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Modern Russian Law of Contracts: A Functional Analysis

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Table of Contents

I.	Introduction: Contract as Promise	116
II.	Background: The Foundation of Russian Contract Law	119
	A. Origins	119
	B. History	120
III.	Primary Sources of Russian Contract Law: A Statutory Law, Case Law and Business Custom Trilogy	122
	A. Statutory Law (<i>Grazhdanskoe Zakonodatelstvo</i>)	122
	B. Case Law (<i>Sudebnoe Pravo</i>)	124
	C. Business Custom (<i>Obychai Delovovo Oborota</i>)	125
IV.	The Theories and Functions of Contract	127
V.	Architecture of Russian Contract Law: Structural Divisions of the Law	129
VI.	Contract Interpretation: Basic Concepts	131
VII.	Contract Formation: Mutual Assent to a Bargain	132
	A. Offer (<i>Oferta</i>)	134
	B. Acceptance (<i>Aktsept</i>)	135
	C. Conformance with the Requisite Form (<i>Forma Dogovora</i>)	138
	D. Agreement on Essential Conditions (<i>Sushchestvennye Usloviia Dogovora</i>)	139
	E. Other Requirements of Contract Formation	141
VIII.	Classification of Contracts: Criteria for Classification and Types of Contracts	145
	A. Public Contract: A Unilaterally Compulsory Contract	153
	B. Gambling Contract: An Unenforceable Contract	155
	C. Donative Contract: A Gratuitous Unilateral Contract	156
	D. Contract for Gratuitous Use of Property: A Gratuitous Bilateral Contract	157
	E. Contract of Adhesion	159
IX.	Substitution of Parties in a Contract: Assignment of Rights and Delegation of Duties	160
	A. Identification of the Issues	160
	B. Assignments of Rights (<i>Tsessiia</i>)	160
	C. Delegation of Duties (<i>Perekhod Dolga</i>)	166
X.	Defenses: Grounds For Voiding a Contract	168
	A. Identification of the Issues	168
	B. Defenses Based Upon Policy	169
	C. Defenses Affecting Assent	171
	1. Capacity and <i>Ultra Vires</i>	171
	2. Mistake	173
	3. Fraud, Coercion and Threat	174
	4. Unconscionability	176
	5. Statute of Limitations	177
	6. Remedies	177

XI.	Devices for Securing the Performance of a Contract.....	178
A.	General Principles.....	178
B.	Nominate Security Devices.....	180
1.	Liquidated Damages (<i>Neustoika</i>).....	180
2.	History and Explanation of Mortgage (<i>Zalog</i>)	186
a.	Background	186
b.	Mortgage Defined (<i>Zalog</i>)	187
c.	Four Types of Mortgages.....	189
d.	Two Schools of Thought	191
e.	Effects of Mortgage	192
3.	Withholding (<i>Uderzhanie Imushchestva Dolzhnika</i>)	199
4.	Suretyship (<i>Poruchitelstvo</i>)	202
5.	Bank Guaranty (<i>Bankovskaia Garantiia</i>).....	208
6.	Earnest Money (<i>Zadatok</i>)	213
XII.	Remedies: Liability for Breach of Contract.....	217
A.	Nature, Functions and Classification of Civil Liability.....	217
B.	Grounds For and Specific Forms of Civil Liability	224
1.	Damages (<i>Ubytki</i>)	226
2.	Liquidated Damages (<i>Neustoika</i>).....	228
3.	Payment of Interest	229
4.	Other Remedies.....	230
C.	Grounds For Release From, Reduction of and Limitation of Civil Liability	234
D.	Election: Tort or Contract Remedies	240
XIII.	Termination and Modification of Contract: Excuse and Discharge of Contractual Duties	241
A.	General Principles.....	241
B.	Termination of Contract	243
C.	Modification and Dissolution of Contract	255
XIV.	Conclusion: The Greening of Russian Contract Law	259

I. INTRODUCTION: CONTRACT AS PROMISE

This article examines Russian contract law, with an emphasis on the concepts of formation, interpretation, classification, substitution of parties, defenses, devices for securing performance,¹ modification, termination and remedies for breach. The concluding section reflects on the development (*greening*) of modern Russian contract law.

To a United States (U.S.) lawyer, Russian contract law seems innocently simple, occasionally baffling and culturally different. One reason for this is, unlike U.S. contract law, Russian contract theory does not view a contract exclusively as a bargained-for exchange of promises;² require consideration for the formation of a contract;³ regard legal detriment as consideration in an onerous contract;⁴ perceive the need to resort to promissory estoppel as a gap-filler;⁵ regard a letter of intent signed by business partners at its pre-contractual phase of their negotiations as per se legally binding;⁶ recognize frustration of purpose as an event that excuses

1. The decision to include a discussion of devices for securing the performance of a contract (e.g., secured transactions) in this analysis calls for some clarification, since a traditional discussion of contract law in U.S. law does not include this topic. See *RUSSIAN CIVIL CODE ANNOTATED* (Christopher Osakwe trans., Moscow University Press 2000). In Russian civil law tradition the topic commonly referred to in U.S. law as "secured transactions" is an institute of the law of obligations. See *id.* Thus, for example, Division 3 of the Russian Civil Code of 1994, which is devoted to the "General Provisions on Obligations," is divided into nine chapters dealing respectively with: concept of and parties to an obligation, performance of obligations, devices for securing the performance of an obligation, substitution of parties in an obligation, liability for breach of obligations, termination of obligations, concept and conditions of contract, conclusion of contract, and amendment and rescission of contract. See *id.* (All English translations of provisions of the Russian Civil Code of 1994 that are used in this study are by the author.)

2. C. CIV. art. 154 (Russ.).

3. *Id.*

4. *Id.*

5. The doctrine of "promissory estoppel" is a device for enforcing promises without reciprocal consideration, such as a promise to make a gift. See *RESTATEMENT (SECOND) OF CONTRACTS* § 90 (1979). The doctrine of promissory estoppel in U.S. contract law is intended to fill a gap in the common law of contract under certain binding conditions. Since Russian law does not require consideration as an element of a contract, there is no need to resort to promissory estoppel. For example, under Russian law a promise to make a gift is binding. See discussion of donative contract in Section VIII(c) below.

6. Under U.S. law, a pre-contractual letter of intent signed by business partners is binding under the theory of promissory estoppel if it induced detrimental reliance by one of the parties. See *RESTATEMENT (SECOND) OF CONTRACTS* § 45 (1979); see also CLAUDE D. ROHWER & GORDON D. SCHABER, *CONTRACTS IN A NUTSHELL* 123-24 (West Publishing Co. 1997). Under Russian law, a pre-contractual letter of intent is per se

performance under a contract;⁷ permit "contract not to sue" as a method for discharging a contractual obligation;⁸ regard a modified offer as an acceptance;⁹ permit withdrawal of an offer prior to the stipulated time of acceptance regardless of consideration;¹⁰ recognize option contracts;¹¹ impose strict liability for breaches of consumer contracts;¹² impose the burden of proving fault on the party that alleges fault, but, instead, makes it a rebuttable presumption;¹³ prohibit the use of punitive liquidated damages;¹⁴ permit punitive damages for breach of contract;¹⁵

not legally binding. A pre-contractual promise between business partners in the form of a letter of intent would be binding if it meets the requirements of a preliminary contract. C. Civ. art. 429 (Russ.).

7. In U.S. contract law, the doctrine of frustration of purpose excuses performance under a contract. RESTATEMENT (SECOND) OF CONTRACTS § 265 (1979); *see also* ROHWER & SCHABER, *supra* note 6, at 389–92. The grounds for the modification or termination of a contract under Russian law are limited to those listed and discussed in Section XIII. That list does not include frustration of purpose, which, in U.S. law, is distinct from the doctrine of frustration of contract. *See* discussion of frustration of contract in the text accompanying notes 1443, 1444 below.

8. The problems posed by a release or a contract not to sue in U.S. law are discussed in U.C.C. § 1-107 (2001), RESTATEMENT (SECOND) OF CONTRACTS § 295(2) (1979), and ROHWER & SCHABER, *supra* note 6, at 395–96. The bottom line is that under U.S. law an agreement not to sue is a permissible method of discharging a contract. A contract by which a person relinquishes fully or partially his right to sue is expressly prohibited under Article 22 and deemed unconstitutional under Article 17 of the 1993 Russian Constitution. *See generally* A.N. GUEV, POSTATEINI KOMENTARII K CHASTI PEROVOI GRAZHDANSKOGO KODESKA ROSSIKOI FEDERAZII [ARTICLE-BY-ARTICLE COMMENTARY ON THE FIRST PART OF THE CIVIL CODE OF THE RUSSIAN FEDERATION] (Infra M 2d ed. 1999) [hereinafter GUEV COMM. ONE].

9. C. Civ. art. 443 (Russ.).

10. C. Civ. art. 436 (Russ.).

11. *Id.* An option contract is a paid-for offer that typically stipulates a time period during which it must remain open for acceptance by the offeree. RESTATEMENT (SECOND) OF CONTRACTS § 45 (1979). The offer cannot be revoked prior to its expiration date, is not terminated by the death or insanity of the offeror or offeree, in most jurisdictions, a specific and unequivocal rejection of the offer by the offeree does not terminate the offer, and is transferable from the offeree to a third party. *See generally* ROHWER & SCHABER, *supra* note 6, at 30, 32–34. Under Russian law, an offer is irrevocable during the stipulated time period. C. Civ. art. 436 (Russ.). An option contract is irrevocable because sufficient consideration for the offer was received by the offeror. An irrevocable offer is irrevocable by virtue of the naked promise of the offeror not to withdraw during a specific time stipulated in the offer.

12. *See* C. Civ. art. 401 (Russ.). The general principle of fault-based liability for breach of contract is stipulated in Article 401, paragraph 1 of the Code; as an exception to this rule, Article 401, paragraph 3 imposes strict liability for breach of commercial contracts. Thus, for breach of consumer (non-commercial) contracts, liability attaches only when there is fault by the breaching party.

13. *Id.*

14. *See* C. Civ. art. 15 (Russ.).

permit damages for emotional distress for any breach of commercial contracts;¹⁶ and subdivide contractual duties into freely delegable and non-delegable duties yet requires, in all situations where delegation of duty is not prohibited by law, the prior case-by-case consent of the creditor before any duty can be delegated to a third party.¹⁷ The conceptual differences between Russian and U.S. theories of contract are staggering and deeply rooted in their respective philosophies of enforceability of promises. Another explanation for these differences is the fact that American contract law, unlike its Russian analogue, was not to any appreciable degree influenced by Roman private law. The functional analysis of the new Russian contract law in this article provides the U.S. reader with a necessary procedural compass to navigate the minefields of this most important aspect of Russian law of obligations.

A contract as a legal fact contains two elements in Russian law: an agreement (*soglashenie*, *conventio*, consensus), and a specific purpose, known in Roman law as *causa*.¹⁸ A requirement for an enforceable contract is a lawful purpose (*cause licite*).¹⁹ Under Russian civil law, a contract is but one of five sources of obligation: contract, tort, unjust enrichment (restitution), spontaneous (unauthorized) agency, and unilateral obligation in the form of a public promise of a reward and public competition (bid).²⁰ A contract is the most dominant source of obligation.²¹ In

15. See *id.*

16. See *id.*

17. C. CIV. art. 391 (Russ.).

18. See C. CIV. art. 169 (Russ.) (stating that an unlawful contract is void.) Article 420 operates against the backdrop of Article 169. In all European civil law systems it is traditional to view a contract as a component of the law of obligation. Other components of the law of obligation are tort, unjust enrichment, unauthorized agency and unilateral obligation. In other words, before zeroing in on contract, one must paint an introductory picture of obligations in general and show where the contract fits in. This civil law approach is best exemplified by the structure of the Louisiana Civil Code; e.g., Title 3 (articles 1756–1905) deals with obligations in general; Title 4 (articles 1906–2291) deals with conventional or contractual obligation; and Title 5 (articles 2292–2324) deals with non-contractual obligation.

19. C. CIV. art. 1108 (Fr.) (1804).

20. C. CIV. arts. 307, 980–88, 1055–56, 1057–61 (Russ.). Modern Russian civil law doctrine on the sources of obligation closely follows Roman law. According to Roman law, the primary sources of obligation were contract (*contractus*), tort (*delictum*), unauthorized agency which was a specific form of *quasicontractus* (*negotiorum gestio*), *quasitort* (*quasidelictum*), and unilateral obligation (*votum*, *policitatio*). See ROMAN LAW 219–95 (V.A. Tomsinov ed., 1999). The concept of promissory estoppel as a source of obligation was unknown in either Roman law or modern Russian law. CHRISTOPHER

certain situations, a contractual obligation operates alongside a non-contractual obligation by defending or securing the performance of the latter.²² This article deals with contract law (*dogovornoe pravo*) as part of the law of obligations.

II. BACKGROUND: THE FOUNDATION OF RUSSIAN CONTRACT LAW

A. Origins

The origin of modern Russian contract theory is variegated. It falls under the Germanic subgroup within the Romano-Germanic civil law family, yet embodies certain idiosyncratic features that distinguish it from pure Germanic contract law. Russian contract law, from formation to discharge, is rooted in Roman private law and infused with continental European civil law by way of pre-revolutionary Russian law. The vocabulary, fictions, methodology and concepts along with the structural organization of Russian contract law are inherited from German and French contract law. The German influence, however, is more pronounced than the French.²³

OSAKWE, SRAVNITELNOE PRAVOVEDENIE V SKHEMAKH: OBSHAIA I OSOBENNAIA CHASTI [COMPARATIVE JURISPRUDENCE IN DIAGRAMS] 158 (U.V. Luizo ed., Delo 2000). In fact, promissory estoppel is a uniquely U.S. concept. ROHWER & SCHABER, *supra* note 6, at 120.

21. This fact is evidenced by the number of chapters devoted to the respective sources of obligation in the Civil Code itself: Tort (chapter 59); Unjust Enrichment (chapter 60); Spontaneous Agency (chapter 50); Unilateral Obligation (chapters 56–57); Contract (chapters 27–29, 30–49, 51–55, 58).

22. For example, contract law backs up the legal relationship created by a public bid. C. CIV. art. 1057 (Russ.). A public bid under Russian law is not a contract but a unilateral transaction. At the completion of the public bid, however, the winner of the bid signs a contract to set the terms of performance of the bid. *Id.*

23. See KONRAD ZWEIGERT & HEIN KOTZ, INTRODUCTION TO COMPARATIVE LAW 308–13 (Tony Weir, trans., Oxford Univ. Press 1987). See also MARY ANN GLENDON, MICHAEL WALLACE GORDON & CHRISTOPHER OSAKWE, COMPARATIVE LEGAL TRADITIONS: TEXT, MATERIALS AND CASES 54–58 (West Publ'g Co. 1985); M.I. BRAGINSKII & V.V. VITRIANSKII, DOGOVORNOE PRAVO, KNIGA PERVAIA, OBSHIE POLOZHENIA [CONTRACT LAW, BOOK ONE, GENERAL PROVISIONS] 6 (Statut 2d ed. 1999) [hereinafter BRAGINSKII CONTRACT 1999]; 1 E.A. SUKHANOV, UCHEBNIK, GRAZHDANSKOIE PRAVO [TEXTBOOK ON CIVIL LAW] (E.A. Sukhanov ed., BEK 2d ed. 1998) [hereinafter SUKHANOV 1]. For general principles of German contract law see A.T. VON MEHREN & J.R. GORDLEY, AN INTRODUCTION TO THE COMPARATIVE STUDY OF LAW: THE CIVIL LAW SYSTEM (Little, Brown and Co., 2d ed. 1977).

Modern Russian contract theory takes a modified civil law approach, patterning itself after Roman law.²⁴ Russian law does not, however, adopt the Anglo-American common law approach. In fact, Russian contract theory is the antithesis of U.S. contract law.²⁵ The difference is in the influence of the government on the bargaining process.²⁶ The principles of U.S. contract law are market-driven and the government has minimal influence on the autonomy of the parties, whereas the principles of Russian contract law are driven by the government's intrusive policies on how social order and the public good should affect the marketplace.²⁷ Public interest is superimposed on private agreements through certain rules, e.g., public contracts and unconscionable contracts. In other words, the government polices the marketplace by limiting freedom of contract in some instances; the government decides what is "public good" and what is not. While U.S. contract law is suited to the needs of a free enterprise society, Russian contract law is not.²⁸ The Russian government perceives contract law as an instrument of social engineering designed to regulate the new Russian marketplace.²⁹

B. History

The reception of Roman law into Russian contract theory is epitomized in the provisions of Book 5 of the 1913 Draft Civil Code of the Russian Empire.³⁰ Although World War I and the Russian Revolution aborted the adoption of this Draft, many of its principles became codified in the Russian Civil Code of 1922, the first socialist civil code of post-tsarist Russia.³¹ Many of these Roman law concepts were carried over into the second Russian

24. A.L. Makovsky & S.A. Khokhlov, *Introductory Commentary to the CIVIL CODE OF THE RUSSIAN FEDERATION* 61-62 (Peter B. Maggs & A.N. Zhiltsov eds. & trans., International Centre for Financial and Economic Development 1997).

