



Andrey  
Gorodissky  
& Partners

## Overview of Key Novelties in General Provisions on Obligations and Contracts

(Federal Law No. 42-FZ of March 08, 2015)

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## INTRODUCTION

In this overview we would like to bring to your attention the principal novelty provisions within the 8-th amendments tranche to the Russian Civil Code (“CC”), introduced by the Federal Law of March 8, 2015, No. 42-FZ “On Amendment of Part One of the Civil Code of the Russian Federation”.

The amendments concern the general part of the law of obligations and will go into effect on June 01, 2015.

The new provisions will apply to legal relationships arising after June 01, 2015. With respect to legal relationships arising before June 01, 2015, new provisions will apply to rights and obligations arising therefrom after June 01, 2015.

Until they have been brought into compliance with the new version of the CC, other laws and regulations will apply to the extent they are not in conflict with the new version of the CC.

*This overview is not intended to provide legal advice and/or any other form of legal assistance that may be rendered by attorney-at-law to client. The exclusive purpose of this overview is to make aware its recipient of certain recent changes in Russian laws and regulations. Any use of the information contained herein for particular purposes may require more detailed case-specific explanations. Further information can be obtained via +7 (495) 933 75 67 or [office@agp.ru](mailto:office@agp.ru).*

## I. GENERAL PROVISIONS ON OBLIGATIONS (1/2)

### Concept of obligation

The novelties are to a large extent of clarifying nature and a significant part thereof enshrines in law the approaches that had manifested themselves in legal precedents:

- In furtherance of the general principle of good faith (Art. 1 of the CC) the obligation of the parties to act in good faith when entering into, performing and after termination of an obligation, giving due consideration to rights and legitimate interests of one another and required reciprocal assistance, including provision of necessary information, has been provided for in the law.
- Rules for correlation between general provisions on obligations and specific provisions of contract and tort law have been determined.
- Legal framework has been provided for the applicability of the general provisions of the law of obligations to claims based on corporate affairs and related to application of consequences of invalidity of void transactions.
- The concept of court fine (*astreinte*), an amount (penalty) recovered in the event of failure to comply with court's order of specific performance by the debtor, and criteria for determining of its size: principles of fairness, commensurability, and inadmissibility of deriving of unjustified benefit, have been provided for in legislation.

## I. GENERAL PROVISIONS ON OBLIGATIONS (2/2)

### Alternative and facultative obligations

- The terms “alternative obligation” and “facultative obligation” have been defined in the law.
- Key difference: two equivalent methods of performance are available in the alternative obligation (either at debtor’s or creditor’s option), while in facultative obligation there is a principal and an accessory (facultative) performance which the debtor may substitute for the principal one.
- Effect of the above difference:
  - In the alternative obligation, if the party to which the right of choice is afforded has not exercised such right within the set time limit, the right of choice actually passes to the other party;
  - In the facultative obligation, if the debtor has failed to start the principal performance within the set time limit, the creditor may demand the principal performance.
- In alternative and facultative obligations it is essential to provide for time limit for the exercise of the right of choice.

## II. PERFORMANCE OF OBLIGATIONS (1/5)

- Emergence of the **intercreditor agreements** concept – agreements among creditors of one and the same debtor under homogeneous obligations for the procedure for satisfaction of claims:
  - The parties may agree, among other things, upon priority of satisfaction of claims or on disproportionality in the distribution of performance;
  - Performance obtained in violation of the agreement is to be transferred to the other creditor and the creditor who has transferred the performance acquires the claim (a relevant part thereof) of the creditor to whom such performance has been transferred;
  - The influence of an intercreditor agreement on relationships with third parties, including debtor, is ruled out.
- Detailing of rules for delivery of performance to an appropriate party: the debtor may require proof of authority of creditor’s representative, issued in a simple written form (e.g., by issuing of a power of attorney, certified by a Notary), except where the creditor delivers such written authority directly to the debtor, or where the authority is stipulated in the contract.
- Third party performance provisions have been extended:
  - Now the creditor is also obligated to accept performance delivered by a third party, if the latter so requests, where an overdue monetary obligation is performed;
  - A third party may deposit the debt amount with a Notary;
  - The creditor’s rights that have passed to a third party who had delivered partial performance cannot be used to the detriment of the “principal” creditor and have no priority with regard to security.

