to be issued for a longer term. At the same time, the existing rule that a PoA that does not state the term for which it is granted is valid for 1 year from the date it was issued, remains.

#### Irrevocable PoAs

The amendments envisage a new type of a PoA which cannot be revoked and/or can be revoked only in certain cases stipulated in the PoA (irrevocable PoA). However, application of this new type of PoA is limited to cases when the PoA is issued for the purposes of performance or to secure the performance of business related obligations of a principal towards an attorney (the person to whom the authority is being delegated under a PoA).

#### Procedure for revocation of a PoA

The amendments provide for one additional procedure for revocation of a PoA: a PoA can be revoked through the publication of an announcement to that effect in a periodical authorised to publish information on bankruptcy. Third parties are deemed to have been informed about revocation of the PoA upon expiration of one month after the publication of the announcement.

### Transactions entered into by an unauthorised person

Under the current rule, a transaction entered into by an agent lacking authority can be subsequently ratified by the principal on whose behalf the transaction was concluded.

Under the amendments, until such transaction has been ratified, a good faith counterparty is entitled to repudiate it. If the principal refuses to ratify the transaction, a good faith counterparty may also claim compensation by way of damages from the unauthorised representative, or alternatively demand that the unauthorised representative performs the transaction.

### Entry into force and transitional provisions

The amendments will become effective on 1 September 2013. Any laws contradicting the rules provided for in the amended Civil Code should be amended to be consistent with the new rules and would apply to the extent they do not contradict the new rules.

The new provisions on the grounds and consequences of challenging vulnerable transactions will apply to transactions entered into after 1 September 2013. The new rules on statutory limitation periods apply to claims subject to the existing limitation periods which have not elapsed as of 1 September 2013.

Although the amendments have not formally entered into force yet, the courts may start applying some of the principles set out in the amendments immediately. This was the message conveyed to the legal community by the President of the Supreme Arbitrazh Court of the Russian Federation at the meeting of the presidents of arbitrazh courts on 25 April 2013.

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This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

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