25. Under the Soviet legal system, government control of the marketplace was carried out through the long arms of the omnipotent and omnipresent Communist party. See Christopher Osakwe, *The Modern Soviet Legal System in Comparative Perspective*, in 8 MODERN LEGAL SYSTEMS CYCLOPEDIA 336-39 (K.R. Redden ed., 1986). In modern Russian contract, government influence on the bargaining process is manifested in the institutions of public contract (Article 426) and model contract (Article 427).

26. *See id.*

27. *See id.* at 394.

28. *See id.*

29. *See id.*

30. BRAGINSKII CONTRACT 1999, *supra* note 23, at 6.

31. *Id.*

Socialist Civil Code of 1964.³² In effect, the natural development of European contract law in Russia went through an incubation period from 1917 through 1991, when it was virtually submerged in and totally bastardized by Soviet socialist law.³³ During this period, however, the study of classical contract law flourished in the universities, especially at the law faculties of Moscow State University and Leningrad State University (now St. Petersburg State University).³⁴ The renaissance of modern Russian contract law started in the late 1980s and culminated in the adoption of the 1991 edition of the Fundamental Principles of Civil Legislation of the U.S.S.R. and the Union Republics (F.P.Civ.L.),³⁵ the harbinger of the post-Soviet Russian Civil Code of 1994 [hereinafter the Code].

Today, there are three types of civil law research centers that study Russian contract law: the law faculties of the state universities of Moscow, St. Petersburg and Ekaterinburg; the Center for Private Law Research attached to the Office of the President of the Russian Federation; and the Institute of Legislation and Comparative Law attached to the Government of the Russian Federation.³⁶ These research centers represent three competing schools of thought in post-Soviet Russian civil law scholarship,³⁷ hereafter referred to as modern Russian civil law doctrine. Although the Code adopts a classical Roman law definition of contract,³⁸ the debate over the nature of contract continues. The best explanation of this debate is in a treatise

32. See generally CIV. CODE OF RSFSR (1964).

33. For a concise restatement of the core principles of Soviet socialist contract law see 1 ENCYCLOPEDIA OF SOVIET LAW 160-68 (F.J.M. Feldbrugge ed., Oceana Publications, Inc. 1973).

34. Two of the most prominent Soviet civil law scholars of this era were Professors L.A. Lunts of Moscow State University and O.S. Ioffe of Leningrad State University. (The city of Leningrad was renamed St. Petersburg in 1993; with that change the name of the city's university was also changed.) Two of their works were recently republished by the Civil Law Department of Moscow State University in a series of publications entitled "Classics of Russian Civil Law Studies." See L.A. LUNTS, MONEY AND MONETARY OBLIGATIONS IN CIVIL LAW (Moscow 1999); O.S. IOFFE, CIVIL LAW: SELECTED WORKS (Moscow 2000).

35. Osnovy Grazhdanskogo Zakonodatelstva Soiuza SSR i Soiuznykh Respublik (Fundamental Principles of Civil Legislation of the USSR and the Union Republics).

36. Makovsky & Khokhlov, *supra* note 24, at 56-57. Nearly all of the fifty drafters of the 1994 Russian Civil Code are affiliated with these Russian centers for civil law research. See *id.*

37. *Id.* at 57.

38. See BRAGINSKII CONTRACT 1999, *supra* note 23, at 6.

written by two prominent Russian civil law scholars, M. I. Braginskii and V. V. Vitrianskii³⁹ A contract is defined as an "agreement of two or several persons on establishing, changing, or terminating civil law rights and duties."⁴⁰

III. PRIMARY SOURCES OF RUSSIAN CONTRACT LAW: A STATUTORY LAW, CASE LAW AND BUSINESS CUSTOM TRILOGY

Modern Russian contract law embodies three primary sources: statutory law, case law and business custom. Thus, the search for the rules of modern Russian contract law probes beyond statutory law and into areas of judicial lawmaking⁴¹ and marketplace practices.⁴²

A. Statutory Law (*Grazhdanskoe Zakonodatelstvo*)

The first major source of Russian contract law is the Code. It is the most comprehensive embodiment of the governing rules of modern Russian contract law.⁴³ It is divided into two parts: Part One contains the general law of contracts (*lex generalis*); and Part Two deals with the special law of twenty-nine individual nominate contracts⁴⁴ (*lex specialis*).⁴⁵ This article focuses primarily on the general rules in Part One of the Code.

The rules of the modern Russian contract law are also fleshed out in ancillary statutes. Unless otherwise provided, these are subordinate to the Code regardless of when ancillary statutes are

39. *Id.* at 1.

40. C. CIV. art. 420 (Russ.). This definition, from the French Civil Code of 1804, will ring a bell with anyone familiar with the Louisiana Civil Code. C. CIV. art. 1101 (Fr.) (1804). The Louisiana Civil Code defines a contract as "an agreement by two or more parties whereby obligations are created, modified, or extinguished." LA. CIV. CODE ANN. art. 1906 (West 1987). Even though California can hardly be described as a civil law jurisdiction, it too defines a contract as an "agreement," rather than as a "promise" that looks to a future performance, reflecting the influence of Spanish law on California law. CAL. CIV. CODE § 1549 (West 2000). Paradoxically, the U.C.C. also defines a contract in the same manner as the California Civil Code. UCC §§ 1-203(3), (11), 2-106(1) (2000).

41. C. CIV. art. 6 (Russ.). See also Makovsky & Khokhlov, *supra* note 24, at 74-75.

42. C. CIV. arts. 5, 427 (Russ.).

43. See generally C. CIV. chs. 1-3, 9-12, 21-60 (Russ.).

44. Nominated contracts are defined by the Louisiana Civil Code as "those that are given a special designation such as sale, lease, loan, or insurance." LA. CIV. CODE ANN. art. 1914 (West 1987).

45. See generally C. CIV. arts. 1-1109 (Russ.). If a general rule and a special rule conflict, the principle of *lex specialis derogat generali* prevails: the special rule shall prevail over/derogate from (*derogat*) the general rule.

adopted.⁴⁶ Thus, the relationship between a Code provision and an ancillary statute is not governed by the principle stating that in the event of a conflict between a special rule and a general rule, the special rule shall prevail over the general rule (*lex posterior derogat priori*).⁴⁷ Ancillary statutes include various statutes on specific nominate contracts⁴⁸ and the protection of the rights of a specific class of contracting parties such as consumers.⁴⁹ Aspects of contract law may also be regulated by decrees of the President of the Russian Federation⁵⁰ or by other executive orders.⁵¹

The enactment of legislation dealing with civil law matters falls exclusively within the jurisdiction of the federal government.⁵² This means that there is only one Code.⁵³ Thus, Russian states cannot enact ancillary statutes on civil law matters, including contract matters.⁵⁴ Two supreme courts opined, however, that a civil law rule contained in a state statute enacted prior to the Code should be a source of law for the courts if such rule does not conflict with the Constitution of the Russian Federation or the Code.⁵⁵

Where statutory law is silent and the contract is not regulated by agreement or business custom, courts may fill in gaps in the law using two devices, "statute by analogy" and "law by analogy."⁵⁶

46. C. CIV. art. 3 (Russ.).

47. *Id.*

48. A nominate contract is one that is given a special designation. It is a term commonly used in civil contract law. See LA. CIV. CODE ANN. art. 1914 (West 1987).

49. Specifically, the 1994 Russian Civil Code mandates the promulgation of twenty-nine ancillary statutes that are subordinated to the Civil Code itself. A full list of these twenty-nine statutes may be found in OSAKWE, *supra* note 20, at 65.

50. C. CIV. art. 3 (Russ.).

51. *Id.*

52. *Id.*

53. *See id.*

54. *See id.*

55. GRAZHDAIVSKII KODEKS ROSSISSKOI FEDERATSII S POSTATEINIMI MATERIALAMI IZ PRAKTIKI VISSHEGO ARBITRAZHNOGO SUDA ROSSISSKOI FEDERATSII [CIVIL CODE OF THE RUSSIAN FEDERATION ANNOTATED WITH ARTICLE-BY-ARTICLE MATERIALS DERIVED FROM CASE LAW OF THE SUPREME ARBITRATION COURT OF THE RUSSIAN FEDERATION] 6 (D.V. Mursin compiler, *Infra* M 1999) [hereinafter C. CIV. ANN.].

56. C. CIV. art. 6 (Russ.). Under article 6, statute by analogy is only used when the relations of the parties are not provided for by legislation, agreement by the parties or business custom. If this is the case civil legislation governing similar relations can be applied by analogy. If statute by analogy is inappropriate, article 6 allows for law by analogy, which provides that a court can apply principles of good faith, reasonableness and fairness. *Id.*

To invoke the principles of statute by analogy and law by analogy three requirements must be met.⁵⁷ First, statute by analogy may not be invoked if it would be inconsistent with the essence of the contract.⁵⁸ Second, any invocation of law by analogy shall be subject to the requirements of good faith, reasonableness and fairness.⁵⁹ Third, statute by analogy and law by analogy may not be used at the same time;⁶⁰ they can only be invoked sequentially.⁶¹ Statute by analogy is used first, and if that fails to resolve the problem, the court is free to fall back on law by analogy.⁶² Both statute by analogy and law by analogy allow courts to act as the legislature for a case under specific conditions.⁶³ A rule created by a court in this manner is an ad hoc rule,⁶⁴ devoid of any precedential authority.⁶⁵

International treaties, to which the Russian Federation is a party, are also integral parts of Russian law.⁶⁶ International treaties apply in Russian courts without enabling legislation unless the treaty calls for creation of an enabling law.⁶⁷ If a conflict arises between a rule of international law and a provision of Russian domestic law, the former prevails.⁶⁸

B. Case Law (*Sudebnoe Pravo*)

The second major source of modern Russian contract law is normative judicial legislation or binding case law.⁶⁹ Normative

57. *Id.*

58. *Id.*

59. *Id.*

60. *Id.*

61. *Id.*

62. C. Civ. art. 6 (Russ.).

63. *Id.*

64. *Id.*

65. Because Russia does not follow the system of *stare decisis*, a judgment by the Supreme Court in a specific case is not binding in future cases. These ad hoc judicial decisions, however, are distinguishable from normative judicial legislation. See *infra* note 72.

66. C. Civ. art. 7 (Russ.).

67. *Id.*

68. *Id.*

69. SUKHANOV 1, *supra* note 23, at 87. A leading Russian civil law textbook prefers to call this binding source of civil law "legal interpretation", as opposed to the non-binding "doctrinal interpretation" used by scholars. *Id.* The terms "judicial legislation" and "binding case law" are used loosely to define a novel phenomenon in Russian law. *Id.* Binding case law is not specifically referred to in the Russian Civil Code, or in any Russian statute, but evolved from Russian judicial practice. A thematic review of Russian judicial law-making practice in the area of contract law is contained in SUDEBNAIA I SUDEBNO-

judicial legislation takes one of four different forms: (1) an interpretive ruling (*raziasnenie*)⁷⁰ of the en banc session (plenum) of the Supreme Court of Arbitration of the Russian Federation [hereinafter S. Ct. Arb. R. F.]; (2) a decree (*postanovlenie*) of the en banc session of the S. Ct. Arb. R. F.; (3) an informational letter (*informatsionnoe pismo*) or overview letter (*obzornoe pismo*) of the presidium (executive committee) of the S. Ct. Arb. R. F.; and (4) a joint decree (*sovmestnoe postanovlenie*) of the en banc session of the S. Ct. Arb. R. F. sitting jointly with the en banc session of the Supreme Court of general jurisdiction of the Russian Federation [hereinafter regular S. Ct. R. F.]. Common to these four forms are the following features: the Supreme Court renders them in the form of advisory opinions (not in the context of an actual case or controversy); they are binding on future cases; the supreme court formulates them if there is a lack of uniformity among lower courts on a specific question of law; and they do not create new legal norms, but merely interpret and clarify existing norms.⁷¹ Thus, although the Anglo-American notion of judicial precedent is alien to the Russian legal system, a variation on binding case law does exist in Russian law.⁷²

C. Business Custom (*Obychai Delovovo Oborota*)

The third major source of modern Russian contract law is

ARBITRAZHNAIA PRAKTIKA, DOGOVORNIYE SPORY, SBORNIK DOKUMENTOV [JUDICIAL AND ARBITRAL PRACTICE, A COLLECTION OF DOCUMENTS ON CONTRACT DISPUTES] (M.U. Tikhomirov ed., Urinformtsentr 1999) [hereinafter TIKHOMIROV].

70. See "interpretive ruling" (*raziasnenie*) in ROSSISSKAIA URIDICHESKAIA ENTSIKLOPEDIYA [RUSSIAN LEGAL ENCYCLOPEDIA] 847-48 (A. Ia. Sukharev ed., Infra M 1999) [hereinafter SUKHAREV].

71. The Russian Legal Encyclopedia maintains that "a normative interpretive ruling does not contain an independent legal norm, [but] only establishes the time, meaning and sphere of operation of the law that it interprets" (author's translation). *Id.* at 847. But, Professor Sukhanov contends that "to the extent a legal interpretation is binding, it, in effect, creates a new legal norm which, as a matter of fact, has a retroactive effect" (author's translation). SUKHANOV 1, *supra* note 23, at 87. The author disagrees with Sukhanov's position. Under modern Russian law, interpretive rulings are a binding source of law, but do not create a new legal norm. Whereas under Soviet law they were neither a binding source of law nor a source of a new legal norm. See OSAKWE, *supra* note 20, at 355-57.

72. In this analysis, emphasis will be given to the increasingly important body of binding case law generated by the Supreme Court of Arbitration and the Supreme Court of General Jurisdiction of the Russian Federation - the highest courts of commercial and civil law in Russia. The most important interpretative rulings of the Supreme Arbitration Court of the Russian Federation are published in two competing casebooks. See C. CIV. ANN., *supra* note 55; see TIKHOMIROV, *supra* note 69.

business custom.⁷³ It includes any general rule of conduct, such as any traditionally accepted method of performing certain types of obligation that is widely accepted in any sphere of business activity,⁷⁴ including international business custom.⁷⁵ Where business custom conflicts with legislation or provisions of a contract, the latter takes precedence.⁷⁶ Otherwise, business custom is applicable regardless of whether it is expressly stated in any document.⁷⁷ To qualify as a business custom, the rule of conduct must be specific in its contents, the practice must be widely accepted and the practice must evolve within a specific sphere of business activity.⁷⁸ It may include localized business practices, but it does not have to be geographically localized.⁷⁹

In addition, legal scholarship (*doktrina*) plays a major role in understanding Russian contract law.⁸⁰ The opinions of Russian civil law scholars take the form of commentaries on the Civil Code,⁸¹ treatises⁸² and textbooks⁸³ on contract law. Whereas the

73. C. Civ. art. 5 (Russ.).

74. O.N. SADIKOV ET AL., KOMENTARII K GRAZHDANSKOMU KODEKSU ROSSISKOI FEDERATSII CHASTI PVOI (POSTATEINI) [COMMENTARY ON THE FIRST PART OF THE CIVIL CODE OF THE RUSSIAN FEDERATION (ARTICLE-BY-ARTICLE)] 17 (O.N. Sadikov ed., *Infra* M 1999) [hereinafter SADIKOV COMM. ONE].

75. C. Civ. art. 6 (Russ.).

76. C. Civ. art. 5 (Russ.).

77. C. Civ. ANN., *supra* note 55, at 8.

78. SADIKOV COMM. ONE, *supra* note 74, at 17.

79. *Id.*

80. SUKHANOV 1, *supra* note 23, at 87-88.

81. The three most authoritative commentaries on the Code are: SADIKOV COMM. ONE, *supra* note 74; O.N. SADIKOV ET AL., KOMENTARII K GRAZHDANSKOMU KODEKSU ROSSISKOI FEDERATSII CHASTI VTOROI (POSTATEINI) [COMMENTARY ON THE SECOND PART OF THE CIVIL CODE OF THE RUSSIAN FEDERATION (ARTICLE-BY-ARTICLE)] (O.N. Sadikov ed., *Infra* M 3d ed. 1999) [hereinafter SADIKOV COMM. TWO]; GUEV COMM. ONE, *supra* note 8; A.N. GUEV, POSTATEINI KOMENTARII K CHASTI VTOROI GRAZHDANSKOGO KODEKSA ROSSISKOI FEDERATSII (*Infra* M 2d ed. 1999) [hereinafter GUEV COMM. TWO]; M.I. BRAGINSKII ET AL., GRAZHDANSKII KODEKS ROSSISKOI FEDERATSII, CHAST PERVAIA, KOMENTARII DLIA PREDPRINIMATELEI [THE CIVIL CODE OF THE RUSSIAN FEDERATION, PART ONE, COMMENTARY FOR ENTREPRENEURS] (Khozaistvo i Pravo Magazine eds., Spark 2d ed. 1999) [hereinafter BRAGINSKII COMM.].