## II. PERFORMANCE OF OBLIGATIONS (2/5)

- Presumption of non-gratuitous nature of a money debt in commercial relations: the concept of **statutory** interest in monetary obligations between commercial organizations. By default the interest rate is determined by the refinancing rate.
- Unlawfulness of compound interest (except in business related and bank deposit agreements).
- Order of priority for discharge of homogeneous obligations in case of deficiency of offered performance (each subsequent item is applicable in the event the previous is inapplicable):
  - Obligation specified by the debtor during performance or immediately thereafter;
  - Unsecured obligations;
  - Obligations with the earlier maturity date;
  - Obligation incurred earlier;
  - Performance is applied proportionately.

## II. PERFORMANCE OF OBLIGATIONS (3/5)

### Unilateral withdrawal from an obligation / variation and termination of a contract (1/2)

- Provisions regulating unilateral withdrawal from an obligation (unilateral change of its terms) have been elaborated on: the right of such withdrawal (variation) may be afforded by contract only to the party that is not engaged in business activity, if the other party's performance is associated with engagement in such activity.
- Withdrawal (variation) for a valuable consideration is allowed with respect to obligations related to parties' business activities: right of unilateral withdrawal/variation may be conditioned upon payment of a certain amount to the other party (a so-called *break-up fee*).
- New rules applicable to contractual obligations:
  - Multilateral agreement (the performance of which is connected with business activities of all its parties) may provide for possible variation or termination thereof by a "majority vote";
  - The right of unilateral withdrawal from a contract or variation thereof must be exercised reasonably and in good faith;
  - Unilateral withdrawal is exercised by giving a notice and automatically entails termination of the contract as of the time of receipt of the notice; and
  - Additional cause for unilateral withdrawal from a contract (associated with the right to claim damages) has been introduced, such cause being the other party's failure to obtain a special authorization (formerly in such a case the contract was invalidated).



## II. PERFORMANCE OF OBLIGATIONS (4/5)

### Unilateral withdrawal from an obligation / variation and termination of a contract (2/2)

#### IMPORTANT:

- Confirmation of a contract (including by acceptance of performance) by a party which has grounds for withdrawal from a contract, renders further withdrawal on the same grounds inadmissible.
- Introduction of the concept of abandonment of rights under a contract (analogue of *waiver*): abandonment of a certain right (upon occurrence of trigger events for the exercise thereof) upon relevant application of the party engaged in business activities, with a reservation about possible exercise of the right in future in the event of repeated occurrence of similar events.
- Rules for abandonment of rights under a contract may also apply in the event of a failure to actually exercise the rights within the set time limit.

## II. PERFORMANCE OF OBLIGATIONS (5/5)

### Conditional performance – “a breakthrough in civil law”

- The concept of conditional performance of obligations has been introduced and thereby admissibility of so-called potestative and mixed terms and conditions has been recognized. The main features:
  - It is applicable to contractual obligations only.
  - Performance of obligations, exercise, change or termination of certain rights arising from an obligation can be made conditional upon:
    - performance or non-performance by one of the parties of certain actions;
    - upon occurrence of other events, including those being within sole control of one of the parties.
  - A number of other CC provisions have been supplemented by references to possibility of conditions, including those being within sole control of the parties.
- “Competition” of provisions on conditional performance and reciprocal performance of obligations is possible. The latter provisions have been supplemented by an important rule: neither party to a “reciprocal performance” obligation may seek in court performance until it has delivered its own performance.
- Provisions on the time limit for the performance of an obligation have been amended: now the limit for the performance may be determined as linked to the time of performance of the obligation by the other party or to another event.\*

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\* Rules for performance of obligations, time limits for the performance of which is not determined, have also been amended. Now rules for “on demand” obligations apply to them.