82. The most authoritative treatise on modern Russian contract law is M.I. BRAGINSKII & V.V. VITRIANSKII, DOGOVORNOE PRAVO, OBSHIE POLOZHENIA [CONTRACT LAW, GENERAL PROVISIONS] (Statut 2d 1998) [hereinafter BRAGINSKII CONTRACT 1998]. This original treatise was transformed into an on-going multi-volume series, as follows: BRAGINSKII CONTRACT 1999, *supra* note 23 and M.I. BRAGINSKII & V.V. VITRIANSKII, DOGOVORNOE PRAVO, KNIGA VTORAIA, DOGOVORI O PEREDACHE IMUSHESTVA [CONTRACT LAW, BOOK TWO, TRANSFER OF PROPERTY CONTRACTS] (Statut 2000) [hereinafter BRAGINSKII CONTRACT 2000].

theory of modern Russian contract law is articulated in statutory law and expounded upon in legal scholarship, it finds its practical fulfillment in judicial interpretations and business customs.⁸⁴ As such, this study will view Russian contract law from the perspectives of theory and practice.

IV. THE THEORIES AND FUNCTIONS OF CONTRACT

The premise of modern Russian contract law is that major decisions governing the production and distribution of public wealth should be autonomous⁸⁵ and not mandatory, private or collective.⁸⁶ The old socialist principle of state planning for the production and distribution of goods and services was abolished by reforms of 1991–1994.⁸⁷ Hence, the dominant economic function of modern Russian contract law is the bargained-for-exchange of

83. The Ministry of General and Professional Education of the Russian Federation officially recommended a textbook published by professors of civil law at Moscow State University for use in Russian law schools. SUKHANOV 1, *supra* note 23; 2(1) E.A. SUKHANOV, UCHEBNIK, GRAZHDANSKOE PRAVO [TEXTBOOK ON CIVIL LAW] (E.A. Sukhanov ed., BEK 2d ed. 1999) [hereinafter SUKHANOV 2(1)]. 2(2) E.A. SUKHANOV, UCHEBNIK, GRAZHDANSKOE PRAVO [TEXTBOOK ON CIVIL LAW] (E.A. Sukhanov ed., BEK 2d ed. 2000) [hereinafter SUKHANOV 2(2)]. A competing and equally authoritative textbook on contract law is a three-volume work published by the law faculty of the St. Petersburg State University: 1 N.D. EGOROV ET AL., GRAZHDANSKOE PRAVO, UCHEBNIK [CIVIL LAW, A TEXTBOOK] (A.P. Sergeev & Iu. K. Tolstoi eds., Prospekt 3d ed. 1999) [hereinafter EGOROV TEXTBOOK 1] (Sergeev and Tolstoi authored eight chapters in this series); 2 N.D. EGOROV ET AL., GRAZHDANSKOE PRAVO, UCHEBNIK (A.P. Sergeev & Iu. K. Tolstoi eds., Prospekt 2d ed. 2000) [hereinafter EGOROV TEXTBOOK 2]; 3 N.D. EGOROV ET AL., GRAZHDANSKOE PRAVO, UCHEBNIK (A.P. Sergeev & Iu. K. Tolstoi eds., Prospekt 2d ed. 2000) [hereinafter EGOROV TEXTBOOK 3]. On several doctrinal disputes involving contract law the Sukhanov textbook takes a position that is different from that which the Egorov textbook espouses – a reflection of the split between the Moscow and St. Petersburg schools of thought. For example, on the question of whether price is a significant condition of a contract of sale, the St. Petersburg school says it is not whereas Professor Braginskii, a prominent representative of its Moscow schools, says it is significant. EGOROV TEXTBOOK 1, *supra* note 83, at 499. See BRAGINSKII COMM., *supra* note 81, at 551, 560–61.

84. See generally TIKHOMIROV, *supra* note 69.

85. This means it should be left to the free will of the parties, as opposed to dictated and imposed by the state for society at large.

86. C. CIV. art. 1 (Russ.). The concepts of mandatory and collective contract processes were major ingredients of Soviet-era planning contracts. The prominent role of planning contracts in Soviet contract law is explained in 1 E. ALLAN FARNSWORTH & VIKTOR P. MOZOLIN, CONTRACT LAW IN THE USSR AND THE UNITED STATES: HISTORY AND GENERAL CONCEPTS 27–36, 60–75, 72–73, 84, 107–08, 132 (Int'l Law Inst. ed., 1987).

87. Makovsky & Khokhlov, *supra* note 24, at 65, 86.

wealth through the promises of individual parties.⁸⁸ The main vehicle for the production and distribution of goods and services is the onerous contract voluntarily entered into by private parties.⁸⁹

The modern Russian civil law doctrine attempts to explain the nature of contract by three theories: the "will theory," the "theory of the priority of law" and the "empirical theory" (economic theory of contract).⁹⁰ The "will theory" sees contract as an expression of the will of the contracting parties and views the law as supplementing or limiting the will of the parties.⁹¹ An element of this theory is the exaggerated notion of the freedom of the contracting parties to agree on whatever their will desires. The "priority of law" theory contends that law is superior to the will of the parties in a contract.⁹² This theory posits that a contract is a derivative from the law and possesses only such effect as the law confers upon it.⁹³ The implication is that the parties will exercise their freedom of contract only within the confines of, and to the extent permitted by the law. Thus, the notion of absolute freedom of contract is a fiction that exists only in a utopian state.⁹⁴ Finally, the "empirical theory" opines that the will of the parties is aimed at producing a specific economic effect and that the consequences of a contract are the means by which this economic result is attained.⁹⁵

The "priority of law" theory⁹⁶ best captures the philosophy of the Code.⁹⁷ According to Russian legal scholars, the essence of a

88. C. CIV. art. 1 (Russ.). The new spirit of private bargaining is reflected in the entrepreneurial philosophy of the 1994 Civil Code. See Makovsky & Khokhlov, *supra* note 24, at 68-69.

89. C. CIV. arts. 1, 9, 421 (Russ.); see also Makovsky & Khokhlov, *supra* note 24, at 70-71.

90. BRAGINSKII CONTRACT 1999, *supra* note 23, at 13.

91. *Id.*

92. *Id.*

93. *Id.*

94. See SUKHAREV, *supra* note 70, at 876.

95. BRAGINSKII CONTRACT 1999, *supra* note 23, at 13.

96. Examples of the priority of law theory include: 1) Article 162 provides that a foreign trade contract must be in writing, to be valid; 2) Under Articles 424 and 485 price is not an essential condition of a contract of sale, whereas under Article 555, price is an essential condition of a contract of sale of immovable property. As such, the parties to such a contract are not free to ignore the requirement of price stipulation. If they fail to stipulate price, the contract is invalid under Article 555; and 3) The rules governing statute of limitations in Articles 196 and 197 are imperative on the parties to a contract; these rules may not be modified or waived by agreement of the parties as stated in Article 198.

97. The priority of legal theory is reflected in the provisions of Articles 1 (not absolute freedom of contract) and 422 (private contracts must conform with law) of the

contract is the regulation of the conduct of its participants within the limits of the law; it is where the law prescribes the outer parameters within which the parties may operate and establishes certain consequences for violating the corresponding requirements.⁹⁸ A contract serves as an ideal way to control the activities of participants in the marketplace.⁹⁹

In Russian legal scholarship, contract (*dogovor*) has three different meanings in three different contexts.¹⁰⁰ First, it means the agreement of two or more persons by which civil law relations are created, modified or terminated.¹⁰¹ In this respect, "contract" means a bilateral or multilateral transaction. "Contract" is synonymous with a legal fact that creates an obligation; a source from which civil law rights and responsibilities emanate.¹⁰² The second meaning of "contract" is the legal obligation itself that arises from the agreement of these persons.¹⁰³ In this second context, "contract" refers to a legal relationship between the parties. In its third meaning, "contract" refers to a document that embodies the expressed will of the parties;¹⁰⁴ "contract" refers to the legal document that embodies the terms of its first and second meanings.

V. ARCHITECTURE OF RUSSIAN CONTRACT LAW: STRUCTURAL DIVISIONS OF THE LAW

The structure of modern Russian contract law follows traditional continental European civil law in that it is housed in the civil code and compartmentalized to govern different sets of contractual relationships.¹⁰⁵ Two approaches in continental European civil law govern the structural location of contract rules within the Code.¹⁰⁶ The French Civil Code of 1804, which houses

Code.

98. For a narrow reading of freedom of contract see SUKHAREV, *supra* note 70. See also my discussion in Section I below of the consequences of contracts that fail to conform to the requirements of the law.

99. BRAGINSKII CONTRACT 1999, *supra* note 23, at 14.

100. *Id.* at 14-15. It is important to be aware of the different meanings of the term "contract" because it enables the reader to understand the narrow context in which contract is being used in this article.

101. *Id.* at 15.

102. *Id.*

103. *Id.*

104. *Id.*

105. See generally C. CIV. (Russ.).

106. *Id.*

the rules on contract in one place (Book Three) represents the first approach.¹⁰⁷ The second approach, adopted by the German Civil Code of 1896, houses contract rules in two separate places: in the section of Book One dealing with transactions in general and in separate sections of Book Two devoted to contracts as special forms of obligation.¹⁰⁸

The Russian Code follows the German model.¹⁰⁹ Contract provisions are found in Part One sections devoted to transactions (*sdelki*) and sections of Part Two are devoted to twenty-six nominate contracts.¹¹⁰ In the event of a conflict between Parts One and Two, the special rules of Part Two prevail (*lex specialis derogat generali*).¹¹¹ The rules in Part One constitute the general rules (*lex generalis*), whereas the provisions in Part Two form the special rules (*lex specialis*). When there is a conflict, Part Two controls.¹¹²

Russian contract law embodies the law of several contracts and there are separate laws of contract for each of the twenty-six nominate contracts.¹¹³ Many of the laws of nominate contracts are fundamentally different from each other, such as formalities or conditions of the contract.¹¹⁴ Nevertheless, they operate against the backdrop of the general provisions of contractual obligations in Part One. This discussion focuses on the general principles of contract law in Part One.

The contract provisions of the Code apply to civil law contracts. It applies secondarily to contracts from parallel codes, such as employment contracts under the labor code, marriage

107. See generally C. Civ. (Fr.).

108. See generally C. Civ. (Ger.).

109. See generally C. Civ. (Russ.).

110. *Id.* Approximately 594 out of the 656 articles in Part Two on various forms of obligation are devoted to nominate contracts. Part Two of the Civil Code consists of thirty-one chapters (chapters 30-60) and 656 articles (arts. 454-1109) of which only five chapters, i.e. chapter 50 (arts. 980-89), 56 (arts. 1055-56), 57 (arts. 1057-60), 59 (arts. 1064-1101) and 60 (arts. 1102-09) deal with issues other than nominate contracts. Thus, in drafting a contract under Russian law, a lawyer must refer both to the general provisions of Part One on transactions and to sections of Part Two dealing with the nominate contract in question. See generally C. Civ. (Russ.).

111. Makovsky & Khokhlov, *supra* note 24, at 78-80.

112. *Id.* For example, in Part Two of the Code, price is not a significant condition of an ordinary contract of sale. See C. Civ. art. 485 (Russ.). But in the provisions governing the sale of realty, price is elevated to the level of a significant condition of the contract. C. Civ. art. 555 (Russ.). Thus, any contract for the sale of realty must stipulate the price. *Id.*

113. C. Civ. arts. 454-1109 (Russ.).

114. *Id.*

contracts under the family code, mineral leases under the mineral code and administrative law contracts under the administrative code.¹¹⁵ The Code governs only if the provisions of the relevant parallel code do not stipulate otherwise.¹¹⁶

The parties themselves decide the form and conditions of a contract.¹¹⁷ Such joint efforts are an exercise of the freedom of contract by the parties.¹¹⁸ If the signing of a contract, however, is a major component of the operations of a commercial organization, the latter might prefer to use model contracts in its operations.¹¹⁹ A model contract embodies standard formulas and terms for commonly used contracts.¹²⁰ A provision in a contract may, by reference, incorporate the terms of a model contract.¹²¹ Even if a contract does not specifically incorporate the provisions of a model contract by reference, such provisions may, nevertheless, be applicable to the contract due to business custom.¹²²

With respect to the application of statutory law to contracts, the general rule is that civil legislation shall operate prospectively.¹²³ Obligations that arise after legislation is adopted shall be governed by the legislation.¹²⁴ If, after a contract has been signed, a new law is passed that changes the existing conditions of the contract that were obligatory, the existing conditions of the contract continue to operate unless the law provides otherwise.¹²⁵

VI. CONTRACT INTERPRETATION: BASIC CONCEPTS

In contract interpretation, two methods are applied in a sequential order of priority.¹²⁶ First, the court discerns the literal meaning of the words and phrases contained in the contract.¹²⁷ This requires analyzing contract provisions in juxtaposition and

115. GUEV COMM. ONE, *supra* note 8, at 6.

116. *Id.*; C. CIV. art. 3 (Russ.).

117. C. CIV. art. 421 (Russ.).

118. *Id.*

119. A model contract, like a boilerplate contract, is intended to avoid repetitious drafting of contracts with similar provisions. See C. CIV. art. 427 (Russ.).

120. *Id.* The problems posed by the use of model contracts in practice are addressed in the Civil Code. See *id.*

121. *Id.*

122. *Id.*

123. C. CIV. art. 4 (Russ.).

124. *Id.*

125. C. CIV. art. 422 (Russ.).

126. C. CIV. art. 431 (Russ.).

127. *Id.*

examining the general meaning of the contract as a whole.¹²⁸ If this method fails to yield the desired result, the court proceeds to the second method: to discern the objective intent of the parties, as opposed to the unarticulated, secret intentions of each party. This objective intent is deduced from the purpose of the contract.¹²⁹ This method reasons that the purpose of the contract may be attained only within the context of the text itself.¹³⁰ To discover the objective intent of the parties, the court examines other related documents, such as pre-contract communications between the parties, other documentary evidence of the existing relationship between the parties, subsequent conduct of the parties, etc.¹³¹ The court uses the latter technique against the backdrop of business custom.¹³² In short, the two-phase technique for contract interpretation gives priority to the contract's literal textual meaning over the general common intent of the parties.¹³³

VII. CONTRACT FORMATION: MUTUAL ASSENT TO A BARGAIN

A contract is "an agreement of two or several persons on establishing, changing, or terminating civil law rights and duties."¹³⁴ Accordingly, it takes a contract to create an obligation; it takes another contract to modify an existing obligation and yet a third contract to extinguish an on-going obligation.¹³⁵ Thus, a mutual agreement to terminate or modify an existing contract is itself a contract,¹³⁶ as is a novation of an existing contract.¹³⁷ More importantly, the legal enforceability of a contract is based not on "promise," as is the case under the Anglo-American common law system, but rather on "agreement" in the tradition of continental European civil law systems.¹³⁸ The Russian definition of a contractual obligation encompasses two different types of

128. *Id.*

129. *Id.*

130. *See id.*

131. *Id.*

132. *Id.*

133. *Id.*

134. C. CIV. art. 420 (Russ.).

135. *See id.* This deductive statement flows from the definition of contract in Article 420, i.e., an agreement that creates, modifies or extinguishes an obligation.

136. *See* C. CIV. art. 450 (Russ.).

137. *See* C. CIV. art. 414 (Russ.).

138. *See* C. CIV. art. 420 (Russ.). Following the tradition of the French Civil Code, the Louisiana Civil Code defines a contract as an agreement, rather than as a promise. LA. CIV. CODE ANN. art. 1906 (West 1987).

obligation: one based solely on an agreement of the parties and immediately performed by both, such as a performed barter or a performed cash sale (non-promissory transaction),¹³⁹ and one based on an exchange of promises that looks to future performance by the parties or by one of the parties (promissory transaction).¹⁴⁰ In U.S. common law only a promissory transaction qualifies as a contract.¹⁴¹

Under Russian law, contract formation requires the participation of two or more persons. One cannot contract with himself¹⁴² because a unilateral contract is a legal impossibility.¹⁴³ Contract formation requires four elements: an offer, an acceptance, compliance with any requisite legal form and an agreement on the significant conditions of the contract.¹⁴⁴ But, the actual process of contract formation contains three steps: an offeror sends an offer to an offeree; the offeree considers the terms of the offer and accepts; and the offeror receives the offeree's acceptance.¹⁴⁵ Unless the parties otherwise agree or a law otherwise provides, a contract is deemed to be concluded when the offeror receives the offeree's acceptance.¹⁴⁶ The exchange of offer and acceptance constitutes the parties' assent to an agreement.¹⁴⁷

In determining what constitutes assent, Russian law does not look to the parties' intentions (the subjective theory), but to their externally manifested objective acts (the objective theory).¹⁴⁸ Under the objective theory, the law looks to the objective manifestation of the parties' intentions as demonstrated by their words or conduct, not to their unarticulated or unmanifested subjective intentions.¹⁴⁹ Therefore, what matters is not what the parties intended to achieve, but failed to express in the contract,

139. In Russian contract law a non-promissory transaction is called "real'nyi dogovor" (executed contract). See OSAKWE, *supra* note 20, at 164.