### III. SECURITY FOR OBLIGATIONS (1/5)

#### Key novelties

- New ways of securing of obligations: independent guarantee and security deposit.
- Suretyship provisions have been adjusted to make their use more “convenient”.
- New rules on correlation between the principal and accessory (securing) obligations:
  - Invalidity of the principal obligation does not by virtue of law render the accessory obligation invalid: the latter continues to secure obligations – resulting from such invalidity – to return the property received under the principal obligation;
  - Now it is possible for the parties to depart in the contract from the rule of termination of the accessory obligation in the event of termination of the principal one.
- Amendment of rules for reduction of a contractual penalty in an attempt to limit judicial discretion with respect to contractual penalty due from a party engaging in business activities:
  - Such reduction is subject to a prior debtor’s request to that effect;
  - such reduction is allowed in exceptional cases only, where it is proved that the recovery of the penalty amount agreed in the contract would result in creditor’s gaining unjust benefit (unlike the general rule about obvious disproportion).

### III. SECURITY FOR OBLIGATIONS (2/5)

#### Independent guarantee (1/2)

The concept of independent guarantee has been introduced to replace the current bank guarantee concept and to amend in certain aspects the existing regulation:

- Any commercial organization may act as a guarantor (in case the independent guarantee is issued by another party; suretyship rules will apply to such legal relationships).
- Requirements with respect to the form and content have been detailed:
  - The guarantee is to be made in writing, in a form which allows one to determine with certainty its terms and conditions and to satisfy oneself that it was duly issued by a certain person in accordance with the procedure established, inter alia, in the contract or by common practice;
  - The following is to be set forth in the guarantee :
    - Date of issue
    - Principal obligation
    - Principal
    - Amount of guarantee (procedure for its calculation)
    - Beneficiary
    - Term
    - Guarantor
    - Trigger events for payment under the guarantee
- Guarantee may contain a clause about the increase/reduction of the amount of guarantee, linked to the time limit or certain events.
- Independent guarantee rules are also applicable where obligation of the “guarantor” consists in the transfer of shares, bonds or things, determined by generic characteristics.

### III. SECURITY FOR OBLIGATIONS (3/5)

#### Independent guarantee (2/2)

- As a general rule, the guarantor may not use the guarantee to set off the claims against the beneficiary, acquired from the principal.
- The provision about transfer of rights under guarantee has been elaborated: a transfer is allowed in case this is provided for by the guarantee, and only in case of simultaneous assignment to the same person of the rights under the principal obligations.
- The following rules have been amended and elaborated. Rules about:
  - Revocation and amendment of guarantee;
  - Procedures for consideration of beneficiary's claims by the guarantor (5 days, if not specified otherwise, but not more than 30 days); and
  - Guarantor's refusal to satisfy the claims: the guarantor is afforded the right to suspend payment for up to 7 days, among other things, when it has reasonable grounds to believe that documents are not reliable or the events in which the guarantee secures the principal's interests have not occurred. Upon expiry of the term and where there are no grounds for refusal, payment must be made.
- The rule about beneficiary's responsibility has been established: in case beneficiary's claim is unreasonable, or if document submitted along with the claim are not reliable, the beneficiary must compensate the guarantor or the principal for the damages resulting therefrom.

### III. SECURITY FOR OBLIGATIONS (4/5)

#### Security deposit

- Is an amount of money deposited by a party in favor of another party.
- Can secure financial obligations (including obligations to compensate damages or pay a penalty) or obligations under non-deliverable forward contracts and similar banks' and professional securities traders' transactions, including future obligations.
- When events provided for in the contract occur, the security deposit is set off against performance of the principal obligation (if no such events occur or in case of termination of the secured obligation, the security deposit, must as a general rule, be repaid).
- Under certain circumstances it is possible to change the size of the security deposit (obligation to make an additional deposit or partially repay the security deposit).
- As a general rule, security deposit does not bear interest.
- Rules about security deposit apply to depositing of securities (including shares, bonds, etc.) or things, determined by generic characteristics, to be transferred as a security for the principal obligation.

### III. SECURITY FOR OBLIGATIONS (5/5)

#### **Suretyship provisions have been amended**

- It is allowed to be used to secure non-monetary obligations. The possibility for the emergence of a suretyship on the basis of law has been provided for.
- Requirements as to the level of detail for suretyship terms concerning the principal obligation have been specified: a reference to a contract is allowed, while for sureties-entrepreneurs the possibility for securing all existing and future obligations to creditors within the limit of a definite amount has been provided for.
- Loss (deterioration) of other security of the principal obligation for obligations depending on the creditor releases the surety from liability to the extent in which it could count on the lost security when making a surety agreement.
- Surety's right not to discharge its obligation, in case the creditor has opportunity to have its claim satisfied by setting it off against debtor's claim has been formalized in legislation.
- Liquidation of a debtor after the creditor files a claim against the surety in court, will not terminate the suretyship.
- Modification of the principal obligation, resulting in the increase of liability or other adverse consequences for the surety does not terminate the suretyship – the surety continues to be liable on the old terms.
- Surety's consent, given in advance in the suretyship contract, to modification of the principal obligation, provided that such consents stipulates limitation of surety's liability, is allowed.
- Other adjustments: provisions on co-sureties, non-competing with the creditor, etc.