140. In Russian contract law a promissory transaction is called "Kontsessual'nyi dogovor" (executory contract). See *id.*

141. See RESTATEMENT (SECOND) OF THE LAW OF CONTRACTS § 1 cmts. a, b, c (1979).

142. C. CIV. art. 420 (Russ.).

143. *Id.*

144. C. CIV. art. 432 (Russ.).

145. *Id.*

146. See C. CIV. art. 431 (Russ.).

147. C. CIV. art. 432 (Russ.).

148. See C. CIV. art. 431 (Russ.).

149. *Id.*

but rather what they manifested by their external acts.¹⁵⁰ Thus, as long as there is agreement on the same thing (*consensus ad idem*), assent to an agreement can exist absent a "meeting of the minds" by the parties.¹⁵¹

A. Offer (*Oferta*)

The first element required for contract formation is an offer, which is an invitation by one person (the offeror) to another person (the offeree) to enter into a contract.¹⁵² To be valid, an offer must be externally manifested¹⁵³ and it must be definite.¹⁵⁴ The external manifestation test requires an offer to be manifested by words or conduct.¹⁵⁵ The definiteness test means that an offer may not leave any doubts as to its terms and conditions.¹⁵⁶ An offer must be definite, embody the significant conditions of the proposed contract, express the intention of the offeror to conclude a contract with the offeree and be addressed to a particular person.¹⁵⁷

An offer may also stipulate a time period for acceptance.¹⁵⁸ There is a presumption that an offer is irrevocable prior to the expiration of the stipulated time limit or, absent such time limit, within a reasonable time.¹⁵⁹ But, the offeror could stipulate that the offer may be withdrawn at any time.¹⁶⁰ Also, the revocability of an offer may be inferred from the nature of the offer or from the totality of the circumstances in which it was made.¹⁶¹ This Russian rule follows the French Civil Code.¹⁶² Under the French

150. *Id.*

151. See C. CIV. art. 431 (Russ.). The "meeting of the minds" test goes to the intention of the parties, whereas the "assent" test goes to how they acted.

152. C. CIV. art. 435 (Russ.).

153. See *id.*

154. *Id.*

155. C. CIV. art. 159 (Russ.). If any governing law does not require a contract to be concluded in a written form, it may be concluded orally. SUKHANOV 1, *supra* note 23, at 344; see C. CIV. art. 159 (Russ.). As such, an offer to conclude an oral contract can be made orally. C. CIV. art. 159 (Russ.). A written offer can be manifested in one of several forms, e.g., letter, telegram, fax, etc. C. CIV. art. 160 (Russ.). See also BRAGINSKII COMM, *supra* note 81, at 569.

156. See GUEV COMM. ONE, *supra* note 8, at 704.

157. BRAGINSKII COMM., *supra* note 81, at 569; see C. CIV. art. 435 (Russ.).

158. C. CIV. art. 440 (Russ.).

159. C. CIV. art. 436 (Russ.).

160. *Id.*

161. *Id.*

162. C. CIV. art. 1142 (Fr.). This principle of French law is derived from case law, not

rule, an offeror who prematurely withdraws his offer is liable in damages to the offeree.¹⁶³ By contrast, under the German contract law, "the offeror is bound by his offer, in the sense that he cannot effectively withdraw it, either during a period set by himself or during a reasonable period."¹⁶⁴

Under Russian law, an offer is to be distinguished from the solicitation of an offer, which is a mere invitation to make an offer.¹⁶⁵ For example, an advertisement is not an offer but merely an invitation to make an offer.¹⁶⁶ Typically, an advertisement is addressed to members of the public, provides generalized information about a product or service and is intended to solicit an offer from the public.¹⁶⁷

Russian law does allow an offer to be made to the public.¹⁶⁸ It distinguishes between a particularized offer and a public offer.¹⁶⁹ A public offer is addressed to an indeterminate number of persons, contains the significant conditions of the proposed contract and explicitly expresses the intention of the offeror to enter into a contract with any person who accepts the terms of the offer.¹⁷⁰ Finally, an offer could be either written or oral.¹⁷¹ The law may require a specific form for a specific type of contract.¹⁷²

B. Acceptance (*Aktsept*)

The second element of contract formation is an acceptance, which is a response from the addressee expressing acceptance of the offer and an intention to enter into a contract with the offeror on the terms and conditions stipulated in the offer.¹⁷³ An acceptance must be total and unconditional.¹⁷⁴ Under this rule, an acceptance must be a firm expression of commitment;¹⁷⁵ the commitment may not be conditioned on any further act by the

from the Civil Code itself. See ZWEIGERT & KOTZ, *supra* note 23, at 39.

163. See ZWEIGERT & KOTZ, *supra* note 23, at 39.

164. *Id.* at 41.

165. C. Civ. art. 437 (Russ.).

166. *Id.*

167. C. Civ. art. 437 (Russ.).

168. C. Civ. art. 437 (Russ.).

169. *Id.*

170. *Id.*

171. C. Civ. art. 158 (Russ.).

172. C. Civ. art. 159 (Russ.).

173. C. Civ. art. 438 (Russ.).

174. *Id.*

175. *Id.*

offeree or the offeror;¹⁷⁶ and the commitment must mirror the terms stipulated in the offer.¹⁷⁷ Under Russian law, the offeror is the master of his offer; only he can dictate the terms of the offeree's acceptance thereof.

The form of an acceptance depends on the nature of the contract itself.¹⁷⁸ It can be oral, written or expressed by conduct.¹⁷⁹ The law creates a presumption that silence or lack of action does not constitute an acceptance.¹⁸⁰ This presumption may be overcome if it can be inferred from statute, business custom or the existing business relationship between the parties that silence or non-action constitutes acceptance.¹⁸¹ To be valid, the offeror must receive the acceptance within the time limit stipulated in the offer or, absent such time limit, within a reasonable time from when the offer was made.¹⁸² Acceptance of an offer on terms different from those in the offer is neither total nor unconditional.¹⁸³ As such, a modified acceptance is not regarded as an acceptance, but rather as a counter offer.¹⁸⁴ Therefore, any modification of the terms of an offer, including insignificant modifications, transforms the offeree's answer into a counter offer.¹⁸⁵

Typically, the contract itself stipulates where or when it is concluded.¹⁸⁶ If it fails to do so, a contract is considered concluded at the offeror's place of residence (if the offeror is a natural person) or at the offeror's seat (if the offeror is a legal person).¹⁸⁷

Generally, a contract between absent parties (*inter absentes*) is deemed concluded when the offeror receives the acceptance.¹⁸⁸ The Russian rule, however, rejects the "mailbox theory" of Anglo-American common law and the "knowledge theory" of French

176. C. Civ. art. 443 (Russ.).

177. *Id.*

178. *See id.*

179. *See* C. Civ. arts. 434, 438 (Russ.).

180. C. Civ. art. 438 (Russ.).

181. *Id.*

182. C. Civ. arts. 440, 441 (Russ.).

183. *See* C. Civ. arts. 443, 448 (Russ.).

184. C. Civ. art. 443 (Russ.).

185. *Id.* This Russian rule is notably different from its modern U.S. usage governing the conditions of an acceptance as it applies to the sale of goods. *See* U.C.C. § 2-207(1), (2) cmts. 2-6 (2001).

186. C. Civ. art. 444 (Russ.).

187. *Id.*

188. C. Civ. art. 433 (Russ.).

law, but is similar to the “time of arrival theory” in German law.¹⁸⁹ If the law requires that the contract must be registered with a state agency, then it is concluded at the time of registration.¹⁹⁰ If the contract calls for the transfer of property, it is considered concluded at the time the property is transferred.¹⁹¹

The following procedure applies to concluding involuntary contracts.¹⁹² Upon receipt of an offer, the offeree must examine the terms and prepare the response within thirty days.¹⁹³ The offeree has three options. The offeree may accept the offer totally and unconditionally,¹⁹⁴ resulting in a signed contract on the terms proposed in the offer.¹⁹⁵ The offeree may express the desire to conclude a contract on terms different from the offer.¹⁹⁶ Finally, the offeree may refuse to enter into the contract.¹⁹⁷ The offeree’s refusal to conclude a public contract with the offeror may be based on either unavailability of goods or the absence of proper facilities for the offeree to render services demanded.¹⁹⁸ Upon the offeree’s refusal, the offeror may take the matter to court,¹⁹⁹ where the offeree may be compelled to enter into the contract and determine

189. ZWEIGERT & KOTZ, *supra* note 23, at 35-44. See also C. CIV. art. 433 (Russ.). For a concise description of these three modern theories see ZWEIGERT & KOTZ, *supra* note 23, at 35-44.

190. C. CIV. art. 433 (Russ.).

191. *Id.*

192. In Russian law, different rules govern if the parties are not free in their decision to enter into a contract (the involuntary or compulsory contract), C. CIV. art. 445 (Russ.); see also EGOROV TEXTBOOK 1, *supra* note 83, at 518-19. For example, a compulsory contract is one that obligates the organizer of a public bid to conclude a contract with its winner. See C. CIV. art. 1057 (Russ.); see also SADIKOV COMM. ONE, *supra* note 74, at 712.

193. C. CIV. art. 445 (Russ.).

194. *Id.*

195. *Id.*

196. *Id.* Under the general rule in Article 438, this would be tantamount to a counteroffer. But, because it is specifically permitted under Article 445 as an exception to its general rule, it does not constitute a counter offer. *Id.* The offeror who receives a list of objections from the offeree must, within thirty days of the receipt of the objections, submit the matter to a court, which decides the terms of the proposed contract. *Id.*

197. *Id.* This third option is only available for public contracts. See C. CIV. art. 426 (Russ.). Article 426 is a special procedure for public contracts. It states that if the offeree has the capacity to provide the needed goods or services, he may not refuse to contract with the offeror; if he unjustifiably refuses to contract, the offeror may trigger the procedure in Article 445 to compel action. *Id.* Thus, Article 426 effectively denies the offeree in a public contract the freedom of contract enshrined in Article 1 for all other types of contract. *Id.* Therefore, Article 426 is read as limiting Article 1 for public contract offerees only.

198. See C. CIV. art. 426 (Russ.).

199. C. CIV. art. 445 (Russ.).

its terms.²⁰⁰

C. Conformance with the Requisite Form (Forma Dogovora)

The third element in contract formation is conformance with the requisite form, which may be directed by law or stipulated by the contract.²⁰¹ Unless otherwise required by law, the general rule is that the parties may form a contract orally²⁰² or they may agree to reduce their contract to writing.²⁰³ In some situations, a statute may require that a contract not only be written, but notarized as well.²⁰⁴ A statute may also require that a contract be in writing and be notarized and registered with a state agency.²⁰⁵ For example, all contracts involving real estate fall within this last category.²⁰⁶

In Russian contract law, a great deal of case law has revolved around the formality of contracts for the sale of realty.²⁰⁷ On this issue, the Court provided the following binding interpretation of the Code. If a contract requiring state registration is concluded in the requisite manner, but one of the parties refuses to register the contract, a court shall have the right, at the other party's petition, to direct the proper state agency to register the contract.²⁰⁸ Prior to state registration of a realty contract, a buyer does not have the right to enter into a contract for the alienation of the said realty.²⁰⁹ A sales contract for a nonresidential building shall be deemed concluded at the time of signing, not at the time of state registration.²¹⁰ A residential building, however, may be the object of a sales contract, but the right of ownership arises only when the state registers the contract.²¹¹

200. *Id.* The procedure for concluding contracts at a public auction is set forth in the Civil Code. C. Civ. arts. 447-49 (Russ.).

201. C. Civ. art. 434 (Russ.).

202. C. Civ. arts. 158, 159 (Russ.).

203. C. Civ. art. 158 (Russ.).

204. C. Civ. art. 160 (Russ.).

205. *Id.*

206. C. Civ. art. 164 (Russ.).

207. That case law is summarized in the Informational Letter of the Supreme Arbitration Court 21 of November 13, 1997 entitled "A Review of Practice Relating to the Settlement of Disputes Arising from the Contract of Sale of Realty."

208. C. Civ. art. 551 (Russ.).

209. *Id.*

210. C. Civ. art. 556 (Russ.).

211. C. Civ. art. 558 (Russ.).

D. Agreement on Essential Conditions (Sushchestvennyye Usloviia Dogovora)

The fourth requirement for contract formation is that an agreement must be reached on material conditions.²¹² Under Russian law, there are three types of conditions: significant, general and specific.²¹³ Significant conditions are those that must be met in order for a particular contract to come into existence.²¹⁴ A general condition is one that is generally associated with a given type of contract.²¹⁵ Normally it is stipulated by law and automatically becomes effective when a given type of contract is formed.²¹⁶ Typically, a general condition does not need to be negotiated by the parties, which is not equivalent to it being involuntarily incorporated into the contract.²¹⁷ Rather, it is stipulated by law and the parties, by entering into the given type of contract, consciously and voluntarily adopt the condition.²¹⁸ If the parties do not wish to adopt the statutorily stipulated general contract conditions, however, they can vary such conditions by mutual agreement.²¹⁹ Lastly, specific conditions are those that supplement or modify the general conditions.²²⁰ In any contract, the parties are free to include specific conditions that fit their purpose.²²¹

The fourth requirement of contract formation focuses on the significant conditions.²²² They include the following: conditions relating to the object of the contract, conditions stipulated by law as essential for a particular type of contract and conditions stipulated by one of the parties as significant for this contract.²²³ Thus, the meaning of significant contractual conditions varies from one contract to another.²²⁴

212. C. CIV. art. 432 (Russ.).

213. EGOROV TEXTBOOK 1, *supra* note 83, at 499.

214. *Id.*

215. *Id.* at 500.

216. *Id.*

217. *Id.*

218. *Id.*

219. *Id.* at 500-01.

220. *Id.* at 501.

221. *Id.* at 501-02.

222. C. CIV. art. 432 (Russ.).

223. *Id.*

224. See GUEV COMM. ONE, *supra* note 8, at 698.

An ongoing dispute among Russian commentators as to whether price is a significant condition of a sales contract highlights the analysis of essential conditions.²²⁵ One school of thought, headed by Professor Vitrianskii, holds that price is a significant condition of any contract in which there is consideration, including a contract of sale.²²⁶ In contrast, Professors Sadikov,²²⁷ Sergeev, Tolstoi and others assert that the Code does not elevate price to the level of a significant condition in all sales contracts.²²⁸

In support of their position, the latter group of authors contend that Article 424, para. 3 of the Code states if the parties fail to stipulate a price, and it is not possible to determine the price from the conditions of the contract, the fair market value for analogous goods or services shall be applied to a contract requiring consideration.²²⁹ In opposition, Vitrianskii cites a ruling interpreting this provision to mean that in determining the prevailing price for analogous goods or services in the marketplace, the burden of proof lies with the interested party.²³⁰ If the parties fail to reach an agreement on the price, the contract shall be deemed incomplete.²³¹ Thus, Vitrianskii reads this section to mean that price is a significant condition of any contract of sale.

Yet, a close reading of Article 424 para. 3 reveals it is erroneous to interpret price as a significant condition of all contracts for sale. In those nominate contracts where the Code intends to elevate price to the level of a significant condition, it does so expressly and unequivocally.²³² For example, price is listed as a significant condition in contracts for the sale of realty.²³³ In all other contracts in which consideration is granted, including the contract of sale, the rule in Article 424 para. 3 applies unless statute or contract provides otherwise.²³⁴ As applied to a sales contract, this means that terms relating to type and quantity of

225. BRAGINSKII COMM., *supra* note 81, at 560.

226. *See id.*

227. EGOROV TEXTBOOK 1, *supra* note 83, at 499; *see also* SADIKOV COMM. ONE, *supra* note 74, at 681.

228. EGOROV TEXTBOOK 1, *supra* note 83, at 499.

229. C. CIV. art. 424 (Russ.).

230. BRAGINSKII COMM., *supra* note 81, at 563.

231. *Id.*

232. C. CIV. art. 555 (Russ.).

233. *Id.*

234. C. CIV. art. 424 (Russ.).

goods are significant contract conditions whereas terms relating to the quality and the price of goods are not significant. Any dispute relating to important items of a contract of sale, such as quality and price of goods, shall be resolved under the general guidelines of Article 424 para. 3. "In cases when in a compensated contract a price is not provided and may not be determined proceeding from the terms of the contract, performance of the contract must be paid for at the price that, under comparable conditions, usually is taken for analogous goods, work, or services."²³⁵

E. Other Requirements of Contract Formation

There are five additional essential requirements of contract formation: (1) the parties have dispositive capacity to contract; (2) the object of the contract is lawful; (3) mutuality of obligation exists between the parties; (4) mutuality of agreement exists between the parties; and (5) there are at least two parties to the contract.²³⁶

As to capacity to contract, the Russian Code distinguishes between legal capacity (*pravosposobnost*)²³⁷ and dispositive capacity (*deesposobnost*).²³⁸ All natural persons, from birth until death, have legal capacity.²³⁹ The general age of dispositive capacity to contract, however, is eighteen years old.²⁴⁰ Yet by virtue of emancipation, persons below eighteen may acquire dispositive capacity to enter into a contract.²⁴¹ Infants (persons between the ages of six and fourteen years) have partial dispositive capacity to contract for essentials.²⁴² By contrast, persons between the ages of fourteen and eighteen years (minors) have partial dispositive capacity to contract.²⁴³ The dispositive capacity of legal persons coincides with their legal capacity and arises at the time of formation, which is the time of their proper registration with state authorities.²⁴⁴

235. *Id.*

236. C. CIV. arts. 21, 420, 432 (Russ.); SUKHANOV 1, *supra* note 23, at 342-44; see generally EGOROV TEXTBOOK 1, *supra* note 83, at 495-504.

237. C. CIV. art. 17 (Russ.).

238. C. CIV. art. 21 (Russ.).

239. C. CIV. art. 17 (Russ.).

240. C. CIV. art. 21 (Russ.).

241. C. CIV. art. 27 (Russ.).

242. C. CIV. art. 28 (Russ.).

243. C. CIV. art. 26 (Russ.).

244. C. CIV. art. 49, 51 (Russ.).

Russian contract law requires a lawful purpose (*pravomernost obekta dogovora* called *cause licite* under French law²⁴⁵ and *causa* under Roman law²⁴⁶ and other continental European civil codes.²⁴⁷) The concept of cause in Roman law or continental European law is not the same as consideration in Anglo-American theory of contract.²⁴⁸ Legal systems that require *causa* as an element of a contract do not require consideration.²⁴⁹ The requirement of consideration for all contracts is an idiosyncrasy of Anglo-American common law. In fact, the concept of *causa* is "a peculiarity of Continental codes and other attempts at systematization . . . The concept is unknown in England and the United States" ²⁵⁰ Even though *causa* is an element of the German contract theory, Professors Zweigert and Kotz note that in German practice "causa plays virtually no part in the law of contracts."²⁵¹ Typically, the object, or purpose, of a contract is an

245. C. Civ. arts. 1108, 1131, 1138 (Fr.) (1804).

246. I.B. NOVITSKII & I.S. PERETERSKII, *RIMSKOE CHASTNOE PRAVO* [ROMAN PRIVATE LAW] 244-46 (Urisprudentsia 1999). In three succinct provisions of the Louisiana Civil Code, the doctrine of cause is described as, "an obligation [that] cannot exist without a lawful cause," the reason why a party obligates himself. "The cause of an obligation is unlawful when the enforcement of the obligation would produce a result prohibited by law or against public policy." LA. CIV. CODE ANN. art. 1966 (West 1987).

247. See e.g., C. Civ. arts. 134, 138, 309 (Ger.). Civil law cause and common law consideration are entirely different things. For a classical civil law definition of cause, see LA. CIV. CODE ANN. art. 1967 (West 1987); see also the accompanying commentary in LA. CIV. CODE ANN. 458 - 59 (West 1999).

248. See ZWIEGERT & KOTZ, *supra* note 23, at 71-82.

249. But the requirement of both *causa* and consideration as elements of a contract may be found in some mixed jurisdictions such as California. For example, the California Civil Code, reflecting the influence of both Spanish and Anglo-American law, requires both *causa* and consideration for formation. CAL. CIV. CODE § 1550 (West 2000). The California Civil Code lists four essential elements of a contract, capacity of the parties to contract, consent of the parties, a lawful object (which is the same thing as *causa*), and a sufficient cause or consideration. *Id.* By contrast, the Louisiana Civil Code requires *causa*, but not consideration for formation. LA. CIV. CODE ANN. arts. 1910, 1966 (West 1987).

250. ZWIEGERT & KOTZ, *supra* note 23, at 8.

251. *Id.* at 81. *Causa* as an element of a contract is a characteristic feature of continental European legal systems that follow the French Civil Code, but not the Germanic systems. C. Civ. art. 1108 (Fr.) (1804). Notwithstanding the fact that in comparative law *causa* is generally distinguishable from the consideration, one must note the fact that the California Civil Code uses the terms *cause* and *consideration* interchangeably, which suggests they could mean the same thing. CAL. CIV. CODE § 1550 (West 2001). Because the same provision of the California Civil Code speaks separately of a lawful object, it follows that the word *cause* in paragraph 4 does not mean the same thing as *cause* in Articles 1108, 1131 and 1133 of the French Civil Code. CAL. CIV. CODE § 1550 (West 2001). Note also that the Restatement distinguishes consideration from the "motive

act that a party to the contract must perform either by action or inaction.²⁵² The contract can explicitly state the purpose, or the purpose could implicitly flow from it.²⁵³ The term “object of a contract” also refers to the thing or value around which relations between the parties to the contract revolve.²⁵⁴ In this context, the object could be tangible, like securities, intangible property, like a property right, or any other object of civil law relations recognized under Article 2.²⁵⁵

Two other requirements are mutuality of obligation and mutuality of agreement. Because a contract creates, modifies, or terminates an obligation between the parties²⁵⁶, mutuality of obligation requires an obligation created for one party to be counterbalanced by an obligation on the other party.²⁵⁷ For example, a contract of donation obligates the donor to make a donation and the donee to accept the donation. Mutuality of obligation, however, does not mean that both parties must have both rights and duties.²⁵⁸ Such distribution of rights and duties is called for only in bilateral contracts.²⁵⁹ A unilateral contract, for instance, only requires that one party have all the rights and the other party have all the duties.²⁶⁰ For example, in the unilateral contract of donation, the donee has all the rights (i.e., the right to demand the donation from the donor, but no duties to the donor) and the donor has all the duties (i.e., the duty to make the donation, but has no rights against the donee). Mutuality of agreement (i.e., coordination of the wills of the parties) calls for a meeting of the minds by the parties on the terms (i.e., significant conditions) of the contract.²⁶¹

Finally, a contract mandates the participation of at least two persons.²⁶² In this sense, Russian law defines a contract as a

or inducing cause” of a contract. RESTATEMENT (SECOND) OF CONTRACTS § 81 (1979).

252. BRAGINSKII COMM., *supra* note 81, at 563.

253. SUKHANOV 1, *supra* note 23, at 344-45. Typically, if a contract is in written form, its purpose is explicitly stated in the contract. But if the contract is concluded orally or by conduct, its purpose is usually implicit. *Id.*

254. BRAGINSKII COMM., *supra* note 81, at 563.

255. C. CIV. art. 2 (Russ.).

256. GUEV COMM. ONE, *supra* note 8, at 669.

257. EGOROV TEXTBOOK 1, *supra* note 83, at 508.

258. *Id.*

259. *Id.*

260. *Id.*

261. See SUKHANOV 2(1), *supra* note 83, at 152.

262. C. CIV. art. 420 (Russ.).

bilateral (or multilateral) transaction because the same person cannot contract with himself.²⁶³

A final consideration in contract formation is the time at which the contract enters into force. A "contract shall enter into force and become obligatory for the parties from the time of its formation."²⁶⁴ As a general rule formation occurs when the offeree accepts the offer.²⁶⁵ The parties, however, may stipulate that the contract conditions are applicable prior to its conclusion.²⁶⁶

For a U.S. lawyer, the following comparative features of Russian law stand out. First, Russian law does not require an exchange of promises for formation.²⁶⁷ Instead, the exchange of promises that looks to a future performance is present only in an executory contract.²⁶⁸ Second, Russian law does not require consideration.²⁶⁹ Consideration is required for the formation of an onerous contract,²⁷⁰ but not for a gratuitous contract.²⁷¹ Third, unless otherwise provided by law or by the terms of the offer itself, an offer is irrevocable prior to the expiration of the offeror's established time limit.²⁷² If a time limit for its acceptance is not established in the offer, it may not be revoked within a reasonable time, which the offeror must allow the offeree for consideration and acceptance.²⁷³ Fourth, the offeree cannot assign an offer to a third person.²⁷⁴ An offer is intended exclusively for the offeree specified by the offeror.²⁷⁵ An offer is not assignable, inheritable

263. C. CIV. art. 154 (Russ.).

264. C. CIV. art. 425 (Russ.).

265. C. CIV. art. 433 (Russ.).

266. C. CIV. art. 425 (Russ.).

267. C. CIV. art. 420 (Russ.). Russian contract law defines contracts as an agreement rather than as a promise to do something in the future. *Id.*

268. Russian law classifies contracts into executed and executory. See OSAKWE, *supra* note 20, at 164; see also SUKHANOV 1, *supra* note 23, at 336. The Code does not denominate contracts as executed or executory. These are doctrinal categories as well as extrapolations based on the author's reading of the code.

269. Russian law classifies contracts into gratuitous (without consideration) and onerous (with consideration). See OSAKWE, *supra* note 20, at 164; see also C. CIV. art. 423 (Russ.); SUKHANOV 1, *supra* note 23, at 336.

270. See OSAKWE, *supra* note 20, at 164; see also C. CIV. art. 423 (Russ.); SUKHANOV 1, *supra* note 23, at 336.

271. See OSAKWE, *supra* note 20, at 164; see also C. CIV. art. 423 (Russ.); SUKHANOV 1, *supra* note 23, at 336.

272. C. CIV. art. 436 (Russ.).

273. SADIKOV COMM. ONE, *supra* note 74, at 706.

274. See SUKHANOV 2(1), *supra* note 83, at 168-73.

275. *Id.*

or transferable by any other method.²⁷⁶ Fifth, the acceptance must be total and unconditional.²⁷⁷ Any modification to the terms of an offer, including insignificant modifications, transforms the offeree's answer from an acceptance into a counteroffer.²⁷⁸

VIII. CLASSIFICATION OF CONTRACTS: CRITERIA FOR CLASSIFICATION AND TYPES OF CONTRACTS

A comprehensive classification of contracts under Russian law is formulated after a close reading of the provisions of the entire Code.²⁷⁹ Some contract types are mentioned in Part One,²⁸⁰ others are discussed in obscure provisions of Part Two²⁸¹ and others are mentioned only in case law. The most elaborate classification of contracts under Russian law is one in which types of contracts are arranged with their opposite counterparts. The following illustrates this arrangement: (1) gratuitous (*bezvozmezdnı*) and onerous (*vozmezdnı*); (2) certain and aleatory; (3) principal and accessory; (4) void and voidable; (5) unilateral and bilateral; (6) bilateral and multilateral; (7) nominate and innominate; (8) oral and written; (9) simple-written and notarially certified; (10) in favor of a third party and in favor of the contracting parties; (11) free and compulsory; (12) unilaterally compulsory and bilaterally compulsory; (13) expressed and implied; (14) conditional and unconditional; (15) suspensive - conditional and resolutory - conditional; (16) divisible and indivisible; (17) jointly negotiated and adhesion; (18) mixed and unitype; (19) preliminary and principal; (20) consensual and real; (21) de jure and putative; (22) de jure and de facto; (23) executed and executory; (24) alternative and single; and (25) enforceable and unenforceable.²⁸²

A gratuitous contract has no consideration.²⁸³ It is an economically sterile transaction because it does not promote an increase in, or an exchange of, public wealth.²⁸⁴ In contrast, an

276. *Id.*

277. See C. CIV. art. 438 (Russ.).

278. C. CIV. art. 443 (Russ.).

279. See generally C. CIV. (Russ.).

280. See C. CIV. arts. 1-453 (Russ.).

281. See C. CIV. arts. 453-1109 (Russ.).

282. OSAKWE, *supra* note 20, at 163-64.

283. C. CIV. art. 423 (Russ.).

284. EGOROV TEXTBOOK 1, *supra* note 83, at 509. Examples of gratuitous contracts include donation contracts or contracts for the free use of property. In a contract of

onerous contract has consideration.²⁸⁵ Russian law presumes that a contract is onerous unless otherwise provided by law or contract.²⁸⁶ An onerous contract is either certain (the bargained-for object is certain to occur) or uncertain (the bargained-for object is dependent on a chance that it may or may not happen).²⁸⁷ The distinction between gratuitous and onerous contracts is based on the meaning of consideration in Russian contract law. Unlike classical U.S. contract theory, which defines consideration as either a legal detriment suffered by the offeree or a legal benefit received by the offeror, Russian contract theory regards only the legal benefit granted by one party to the other as consideration.²⁸⁸ The mere fact that the offeree suffered a legal detriment is not sufficient consideration for an onerous contract.²⁸⁹

Other types of contracts are aleatory contracts, or contracts of chance,²⁹⁰ and accessory contracts, which depend upon and service a principal contract.²⁹¹

donation (article 572), as in a contract of gratuitous use of property (article 689), the grantor does not receive any reciprocal consideration whatsoever from the grantee. C. Civ. arts. 572, 689 (Russ.). To a U.S. lawyer, the thought that a donation is treated as a contract may be puzzling.

285. C. Civ. art. 423 (Russ.). An example of an onerous contract is a sales contract where the seller promises to transfer goods and the buyer promises to pay. C. Civ. art. 454 (Russ.); EGOROV TEXTBOOK 1, *supra* note 83, at 509.

286. C. Civ. art. 423 (Russ.); see also EGOROV TEXTBOOK 1, *supra* note 83, at 509.

287. M.I. BRAGINSKII & V.V. VITRIANSKII, DOGOVORNOE PRAVO, OBSHIE POLOZHENIA [CONTRACT LAW, GENERAL PROVISIONS] 317-18 (Statut 1st 1997) [hereinafter BRAGINSKII CONTRACT 1997].

288. See EGOROV TEXTBOOK 1, *supra* note 83, at 509; see also SUKHANOV 1, *supra* note 23, at 336. In fact, according to Sukhanov, consideration can only take the form of a transfer of money or property, delivery of services, or some other similar granting of a legal benefit. *Id.* at 336.

289. See *id.* For example, a leading Russian contract law book defines an onerous contract as one "by which the material benefit offered by one party induces the material benefit by the other party . . . In a gratuitous contract, material benefit is conferred only by one party, without receiving any reciprocal material benefit from the other party." EGOROV TEXTBOOK 1, *supra* note 83, at 509 (author's translation.)

290. BRAGINSKII CONTRACT 1997, *supra* note 287, at 317-18. For a definition of an aleatory contract see LA. CIV. CODE ANN. art. 1912 (West 1987). An example is a government operated lottery, raffle or gambling contract. *Id.* See generally C. Civ. arts. 1062, 1063 (Russ.) (covering statutes regulating games, wagers, lotteries).

291. BRAGINSKII CONTRACT 1997, *supra* note 287, at 317. A mortgage contract that depends upon and services a loan agreement between the mortgagor and the mortgagee is an accessory contract. See *id.*; C. Civ. art. 334 (Russ.). For a definition of a principal, or accessory, contract see LA. CIV. CODE ANN. art. 1913 (West 1987).

Contracts that are void (*nichtozhnaia*) or voidable (*osporimaia*) constitute another category of contracts.²⁹² A contract is deemed void if it is invalid at its inception (*ab initio*), meaning it does not create any obligations between the parties except for the obligations resulting from its invalidity.²⁹³ By contrast, a voidable contract is presumed valid until an interested party challenges and causes its validity to be overturned by a court decision.²⁹⁴ A validable contract exists between the spectrum of void and voidable contracts. A validable contract is presumed to be invalid until challenged and rendered valid by a court.²⁹⁵

Another contract category is unilateral contracts.²⁹⁶ In a unilateral contract, one party, the creditor, has rights and the other party, the debtor, has duties.²⁹⁷ A unilateral contract (*odnostoronnii dogovor*) is distinguishable from a unilateral transaction (*odnostoronnaia sdelka*).²⁹⁸ In a unilateral transaction only one party's expression of will is sufficient to create an obligation for such party in favor of the party to whom such an expression is addressed.²⁹⁹ By contrast, in a bilateral contract,³⁰⁰ each party is both a creditor and a debtor.³⁰¹ A bilateral contract embodies mutuality of rights and responsibilities.³⁰² A bilateral contract in which the parties' rights and duties are proportional (i.e., economically equivalent), is called a synallagmatic contract.³⁰³ A bilateral transaction, as opposed to a bilateral contract, requires the expression of the will of two or more

292. C. CIV. art. 166 (Russ.); OSAKWE, *supra* note 20, at 163.

293. C. CIV. arts. 166-67 (Russ.). Examples of void contracts include those failing to conform to the requirements of the law, those contrary to the legal order and morality, and sham and feigned contracts. C. CIV. arts. 168-70 (Russ.).

294. See C. CIV. art. 166 (Russ.). See C. CIV. arts. 173-79 (Russ.) for examples of voidable contracts.

295. See OSAKWE, *supra* note 20, at 163. A mixed contract may be defined as a validable contract. *Id.*

296. BARRY NICHOLAS, AN INTRODUCTION TO ROMAN LAW 162 (H.L.A. Hart ed., Oxford Univ. Press 1979).

297. EGOROV TEXTBOOK 1, *supra* note 83, at 508; see C. CIV. art. 154 (Russ.).

298. EGOROV TEXTBOOK 1, *supra* note 83, at 509.

299. *Id.* Examples include a will, a public promise of reward or a public bid. C. CIV. arts. 1055, 1057 (Russ.); see also SUKHANOV 1, *supra* note 23, at 334.

300. Use of the term bilateral is also meant to convey the concept of multilateral contracts or transactions (i.e., involving the participation of more than two persons).