## IV. LIABILITY FOR BREACH OF OBLIGATIONS (1/2)

Modifications have been made mainly in provisions concerning damages and interest.

- It has been determined that reimbursement of damages in full means bringing the creditor in such situation which would exist if the obligation would have been duly performed.
- Exact size of damages is not subject to obligatory proving: the size of damages is determined with reasonable reliability, however inability to determine in such a manner the size of damages is not a cause for denial of reimbursement. In such a case a court determines the size of damages relying on the principle of equity and commensurability between the liability and the breach.
- Rules about specific and abstract damages are now applicable to all contracts in case of termination thereof for breach of obligations (earlier such rules were applicable to delivery contracts only).
- In case of a breach of a negative obligation now it is possible to seek a restraining order to stop such violation.
- Change of the an interest rate chargeable in case of breach of monetary obligations: now, unless otherwise specified, average bank interest rate for private deposits at creditor's location, published by the Central Bank, for the relevant period, will be used.
- The court has been afforded the right to reduce the interest rate in the event of its obvious incommensurability with the consequences of the breach, but not below the rate applicable unless otherwise specified.



## IV. LIABILITY FOR BREACH OF OBLIGATIONS (2/2)

### Reimbursement of losses

A new concept has been introduced in the CC: reimbursement of losses arising upon occurrence of events stipulated in a contract (a certain analogue of *indemnity* in English law has been adopted):

- It is allowed, subject to agreement between the parties to an obligation, engaging in business activities (and also where it is provided for in a corporate agreement or a share transfer agreement, one of the parties to which is an individual).
- Pecuniary losses of a party to an obligation may be reimbursed (i.e. certain adverse effects of pecuniary nature).
- The losses are to be associated with occurrence of events stipulated in the contract (including losses resulting from impossibility to perform an obligation or claims against a party or a third party).
- Losses are not connected with counterparty's conduct and in view of a direct reference must not be associated with its breach of an obligation.
- Amount of reimbursable losses (a method of determination thereof) is to be determined by an agreement only. A court may not reduce an amount of reimbursable losses, unless a party willfully contributed to an increase of losses.

## V. CONTRACTS (1/7)

### Principal modifications (1/2)

- Making of a contract: a broader field for use of electronic documents and communications facilities (specifically, e-mail) without sacrificing the credibility of the source (credibility criteria have not been expressly specified).
- Confirmation of a contract: a party which has accepted performance under a contract or otherwise confirmed its effect may not demand reversal thereof, if this contradicts the principle of good faith.
- New concept: **representations**.
- Provisions on pre-contractual negotiations.
- Broader scope of applicability of the rules concerning **adhesion contracts**: now they are also applicable to agreements terms and conditions of which were determined by one of the parties, while the other party due to obvious inequality of bargaining power was placed in a position making it difficult to negotiate different content of certain clauses.
- Requirements concerning **preliminary agreement** have been simplified: there is no need for agreeing upon all essential terms of the contract – it is sufficient to agree upon its subject matter.

## V. CONTRACTS (2/7)

### Principal modifications (2/2)

- New contractual structures (subcategories of contracts):
  - **Framework agreement** (contract with open terms) – determines general terms of relationships between the parties, related to obligations, which may be specified in separate contracts, orders, etc.;
  - **Agreement providing for performance upon request** (subscription agreement) – provides for making payments (including periodical payments) by one party, affording it the right to require performance of obligation;
  - **Options** (option to make a contract, option agreement).
- Special rules about **invalidity** of contracts related to business activities:
  - A party that has failed to perform a contract but has accepted performance thereof by the other party will have a limited right to seek invalidation thereof (transactions conflicting with companies' objectives, misrepresentation, fraud, etc.);
  - Effects of invalidation of a voidable contract may be stipulated in an agreement between parties upon recognition of its invalidity.