301. NICHOLAS, *supra* note 296, at 162.

302. SUKHANOV 1, *supra* note 23, at 335.

303. LA. CIV. CODE ANN. art. 1908 (West 1987).

parties.³⁰⁴ By definition, a contract is a bilateral transaction;³⁰⁵ thereby indicating a unilateral transaction is not a contract.³⁰⁶ Depending on the number of parties, all contracts are either bilateral or multilateral.³⁰⁷

Another contract classification distinguishes nominate and innominate contracts.³⁰⁸ Part Two of the Code outlines twenty-six nominate contracts.³⁰⁹ In contrast, innominate contracts are not specially designated under the Code.

Contracts are also categorized as oral or written.³¹⁰ An oral contract is not committed to writing.³¹¹ A written contract is either notarized or does not require notary certification,³¹² and can be embodied in one consolidated document or in a series of written exchanges.³¹³ These exchanges can occur via postal mail, electronic mail, telegram, fax or any other method that makes it possible to determine the originating and receiving parties to the communication.³¹⁴

Contracts are also characterized as being in favor of a third party or the contracting parties.³¹⁵ When a third party beneficiary expresses an interest in exercising his rights, the contracting parties cannot unilaterally terminate the contract.³¹⁶ By contrast, a contract in favor of the contracting parties creates rights in favor of the parties, themselves.³¹⁷

Another contract category separates voluntary from compulsory contracts.³¹⁸ The parties to a voluntary contract are free to choose their obligations and determine any special conditions governing their performance.³¹⁹ By contrast, a unilaterally compulsory contract obligates one of the contracting

304. SUKHANOV 1, *supra* note 23, at 334-35.

305. C. CIV. art. 154 (Russ.).

306. *See id.*

307. *Id.*

308. BRAGINSKII CONTRACT 1997, *supra* note 287, at 323.

309. *See generally* C. CIV. arts. 454-1109 (Russ.).

310. OSAKWE, *supra* note 20, at 163; C. CIV. art. 158 (Russ.).

311. C. CIV. art. 159 (Russ.). A contract is also considered oral where the will of one or both parties is expressed by conduct. C. CIV. art. 158 (Russ.).

312. C. CIV. art. 161 (Russ.).

313. *See* GUEV COMM. ONE, *supra* note 8, at 300.

314. *Id.*

315. EGOROV TEXTBOOK 1, *supra* note 83, at 506-08.

316. *Id.* at 506.

317. *Id.*

318. *Id.* at 509-12.

319. *Id.* at 509-11.

parties to form a contract with the other interested party.³²⁰ The involuntary nature typically relates to the choice of a contracting party,³²¹ whereby, in some cases, some of the contract terms may be set by law in the so-called “model conditions” of contract.³²² In a bilaterally obligatory contract, however, the parties, typically due to a prior voluntary duty, are obligated to form a contract.³²³

Contracts are further classified as either express or implied.³²⁴ When the offer and acceptance are clearly articulated, the contract is express.³²⁵ This contrasts with a contract in which the offer and acceptance are implied, typically by conduct in the form of action or non-action.³²⁶

Additionally, contracts are classified as either conditional or unconditional. In an unconditional contract, duties and rights are not predicated on future events.³²⁷ In a conditional contract, however, the exercise of rights and performance of obligations is predicated upon the happening of certain or uncertain events.³²⁸ Conditional contracts are divided into two groups: (1) one where the conditions are suspensive, i.e., the performance of duties and the exercise of rights begin when the contract is formed, and are terminated when the stipulated events occur; and (2) one where the conditions are resolutive or dissolving, i.e., the exercise of rights and performance of duties do not commence until the events stipulated in the contract occur.³²⁹

Furthermore, contracts can either be divisible or indivisible and mixed or unitive.³³⁰ A divisible contract contains several obligations segregated into groups where the performance of one

320. *Id.* at 509.

321. *Id.* at 509-511. Examples of unilaterally compulsory contracts include public contracts and contracts with the winner of a public bid. *Id.*; C. CIV. arts. 426, 1057 (Russ.). In both examples, the commercial organization and the organizer of a public bid are unilaterally obligated by law to conclude a contract with the other interested person, thereby denying them the freedom of deciding whether or not to contract with a particular person that expresses an interest in contracting with them. *Id.*

322. C. CIV. art. 427 (Russ.).

323. C. CIV. art. 429 (Russ.). An example is the signing of a principal contract within the time limit and on the terms stipulated in a preliminary contract. C. CIV. art. 429 (Russ.).

324. OSAKWE, *supra* note 20, at 164.

325. *Id.*

326. *Id.*

327. See SUKHANOV 1, *supra* note 23, at 338-41.

328. *Id.* at 338.

329. *Id.* at 339-40.

330. OSAKWE, *supra* note 20, at 164.

set of obligations does not depend on the performance of the other set of obligations.³³¹ If the several obligations cannot be segregated into autonomous groups, the contract is deemed indivisible.³³²

Depending on the formation method, a contract is either an adhesion contract or a jointly negotiated contract (*vzaimosoglasovannii*).³³³ In an adhesion contract, the terms are formulated by one of the parties in boilerplate terms and the other party has the option of accepting them.³³⁴ Depending on how many types of different obligations are bundled into one contract, a contract can be mixed, which includes two or more different obligations, or a unitype obligation.³³⁵

Another category distinguishes preliminary from principal contracts.³³⁶ A preliminary contract is one that precedes a principal contract.³³⁷ It spells out the terms of, and sets a time limit for, the conclusion of a principal contract.³³⁸ A preliminary contract obligates both parties to sign the principal contract.³³⁹ Once the principal contract is signed, it subsumes and extinguishes the preliminary contract.³⁴⁰ The signing of a principal contract is a form of obligatory contract, but the obligation is voluntarily assumed under the preliminary contract and the obligation is bilateral.³⁴¹ In signing the principal contract, the parties are free to depart from, or modify the terms in, the preliminary contract.³⁴²

Contracts can also be either consensual or real. A consensual contract is founded upon and completed by the mere agreement of the parties without any external formality or symbolic act to fix the

331. *Id.* An example of a divisible contract is a contract for the sale of goods that calls for the delivery of the goods to the buyer using the seller's mode of transportation. The contract may be divided into two autonomous sets of obligations: (1) the sale of goods; and (2) the delivery of goods. See C. CIV. art. 161 (Russ.). Within this arrangement, the delivery of goods may be terminated without affecting the sale of goods. See C. CIV. art. 161 (Russ.).

332. OSAKWE, *supra* note 20, at 164.

333. EGOROV TEXTBOOK 1, *supra* note 83, at 512.

334. *Id.*

335. OSAKWE, *supra* note 20, at 163.

336. See C. CIV. art. 429 (Russ.).

337. See *id.*

338. *Id.*

339. *Id.*

340. See EGOROV TEXTBOOK 1, *supra* note 83, at 505-06.

341. *Id.*

342. See *id.*

obligation.³⁴³ By contrast, a real contract must have more than mere consent.³⁴⁴ Unless otherwise provided by law, a contract is presumed consensual.

Contracts are also characterized as either *de jure* or *putative*.³⁴⁵ A *de jure* contract is one that meets all the legal formation requirements.³⁴⁶ By contrast, a *putative* or *alleged* contract (*nesostoiavshiisia* or *nezakliuchennyi dogovor*) is one that was formed in good faith, but for some reason, fails to satisfy all the legal formation requirements.³⁴⁷

Contracts can also be either *de jure* or *de facto*. While the distinction between a *de jure* and a *de facto* contract is not articulated in the Code itself, it is recognized in Russian case law.³⁴⁸ A *de facto* contract exists between the parties because it has been relied upon and executed to some extent, although it fails the legal requirement that it be in simple written form.³⁴⁹ Despite its lack of written form, a *de facto* contract is neither void nor voidable.³⁵⁰

343. BLACK'S LAW DICTIONARY 323 (6th ed. 1990).

344. *Id.* Examples of a real contract under Russian law are loan (Article 807), bailment (Articles 886, 888) and pledge (Article 358).

345. See SADIKOV COMM. ONE, *supra* note 74, at 355-56.

346. See *id.* For example, Article 162 requires a contract for the supply of energy between a consumer and an energy supply company be in writing, but a failure to put it in writing does not invalidate the contract. C. CIV. art. 162 (Russ.). For example, A (the energy supply company) supplies energy to B (the consumer) without a written contract. During a period of one month, B actually consumes the energy. When A demands payment, B demurs, claiming that there is no contract. In this hypothetical, there is a *de facto* contract between A and B.

347. *Id.* An example of a *putative* contract is a loan that requires that the loaned money be transferred to the borrower in order for the contract to be concluded. If all the requirements are fulfilled (form, agreement, capacity, consideration in the form of a promise to repay the loan), but money is not delivered to the borrower, the contract is *putative*. A borrower can institute a lawsuit to declare the contract *putative* if neither money or property was transferred; see C. CIV. art. 812 (Russ.). Because this is a real contract the law requires that it go into effect at the time money or property is transferred. C. CIV. art. 807 (Russ.). See also SADIKOV COMM. ONE, *supra* note 74, at 355-56. This missing link prevents the contract from becoming *de jure*. In this regard, the Code draws a distinction between a *putative* contract, a *de facto* contract, and a void contract. C. CIV. arts. 812, 162, 166 (Russ.).

348. C. CIV. ANN., *supra* note 55, at 426-27.

349. See C. CIV. art. 162 (Russ.).

350. See *id.* (stating the simple written form requirement). For example, all contracts between a legal person and a natural person must be in simple written form, unless the law requires otherwise. C. CIV. art. 161 (Russ.). Thus, an energy supply services contract between an energy supply company and a consumer must be in simple written form. See *id.* Failure to comply with the simple written form requirement does not invalidate such contract, but triggers the consequences set forth in article 162. C. CIV. art. 160 (Russ.). In a

Another classification characterizes all contracts as executed or executory.³⁵¹ An executed contract calls for simultaneous performance by both parties and does not require any further action.³⁵² By contrast, an executory contract defers performance to a later time as established by the terms of the contract.³⁵³

Contracts may also be classified as alternative or single.³⁵⁴ An alternative contract embodies two promises, but the debtor chooses only one, unless the choice is expressly granted to the creditor, who is then released from the other obligation.³⁵⁵ A single contract, on the other hand, embodies only one promise.³⁵⁶ The debtor may not force the creditor to accept partial performance of both or either promise.³⁵⁷

Finally, a contract may be either enforceable or unenforceable.³⁵⁸ Whereas the law provides a cause of action for breach of an enforceable contract, an unenforceable contract has no such remedy.³⁵⁹

With the exception of gratuitous and nominate contracts, which are unique to civil law systems, and certain types of unilaterally compulsory contracts, which are indigenous to Russian law, all the aforementioned classification criteria are recognized by contract laws in forty-nine U.S. states that follow the common law system.³⁶⁰ Five specific contract types deserve further attention in the next section.

1997 ruling, the Presidium of the Supreme Arbitration Court held that a *de facto* energy supply contract exists if the consumer consumes energy but refuses to sign a formal energy supply contract with the company. See C. CIV. ANN., *supra* note 55, at 426-27.

351. SUKHANOV 1, *supra* note 23, at 336-37.

352. *Id.*

353. *Id.*

354. See generally C. CIV. arts. 307, 320 (Russ.). This classification is not specifically denominated in the Code.

355. C. CIV. art. 320 (Russ.). A contract that gives the debtor a choice to either pay money or perform specific services is considered an alternative contract. *Id.*

356. C. CIV. art. 307 (Russ.). A single contract offers no alternative to the debtor. *Id.*

357. C. CIV. art. 311 (Russ.). For example, debtor may not pay half the money and perform half the services.

358. All valid contracts are enforceable unless the law renders them unenforceable. An example of an unenforceable contract is a gambling contract.

359. See *infra* for a discussion of unenforceable contracts.

360. The Louisiana Civil Code recognizes the concept of a gratuitous contract and the distinction between nominate and innominate contracts. LA. CIV. CODE ANN. art. 1914 (West 1987). Louisiana's approach to gratuitous and nominate contracts is modeled after the French Civil Code where one party confers upon the other a purely gratuitous advantage. CIV. CODE art. 1105 (Fr.). The classification of contracts into nominate and innominate contracts is recognized in article 1107 of the French Civil Code.

A. Public Contract: A Unilaterally Compulsory Contract

The Code provides an open-ended list of obligatory contracts, also known as public contracts.³⁶¹ Additionally, the Code denominates individual nominate contracts as public contracts.³⁶² Russian law views public contracts as a social institution and governs such contracts to make them more just.³⁶³ A public contract is formed when the obligated party must contract with another who expresses a mutual interest in entering the contract. A public contract aims to prevent discrimination in the marketplace³⁶⁴ by protecting consumers from potential discrimination by business establishments.³⁶⁵

A public contract denies the obligated party two traditional freedoms: the freedom to determine whether or not to conclude a contract with the other party, and the freedom to determine the contract terms.³⁶⁶ Under these restrictions, the public policy of contractual justice supersedes the principle of freedom of contract.

To qualify as a public contract, three requirements must be met.³⁶⁷ First, the obligated party must be a commercial organization.³⁶⁸ Second, the activities undertaken by the

361. C. CIV. art. 426 (Russ.); See also P. ATIYAH, *THE RISE AND FALL OF FREEDOM OF CONTRACT* (1979).

362. These include the following: retail sale, energy supply, ancillary contracts connected with energy supply, hire, consumer work, all Chapter 39 contracts of compensated services, bank deposit where the depositor is an individual, bank account, bailment at a pawnshop where bailor is an individual, bailment at a warehouse of common use, bailment at storage room of a transport organization and personal insurance. See C. CIV. arts. 492, 539, 548, 626, 730, 779-83, 834, 846, 908, 919, 923, 927 (Russ.).

363. See BRAGINSKII CONTRACT 1998, *supra* note 82.

364. See generally *id.*, at 197-208.

365. C. CIV. art. 426 (Russ.); See also BRAGINSKII CONTRACT 1998, *supra* note 82, at 201. Although the 1994 Russian Civil Code first introduced the concept of public contract into Russian civil law, many of the principles of public contract had long existed in Russian consumer protection law prior to 1994.

366. C. CIV. art. 426 (Russ.).

367. *Id.*

368. C. CIV. art. 50 (Russ.). Russian commentators are divided on the question of whether the obligation to conclude a public contract extends to sole proprietors. Sadikov holds that the public contract rules apply exclusively to commercial organizations. SADIKOV COMM. ONE, *supra* note 74, at 687. In contrast, Guev contends that a combined reading of articles 426 with 23-25 of the Code suggests that public contract rules cover both a sole proprietor that engages in commercial activities as well as commercial organizations. GUEV COMM. ONE, *supra* note 8, at 682. Professors Braginskii and Vitrianskii support Professor Guev's position. BRAGINSKII CONTRACT 1999, *supra* note 23, at 254. In the author's view, Guev, Braginskii and Vitrianskii espouse the letter and spirit of the Code and, therefore, the author believes that the public contract rules do apply to sole proprietors.

commercial organization must be of a public nature, i.e., activities open to any member of the public who expresses an interest in obtaining such services.³⁶⁹ Finally, the object of the contract must be either the sale of goods, the performance of work, or the provision of services.³⁷⁰

If a nominate contract falls within the definition of a public contract, the formation and the terms must meet the conditions imposed upon public contracts.³⁷¹ First, a commercial organization with the capacity to do so may not refuse to form a contract with a party who expresses a desire to form a contract.³⁷² Second, the price for the services or goods must be the same for all categories of persons using the services or purchasing the goods.³⁷³ Third, a commercial organization may not offer special privileges to one person in the process of forming a public contract.³⁷⁴ Fourth, a public contract must be formed under the procedures in the Code.³⁷⁵

The Code also enumerates remedies for the violation of a rule pertaining to public contracts.³⁷⁶ If a commercial organization unjustifiably refuses to conclude a public contract with an interested party, the latter may seek a court injunction to compel action.³⁷⁷ If a commercial organization discriminates in favor of one consumer in its price policy, an aggrieved party may compel the organization to give the same price as given to the favored customer.³⁷⁸ A party that suffers damages as a result of a commercial organization's violation of the public contract rules

369. C. Civ. art. 426 (Russ.).

370. *Id.* These fall within the general meaning of "public": retail trade and carriage by a common carrier, communications services, energy supply services, medical services, hotel services and others. *Id.*

371. *Id.*

372. *See id.* For example, if a commercial airline has seats available on an announced flight, it must sell tickets for that flight on a first-come-first-serve basis to those who express a desire to purchase those tickets. *Id.*

373. *See id.* If a hotel offers discounts to one particular customer, it must offer the same discounts to all other customers. A hotel, however, may offer special discounts to members of a group considered to be frequent customers as long as membership to that group is open to all persons who wish to join.

374. *See id.* For instance, if an announced flight is overbooked and an airline maintains a list of standby passengers who can board the flight in case a reservation is cancelled, the airline may not give preferential treatment to one passenger over all standby passengers.

375. *Id.*

376. C. Civ. arts. 426, 445 (Russ.).

377. C. Civ. art. 445 (Russ.).

378. *See id.*

may seek damages in a court action.³⁷⁹ An offending commercial organization may also be fined.³⁸⁰ In an action to compel an unwilling party to form a contract, courts have ruled that the commercial organization has the burden of showing the other party's incapacity to form the contract.³⁸¹ An aggrieved party may file a lawsuit involving a public contract dispute in court without the consent of the other party.³⁸² Several statutes carve out exceptions to the public contract rules.³⁸³

*B. Gambling Contract: An Unenforceable Contract*³⁸⁴

The Code approaches gambling in an ambiguous and contradictory manner. Although it contains an entire chapter entitled "Conduct of Games and Wagers"³⁸⁵—a fact which, in and

379. C. Civ. art. 345 (Russ.).

380. See BRAGINSKII COMM., *supra* note 81, at 554. In a 1997 Informational Letter, the Presidium of the Supreme Arbitration Court ruled on a problem that has become known in Russian contract law as the "reverse public contract." See C. CIV. ANN., *supra* note 55, at 426-27. In such a contract, commercial organizations seek to compel consumers into a public contract. *Id.* The ruling addressed whether a commercial organization can bring an action to compel a consumer to sign a public contract. *Id.* at 426. The issue arose when an energy company brought an action to formalize the consumer's actual consumption of energy. *Id.* The Court ruled that only the party that contracted with the commercial organization could institute an action to compel the organization's signature to a public contract. *Id.* Moreover, the Court concluded that a commercial organization might not compel a consumer to sign. *Id.* The consumer's consumption of energy supplied by the energy company may be construed, however, as an acceptance of the company's offer. C. CIV. art. 438 (Russ.). Accordingly, the Court construed the relationship between the energy supply company and the consumer as a *de facto* contractual relationship. C. CIV. ANN. *supra* note 55, 426-27.

In the same ruling, the Court treated a similar situation between a telecommunications company and a subscriber as a *de facto* contract for telecommunications services. See *id.* If a consumer receives telecommunications services, but refuses to sign a formal contract with the provider of such services, the relationship between the company and the consumer is one of a *de facto* contract. *Id.* The ruling's practical effect was to introduce into Russian law the notion of a *de facto* contract, a concept unknown in Russian statutory law. The 1994 Civil Code does not contain any provision governing *de facto* contracts.

381. BRAGINSKII COMM., *supra* note 81, at 554.

382. *Id.*; see generally C. CIV. art. 445 (Russ.).

383. See generally SUKHAREV, *supra* note 70, at 839 (defining a public contract). For example, families with many children (*mnogodetnye sem'i*) are entitled to not less than thirty percent reduction in charges for public utility services and World War II invalids are given preferential treatment for the installation of telephone lines in private homes. See *id.* Today, the average waiting time to have a telephone installed in a home is two to three years.

384. The contract of gambling is distinguished from a contract of lottery or raffle, which is enforceable if approved by the government. C. CIV. arts. 1062, 1063 (Russ.).

385. C. CIV. arts. 1062, 1063 (Russ.).

of itself, elevates gambling to the level of a nominate contract—it does not expressly recognize a gambling contract as a civil law contract.³⁸⁶ The Code further states that judicial protection does not extend to claims arising from the organization of, and participation in, gambling, unless such claims are brought by those individuals who participated under the influence of fraud, coercion, threat or a bad-faith agreement between their representatives and the organizers of the gambling.³⁸⁷ The Code's restrictive attitude toward gambling is further reflected in the fact that losses suffered in the course of gambling are classified as uninsurable interests.³⁸⁸ The Code, however, does not specifically list gambling as an anti-social activity.³⁸⁹

The puzzle that remains unresolved may be summarized as follows: if gambling is not a crime and is, in fact, condoned by the government,³⁹⁰ and if participation in gambling establishes a contractual relationship between the gambler and the organizers of the gambling, how can a gambling participant protect his claims arising from such a contract? One possible answer may be self-help.³⁹¹

C. Donative Contract: A Gratuitous Unilateral Contract

A donative contract is an agreement where the donor gratuitously transfers or promises the donee any object of value, and the donee in turn agrees to accept and receive the thing of

386. SADIKOV COMM. TWO, *supra* note 81, at 659. The contract of gambling is not designated as a civil law contract. See C. CIV. art. 1062 (Russ.). The exhaustive list of twenty-six nominate contracts in the Russian Civil Code includes the contract of gambling. The carefully crafted language of article 1062, however, intentionally leaves doubt as to the legal status of the arrangement between the gambler and the organizers of gambling. See SADIKOV COMM. TWO, *supra* note 81, at 659.

387. C. CIV. art. 1062 (Russ.). Curiously, this Article recites the four legal facts recognized in article 129 of the Code as grounds for rescinding a civil law contract. C. CIV. art. 129 (Russ.). In so providing, Article 1062 tacitly recognizes participation in gambling as a civil law contract. See C. CIV. art. 1062 (Russ.).

388. C. CIV. art. 928 (Russ.).

389. See C. CRIM. art. 151 (Russ.) (1996). The four anti social activities listed under this provision are systematic use of alcohol, systematic use of mind-altering substances, prostitution, begging for money, and loitering. *Id.* Parenthetically, it should be noted that article 208-1 of the Soviet-era Russian Criminal Code of 1964, which classified gambling as a crime, was deleted from the new Russian Criminal Code of 1996. C. CRIM. arts. 208-1 (Russ.) (1964).

390. As is evidenced by the existence of several licensed casinos throughout Russia.

391. C. CIV arts. 12, 14 (Russ.). Self-help is recognized in Article 12 as a permissible form of civil remedy and is spelled out in Article 14. *Id.*

value.³⁹² Under Russian law, the object of donation can be one of three things: a tangible object, a property right (including right of claim), or release of the donee from a material obligation to the donor or to a third party.³⁹³ To validly form a donative contract, six elements must be satisfied. First, the parties must have a dispositive capacity to transact.³⁹⁴ The donor must have the dispositive capacity to fully understand the meaning of his action(s). The donee must have the dispositive capacity to receive and accept the thing of value being donated to him by the donor.³⁹⁵ Second, there must be mutuality of obligation between the donor and donee.³⁹⁶ Third, the donor must have the intent to donate the thing of value.³⁹⁷ Fourth, the thing of value must be transferred at the time the contract is made or, in the case of an executory donation, the donor must make a firm promise to transfer the thing of value to the donee in the future.³⁹⁸ In both cases, the transfer of the thing of value could be actual or symbolic.³⁹⁹ Fifth, the donee shall accept the gift either in the form of actual or symbolic acceptance.⁴⁰⁰ Sixth, the transaction must be gratuitous, in that the donee may not receive reciprocal consideration from the donor and the gift may not be predicated upon any reciprocal performance by the donee.⁴⁰¹ If the donee provides consideration in any form or amount, the contract becomes one of barter rather than of donation.⁴⁰²

D. Contract for Gratuitous Use of Property: A Gratuitous Bilateral Contract

In a contract for the gratuitous use of property, the grantor

392. C. Civ. art. 572 (Russ.).

393. *Id.*

394. *See* C. Civ. art. 21 (Russ.).

395. *Id.*; SADIKOV COMM. TWO, *supra* note 81, at 160.

396. C. Civ. art. 468 (Russ.). The donor obligates himself to make the gift and the donee reciprocally obligates himself to accept the gift. SADIKOV COMM. TWO, *supra* note 81, at 159.

397. SADIKOV COMM. TWO, *supra* note 81, at 159-61.

398. *Id.* at 160. For an executory donation, the Code imposes two additional requirements: 1) any requisite form for the conclusion of a contract of this type, depending on the object of the donation, shall be complied with; and 2) the donative intent of the donor must be explicit and specific. *Id.* at 159-61.

399. C. Civ. art. 574 (Russ.).

400. *See id.*

401. *See* SADIKOV COMM. TWO, *supra* note 81, at 159-61.

402. *Id.* at 161.

grants, or undertakes to grant, the temporary free use of property.⁴⁰³ The grantee undertakes to return the property to the grantor at the end of the specified term in its original condition, allowing room for ordinary or stipulated wear and tear.⁴⁰⁴ This definition makes the contract both gratuitous and bilateral.⁴⁰⁵ Under this contract, the grantor has both a duty to convey the property and a right to demand return of the property.⁴⁰⁶ The grantee also has both a right to demand that the grantor transfer the property and a duty to return the property at the end of the contract term.⁴⁰⁷ This contract is similar to a property lease contract, but differs in that a lease contract is not gratuitous.⁴⁰⁸

Seven requirements must be met for a contract to qualify as a contract for the gratuitous use of property.⁴⁰⁹ First, the parties to the contract must be dispositive in capacity.⁴¹⁰ The grantor must have the capacity to grant the property and comprehend the full meaning of such an action, and the grantee must have the capacity to accept the granted property.⁴¹¹ Second, the grantor must express a specific intent to grant the property to the grantee for the latter's free use.⁴¹² Third, there must be mutuality of obligation.⁴¹³ The grantee has the duty to return the property as well as the right to demand transfer of the property.⁴¹⁴ Fourth, the grantor must actually transfer the property or firmly promise to convey the property in the future.⁴¹⁵ In both cases, the transfer of the property could be actual or symbolic.⁴¹⁶ Fifth, the grantee must agree to accept the property for his free use.⁴¹⁷ Sixth, the grant of property from the grantor must be gratuitous.⁴¹⁸ Lastly, the object of transfer must be tangible.⁴¹⁹

403. C. CIV. art. 689 (Russ.).

404. *See id.*

405. *See id.*

406. GUEV COMM. TWO, *supra* note 81, at 292.

407. *See id.*

408. *Id.* at 291-92.

409. *See generally* C. CIV. art. 689 (Russ.).

410. *See generally* C. CIV. art. 21 (Russ.).

411. *Id.*

412. GUEV COMM. TWO, *supra* note 81, at 291-93.

413. *See id.*

414. *See id.*

415. *Id.* at 292.

416. *Id.* at 291-93.

417. *Id.*

418. *Id.* at 292.

419. *Id.*

E. Contract of Adhesion

In an adhesion contract, one party presents the conditions in the form of standard or fixed boilerplate terms and delivers the terms to the other party with the choice of “take it or leave it.”⁴²⁰ It is distinguishable from other contracts by the procedure that generates its terms, not by the nature of the obligation or the sphere of activities to which it applies.⁴²¹ To be an adhesion contract, two conditions must be met.⁴²² First, one party must predetermine and package the contract terms in the form of standard or boilerplate language.⁴²³ Second, the other party must accept the terms on an “all or nothing” basis.⁴²⁴ This format essentially denies the acceding party any opportunity to bargain for the terms.⁴²⁵ Adhesion contracts are commonly used in commercial practices, specifically in services related to banking, energy supply, air transportation, hotel and hospitality, and telecommunications.⁴²⁶

One of the legal implications of an adhesion contract is the acceding party has special rights and special grounds for seeking termination or modification of the contract.⁴²⁷ For example, if the acceding party feels that the terms grant him fewer rights than customarily granted or shield the other party from liability to an extent that exceeds other analogous contracts, that party has the right to demand either a modification or termination of the contract.⁴²⁸ The scope of the acceding party’s rights vary widely depending on the status of the party.⁴²⁹ As a rule, citizen consumers have more rights than commercial organizations or sole proprietors who seek to modify or terminate adhesion contracts.⁴³⁰

420. C. CIV. art. 428 (Russ.).

421. See generally GUEV COMM. ONE, *supra* note 8, at 687-89; SADIKOV COMM. ONE, *supra* note 74, at 690-93; EGOROV TEXTBOOK 1, *supra* note 83, at 512-13.

422. C. CIV. art. 428 (Russ.).

423. *Id.*

424. *Id.*

425. See GUEV COMM. ONE, *supra* note 8, at 687-89.

426. SADIKOV COMM. ONE, *supra* note 74, at 692.

427. C. CIV. art. 428 (Russ.).

428. *Id.*

429. See *id.*

430. See BRAGINSKII CONTRACT 1998, *supra* note 82, at 214.

IX. SUBSTITUTION OF PARTIES IN A CONTRACT: ASSIGNMENT OF RIGHTS AND DELEGATION OF DUTIES

A. Identification of the Issues

The Code regulates six situations in which the substitution of parties occurs in a contractual obligation.⁴³¹ These are: (1) assignment of rights (*tsessiia*);⁴³² (2) universal succession to the rights of a creditor;⁴³³ (3) subrogation of rights to an insurance company under an insurance contract or indemnity;⁴³⁴ (4) transfer of rights by the decision of a court when such transfer is permissible by law;⁴³⁵ (5) transfer of claims to a surety or to a third-party mortgagor who performed obligations of the debtor in a principal obligation;⁴³⁶ and (6) delegation of duties from one debtor to another.⁴³⁷ The first five situations involve the transfer of rights and the sixth deals with the transfer of duties.⁴³⁸ This analysis will examine only two of the six situations mentioned above, i.e., assignment of rights and delegation of duties.

B. Assignments of Rights (*Tsessiia*)

In an assignment of rights, the original obligation is not terminated and continues to exist despite the substitution of parties.⁴³⁹ This feature, and the fact that an assignment of rights does not require the consent of the other party, distinguishes assignment of rights from novation. Novation occurs when, either as a result of the change in the method of performance or change in the object of an obligation, an original obligation is extinguished and replaced with a new one, without any change of the parties to the original obligation.⁴⁴⁰ Three principal differences exist between an assignment of rights and novation: (1) where assignment of rights does not extinguish the existing obligation nor

431. C. Civ. arts. 382, 387, 391 (Russ.).

432. C. Civ. arts. 382-90 (Russ.).

433. C. Civ. art. 387 (Russ.).

434. *Id.*

435. *Id.*

436. *Id.*

437. C. Civ. art. 391 (Russ.).

438. C. Civ. arts. 382, 387, 391 (Russ.).

439. See C. Civ. arts. 382, 387 (Russ.). The exhaustive list of the ten grounds for the termination of a contract contained in Chapter 26 of the Civil Code does not include any of these five situations.

440. C. Civ. art. 414 (Russ.).

create a new one, novation extinguishes an existing obligation and substitutes a new one; (2) whereas assignment of rights substitutes a new obligee for the outgoing one, novation does not substitute any of the existing parties; and (3) assignment of rights, as a general rule, does not require the consent of the obligor (debtor) to take effect, but novation always requires the consent of both the obligee (creditor) and the obligor.⁴⁴¹

In addition, Russian law does not characterize an indemnification claim as a transfer of rights because it is an original claim not an assigned claim.⁴⁴² Furthermore, in an indemnification claim, the statute of limitations starts to run when the party seeking indemnification acquired the right to indemnification.⁴⁴³ By contrast, in an assignment of rights, the statute of limitations starts to run when the rights being assigned arose, which, in some cases, could precede the time the right was assigned.⁴⁴⁴

There are four categories for assignment of rights.⁴⁴⁵ These include: (1) rights that are assignable without the consent of the debtor; (2) rights that are, by their nature, unassignable even with the consent of the debtor; (3) rights that are by operation of law absolutely unassignable; and (4) rights that are unassignable without the prior consent of the debtor either by virtue of contract or by reason of the nature of the rights involved.⁴⁴⁶

An assignment is the transfer of an interest in a property right from one party, the assignor, to another, the assignee.⁴⁴⁷

441. This deduction is based on a close reading of articles 382 (tsessia), 450 (novation) and 414 (termination of an obligation by a substitution).

442. C. CIV. art. 382 (Russ.). Indemnification takes place when A satisfies the claims of B against C and in turn files an original claim against C for indemnity. Examples of indemnification claims under the Russian Civil Code may be found in articles 325, 365, 379 and 399. BRAGINSKII COMM., *supra* note 81, at 480.

443. BRAGINSKII COMM., *supra* note 81, at 480.

444. *Id.* For an in depth analysis of the current law and policy on substitution of parties under the Code see V.A. BELOV, SINGULAR LEGAL SUCCESSION IN AN OBLIGATION (2000).

445. C. CIV. arts. 382-90 (Russ.).

446. *Id.*

447. C. CIV. art. 382 (Russ.). See BRAGINSKII COMM., *supra* note 81, at 475-81. The modern Russian rule on assignment of rights follows the German Civil Code with a few minor refinements. ZWIEGERT & KOTZ, *supra* note 23, at 127-31. The German Civil Code does not require debtor consent or knowledge to complete an assignment of rights from an assignor to an assignee. *Id.* German rule contrasts sharply with the French rule where an assignment is complete after the debtor is informed by the assignor or an assignee. See *id.* at 131-35.

Generally, an assignment does not require the debtor's consent.⁴⁴⁸ Thus, unless law, contract or the nature of the right itself places the assignment into one of the latter three of the aforementioned categories, a creditor's right is presumed to be freely assignable.⁴⁴⁹ A contract, even without consideration, determines the relationship between assignor and assignee.⁴⁵⁰ If the contract is for consideration, Russian law does not require an exchange of equivalent economic value as long as an agreement on the terms is reached between the parties.⁴⁵¹

The Code contemplates four situations where a creditor's claim of assignment may be prohibited or conditionally restricted.⁴⁵² One situation involves *per se* or absolutely nontransferable (unassignable) rights. These include claims that are intimately linked with the individual personality of the creditor, such as alimony payment, personal injury tort claims and rights under a personal insurance policy.⁴⁵³ In these instances, the creditor must be a natural person, not a legal entity. Article 383 provides an illustrative, not exhaustive, list of nontransferable rights.⁴⁵⁴ Statutes and case law add their individually personalized rights.