## V. CONTRACTS (3/7)

### Representations (1/2)

The concept which had been widely used is now provided for by law – representations essential for making, performance or termination of a contract (analogous to *representations and warranties*). Essential characteristics of the new regulation:

- Indicative list of facts with respect to which representations are made: subject matter of the contract, powers, compliance of the contract with applicable law, possession of a license, financial standing, third party.
- Representations are provided by a party to a contractual obligation before, during or after execution of a contract.
- Implications of inaccuracy:
  - The party who made inaccurate representations will be obligated to reimburse the other party for damages or pay a penalty;
  - If representations are essential, the party who has relied upon them may withdraw from the contract;
  - The “aggrieved” party may also challenge the agreement, referring to fraud or material misrepresentation.

## V. CONTRACTS (4/7)

### Representations (2/2)

- A liability is imposed where a party who has made representations assumes (has reasonable grounds for assuming) that the other party will rely upon such representations.
- Stricter rules are provided for a party making a representation in the course of business activities and in connection with a corporate agreement, or a M&A transaction:
  - A party who made inaccurate representations will be liable regardless of whether or not it was aware of inaccuracy of such representations;
  - Presumption of awareness of a party about the other party's reliance on its representations has been established.

## V. CONTRACTS (5/7)

### Options

	Option to make a contract	Option agreement
Contents	Irrevocable offer to make one or more contracts.	The right to demand performance of a certain action (e.g., money payment, transfer or acceptance of property).
Exercise	Acceptance of an offer in accordance with the procedure, within time limits, and on terms and conditions provided for by the agreement. It may be made conditional on events, including those being within control of the parties.	Making of a call (a presumption of making of a call upon occurrence of certain trigger-events may be provided for).
Non-gratuitous nature	Is provided for.	Is provided for.
Term	One year, if not agreed otherwise.	Is to be provided for in the agreement. The agreement is terminated if the call is not made within the set term.
Conclusion	Resembles a kind of preliminary contract.	Resembles a kind of conditional performance of an obligation and bears certain similarity to the subscription agreement.

## V. CONTRACTS (6/7)

### Negotiations (1/2)

In elaboration of the principle of good faith, regulation of precontractual negotiations has been included in the CC and protection to agreements for conducting of negotiations has been granted:

- Parties are obligated to act in good faith when entering into negotiations, in course and upon completion thereof.
- Examples of inadmissible behavior, which may be considered negotiating in bad faith:
  - Deliberately entering into negotiations without intent to reach an agreement;
  - Providing incomplete or inaccurate information about material circumstances (including by not disclosing them);
  - Unexpected breaking off negotiations without good reasons.
- Prohibition on disclosure of received confidential information and undue use thereof for one's own purposes.
- Liability for breach of the established rules – reimbursement of damages, including loss of a contract with a third party (tort liability is also possible).

## V. CONTRACTS (7/7)

### Negotiations (2/2)

- Negotiating issues may be regulated under an agreement between the parties, including:
  - Procedures for holding negotiations, including specific good-faith requirements;
  - Distribution of costs;
  - Other similar rights and obligations;
  - Penalty for a breach of contract.
- Liability for unfair acts may not be limited by an agreement on holding of negotiations.





**DMITRY A. LUBOMUDROV**  
*Partner, Attorney-at-Law*  
*Head of Practice*  
*Corporate law/ Mergers & Acquisition*



**ALEXEY A. GORODISSKY**  
*Partner, Attorney-at-Law*  
*Head of Practice*  
*Project Finance/ Business Finance*



**JOSE K. TOBAR KIRILLOV**  
*Lawyer*

## Contact details

**Address:** Znamenka 13, bldg. 3, 3rd floor,  
Moscow, 119019, Russia

**Telephone:** +7 (495) 933 7567  
(switchboard)

+7 (495) 697 4831

+7 (495) 691 9813

+7 (495) 697 6394

+7 (495) 691 8498

**E-mail:** [office@agp.ru](mailto:office@agp.ru)

**Internet:** <http://www.agp.ru>

<http://www.andreygorodisskypartners.com/>