Another situation in which claim of assignment may be restricted is where the creditor's personality holds significance to the debtor. In such cases, even if the contract does not so stipulate, transferring the creditor's rights to another person requires the debtor's consent. In this sense, the rights are deemed conditionally unassignable.⁴⁵⁵ A right deemed unassignable without the prior consent of the creditor by virtue of a contractual prohibition also qualifies as a conditionally unassignable right and is discussed as the fourth situation below.⁴⁵⁶

A third situation arises if law or other normative acts prohibit the assignment of rights.⁴⁵⁷ For example, Russian commentators

448. C. CIV. art. 382 (Russ.); *see also* BRAGINSKII COMM., *supra* note 81, at 475.

449. C. CIV. art. 382 (Russ.).

450. SADIKOV COMM. ONE, *supra* note 74, at 629.

451. C. CIV. art. 424 (Russ.).

452. C. CIV. arts. 382-88 (Russ.).

453. C. CIV. art. 383 (Russ.).

454. *Id.*

455. C. CIV. art. 388 (Russ.).

456. *See below* in this Section of the analysis for a detailed discussion of contractual stipulation disallowing assignment of rights.

457. C. CIV. art. 388 (Russ.).

interpret Chapter 24 of the Code as prohibiting any assignment of claims against a railroad company by a shipper or recipient of goods.⁴⁵⁸ Thus, to file claims against the railroad company, the shipper or recipient of goods must transfer his rights to a third party.⁴⁵⁹ The transfer must be a properly executed instrument of agency, or by power of attorney, and must authorize the third party to act on behalf of the shipper or recipient of goods.⁴⁶⁰ Such a performance, does not qualify as an assignment of right under Chapter 24 since the third party acts on behalf of the principal.⁴⁶¹

The fourth situation involves the creditor and the debtor disallowing any assignment of the creditor's claims to a third party.⁴⁶² The Code implies that the creditor agrees with the obligor not to assign any contractual rights to a third party without the obligor's prior consent. Because there is no change in the original obligation or in the method of its performance, Russian law does not regard the substitution of parties as novation.⁴⁶³

Under an assignment of claims, the new creditor must immediately notify the debtor in writing that he assumed the rights of the outgoing creditor under the original agreement.⁴⁶⁴ Otherwise, the new creditor runs the risk the debtor might perform the obligation to the outgoing creditor, which then concludes the obligation.⁴⁶⁵ Thus, if a debtor is unaware of the substitution of creditors, he can perform his obligation to the old creditor, which terminates the obligation between the outgoing creditor and the debtor. In turn, the performance vitiates any claims the incoming creditor might have against the debtor.⁴⁶⁶ Under an assignment, an incoming creditor assumes the outgoing creditor's full scope of rights, including any ancillary rights

458. See C. CIV. ch. 24 (Russ.). Article 383 of the Code specifically lists one category of rights that are not transferable. But commentators read Article 383 expansively to include preclusion of assignment of rights under other federal statutes, e.g., the Railway Code, the Air Code, and the Internal Waterway Code. See SADIKOV COMM. ONE, *supra* note 74, at 631; BRAGINSKII COMM., *supra* note 81, at 477.

459. BRAGINSKII COMM., *supra* note 81, at 477.

460. *Id.*

461. See SADIKOV COMM. ONE, *supra* note 74, at 631; see also BRAGINSKII COMM., *supra* note 81, at 477.

462. C. CIV. art. 382 (Russ.).

463. C. CIV. art. 414 (Russ.).

464. C. CIV. art. 385 (Russ.).

465. C. CIV. art. 382 (Russ.).

466. *Id.*

securing the principal obligation.⁴⁶⁷ Accordingly, the outgoing creditor turns over to the new creditor all documents and information related to the obligation.⁴⁶⁸ The debtor also has the right to assert any objections or defenses against the new creditor he would have against the outgoing creditor.⁴⁶⁹

In an important but questionable 1998 ruling, the Presidium of the Supreme Court of Arbitration of the Russian Federation held that the assignment of rights under Section 1, Chapter 24 of the Code requires all rights of the outgoing creditor assigned in full, not in part, to the new incoming creditor.⁴⁷⁰ Additionally, the parties in the obligation must change.⁴⁷¹ Absent a complete change in parties, an assignment of rights does not exist.⁴⁷²

The case involved a contract between an energy supply company and its subscriber.⁴⁷³ Both parties agreed to extend the term of the contract.⁴⁷⁴ The energy supply company then assigned its rights to receive payment from the subscriber to a third party.⁴⁷⁵ The third party immediately filed suit to collect the assigned amount due. The trial court held for the plaintiff and directed the subscriber to pay the amount in question.⁴⁷⁶

On appeal, the Presidium of the Supreme Court of Arbitration reversed the lower court's decision, holding that the energy supply company could not assign only partial claims against the debtor to a third party.⁴⁷⁷ Additionally, the Court noted the contract between the energy company and the subscriber continued and thus, there was no substitution of the assignor from the obligation in question.⁴⁷⁸ Consequently, the Court held there was no assignment for claims for the period beyond the original

467. C. Civ. art. 384 (Russ.).

468. C. Civ. art. 385 (Russ.).

469. C. Civ. art. 386 (Russ.). If the debtor had any counterclaims against the original creditor, such counterclaims may be asserted against the incoming creditor. *Id.* The debtor could also assert against the new creditor that the original obligation is invalid or the statute of limitations on the original obligation tolled. C. Civ. art. 392 (Russ.).

470. BRAGINSKII COMM., *supra* note 81, at 475-76.

471. *Id.*

472. *Id.* at 476.

473. *Id.* at 475-76.

474. *Id.*

475. *Id.*

476. *Id.*

477. *Id.* at 476.

478. *Id.*

contract dates.⁴⁷⁹

Professor Vitrianskii and other authoritative Russian commentators believe the Court erred in its decision.⁴⁸⁰ In Vitrianskii's view, assignment of claims means assignment of rights and does not necessarily require the substitution of creditors in an ongoing obligation.⁴⁸¹ Vitrianskii also believes that under Chapter 24 a creditor may assign some and not all, of his rights to a third party.⁴⁸² A distinguishing feature of assignments under Russian law is the fact that a creditor may assign all or part of his rights under a contract to a third party. As later detailed, under the delegation of duties provision, a debtor has no such discretion; he must delegate all or none of his duties.⁴⁸³ With this in mind, it seems Vitrianskii's reading of Chapter 24's intent is correct, and the Court's decision in the above-referenced case was mistaken.

In an assignment, the outgoing creditor is liable to the new creditor in the event the claim that was assigned is subsequently determined to be invalid. The outgoing creditor will not, however, be liable for the debtor's subsequent nonperformance of the assigned obligation, unless he agreed in the contract of assignment to act as a surety for the debtor's nonperformance.⁴⁸⁴ The law governing the form for the assignment of rights is as follows: a right assigned under a transaction, which the law requires to be in a simple or notarized written form, must be performed in the same form that is required for the transaction under which the transferred right is assigned; a right assigned under a transaction that calls for state registration must also meet the form of state registration.⁴⁸⁵

Substitution of parties under an obligation also takes place under a universal succession to the rights of a creditor. Universal succession, for example, occurs in the case of a creditor's death.⁴⁸⁶ Here, all rights belonging to the deceased pass to his heirs.⁴⁸⁷ Universal succession also takes place when a legal entity

479. *Id.*

480. *Id.*

481. *Id.*

482. *Id.*

483. See my discussion of delegation of duties below in this analysis.

484. C. Civ. art. 390 (Russ.).

485. C. Civ. art. 389 (Russ.).

486. C. Civ. art. 700 (Russ.).

487. *Id.*

reorganizes in one of five forms enumerated in the Code.⁴⁸⁸ In such cases the rights and responsibilities of the liquidated legal entity pass to the legal successor by way of universal succession of the reorganized entity. If there are several legal successors to a reorganized legal entity, the transfer document or division balance sheet determines which entity will succeed to the obligations. If it is impossible to determine from the transfer document or division balance sheet, all the successors of the reorganized entity are solidarily liable for its obligations.

C. Delegation of Duties (Perekhod Dolga)⁴⁸⁹

Russian law defines delegation of duties as the substitution of a debtor in an obligation.⁴⁹⁰ The creditor takes into consideration the debtor's financial situation and other qualities, such as reliability and trustworthiness. For these reasons, rules governing the delegation of duties contrast with rules governing the assignment of rights, which assume the individual personalty of the creditor is not always of significant importance to the debtor.⁴⁹¹

Under Russian delegation of duties law, a creditor's delegable duties arise from a contractual obligation where delegation is not statutorily prohibited.⁴⁹² The rule requiring creditor's ad hoc prior consent before the debtor delegates a duty to another person is imperative even for the creditor, but his right to delegate his duties to another debtor is, in many cases, also regulated by law. Thus, in order to delegate his duties, he not only needs to obtain the creditor's consent, but must also in each instance delegate his duties only with the specific consent of the creditor even if the parties have contractually waived such a requirement.⁴⁹³ Any such waiver clause in a contract is deemed invalid.⁴⁹⁴ This contrasts with the rule governing the assignment of rights where a waiver of

488. C. Civ. arts. 57, 58 (Russ.).

489. C. Civ. art. 391 (Russ.).

490. *Id.*

491. See C. Civ. arts. 391, 392 (Russ.). The law governing delegation of duties are embodied in Articles 391 and 392. For the most part, this law corresponds with the law governing the assignment of rights in Articles 382-90 with one substantial difference: in all situations, the delegation of duties from one debtor to another requires the affirmative consent of the creditor. This is because the creditor exercises particular care in choosing his debtor, but not visa versa. See SADIKOV COMM. ONE, *supra* note 74, at 638.

492. See C. Civ. art. 391 (Russ.); SADIKOV COMM. ONE, *supra* note 74, at 638.

493. GUEV COMM. ONE, *supra* note 8, at 625.

494. *Id.*

consent clause in a contract is deemed valid.⁴⁹⁵ A creditor must give consent to permit a debtor to delegate his duty after the contract is signed and operative. The rules governing the form of delegation of duties are the same as those governing the form of assignment of rights.⁴⁹⁶

In a delegation of duties, only the debtor's duty transfers, not the debtor's liability for nonperformance.⁴⁹⁷ The original debtor remains liable to the creditor for his nonperformance or improper performance of the original obligation.⁴⁹⁸ As the name suggests, the delegation of duties is not the same thing as an assignment of right. In an assignment of rights, the assignor disappears entirely from the original contract and is replaced by the assignee.⁴⁹⁹ Similarly, in a delegation of duties, the original debtor transfers the performance of the duty to the incoming debtor, thereby releasing himself from further liability for the obligation.⁵⁰⁰

When an existing debtor delegates his duties under an existing contract to a new debtor, the debtor cannot delegate only a portion of his duties to a new debtor.⁵⁰¹ The rule here is all or nothing.⁵⁰² This distinguishes delegation of duties from the assignment of rights. The transfer of duties under a principal obligation constitutes grounds for the termination of accessory, secondary obligations, such as a suretyship⁵⁰³ and a third-party mortgage if the surety or third party mortgagor refuses to secure the obligation of the new debtor.⁵⁰⁴ In the event of reorganization of a legal entity, the members must immediately notify all the creditors in writing.⁵⁰⁵ A creditor has the right to terminate or demand premature performance of any obligations owed by the legal entity being reorganized, as well as the right to seek any resulting damages from the legal entity or its universal successors.⁵⁰⁶

495. *Id.*

496. C. CIV. art. 391 (Russ.).

497. BRAGINSKII COMM., *supra* note 81, at 481.

498. *Id.*

499. C. CIV. art. 390 (Russ.).

500. GUEV COMM. ONE, *supra* note 8, at 625.

501. *Id.*

502. *Id.*

503. C. CIV. art. 356 (Russ.).

504. C. CIV. art. 367 (Russ.). A mortgage in which the mortgagor is not the debtor in the original obligation. See also BRAGINSKII COMM. *supra* note 81, at 481.

505. C. CIV. art. 60 (Russ.); BRAGINSKII COMM., *supra* note 81, at 481.

506. *Id.*

X. DEFENSES: GROUNDS FOR VOIDING A CONTRACT

A. Identification of the Issues

A contract signed by both parties may be voided on several grounds.⁵⁰⁷ The Code defenses fall into two groups: defenses affecting assent and defenses based upon policy.⁵⁰⁸ Depending on the applicable defense, contracts fall into three groups: void, validable and voidable.⁵⁰⁹ A void contract is an absolute nullity.⁵¹⁰ This means that it is *void ab initio*, or totally devoid of legal force or effect and incapable of being made so, and does not create any obligations for the parties except those associated with its nullity.⁵¹¹ As a general rule, a successfully pleaded defense based upon policy renders the contract void (*void ab initio*).⁵¹² A voidable contract is presumed valid until overturned by a court decision.⁵¹³ If a voidable contract is subsequently voided by judgment of a court but the contract has been partially performed at the time of its voidance, the judgment of the court has a prospective, not retroactive, effect.⁵¹⁴

On the other hand, a validable contract is presumed invalid until adjudged valid.⁵¹⁵ A validable contract may, at the petition of an interested party, be adjudged valid.⁵¹⁶ A judgment, like the judgment to void a voidable contract that has been performed partially, also does not apply retroactively if the contract has been partially performed.⁵¹⁷ A validable contract can take several forms, depending on a reversal of the presumptions. The legal consequences of validating a validable contract are the same as voiding a voidable contract.⁵¹⁸

507. C. CIV. arts. 166-81 (Russ.).

508. See C. CIV. arts. 168-79 (Russ.).

509. See generally C. CIV. arts. 166-81 (Russ.).

510. C. CIV. art. 167 (Russ.).

511. *Id.*

512. C. CIV. art. 169 (Russ.).

513. C. CIV. art. 166 (Russ.).

514. C. CIV. art. 180 (Russ.).

515. BRAGINSKII COMM., *supra* note 81, at 284.

516. C. CIV. arts. 171, 172 (Russ.).

517. See C. CIV. art. 180 (Russ.).

518. See C. CIV. arts. 166, 167 (Russ.). The consequences of voiding a contract vary according to whether the contract is void or voidable. BRAGINSKII COMM., *supra* note 81, at 284-301. As a general rule, Russian law defenses affecting assent relate to voidable contracts. *Id.* The Code lists fifteen specific defenses: four based upon policy and eleven based on grounds affecting assent. C. CIV. arts. 168-79 (Russ.).

A petition to declare a contract void may be filed by a party to the contract or by an interested third party.⁵¹⁹ Also, a court can rule a contract void.⁵²⁰ By contrast, a petition to void a voidable contract or to validate a validable contract may be filed either by an interested party to the contract or by an interested third party named in the Code.⁵²¹ Whereas an action to void a voidable contract or to validate a validable contract is subject to the general rules of the statute of limitations, an action to declare a contract as void is not subject to the statute of limitations.⁵²² Under a voided contract, the parties must return to each other anything received from the other party.⁵²³ Bilateral restitution tries to restore the parties' original status prior to the conclusion of the contract.⁵²⁴

B. Defenses Based Upon Policy

If a contract fails to conform to mandatory requirements of law or other legal acts, such contract is void, unless a statute deems it voidable rather than void.⁵²⁵ Under this provision, the requirements of the law relate to the subject matter,⁵²⁶ form⁵²⁷ or status of the participants in a contract.⁵²⁸ The law also applies to the prerequisites and procedures for forming particular types of contracts.⁵²⁹

If a state enterprise, which is organized as a legal person, signs a contract that exceeds its authority or violates its charter, it is

519. C. CIV. art. 166 (Russ.).

520. *Id.*

521. *Id.*

522. C. CIV. art. 181 (Russ.); BRAGINSKII COMM., *supra* note 81, at 301, n. 409.

523. C. CIV. art. 167 (Russ.).

524. BRAGINSKII COMM., *supra* note 81, at 287.

525. C. CIV. art. 168 (Russ.).

526. C. CIV. art. 153 (Russ.). Denying a partner the right to withdraw from a partnership is contrary to the Code, which prohibits such a contract. *Id.*

527. C. CIV. art. 158 (Russ.). A mortgage contract must be in written form. C. CIV. art. 339 (Russ.).

528. C. CIV. arts. 17-47 (Russ.). Persons lacking dispositive capacity may not participate in a contract. C. CIV. art. 171 (Russ.).

529. C. CIV. art. 432 (Russ.). A contract signed by a party that does not possess the requisite license is void. C. CIV. art. 49 (Russ.). By the same token, a contract that violates banking regulations is void under article 836 of the Code. SADIKOV COMM. ONE, *supra* note 74, at 359. A carriage contract that fails to meet the requirements set by article 143 of the Railway Code or by article 126 of the Automobile Transportation Code is also void. *Id.* The sale of state property by a procedure that bypasses a public bid required by law is also void. *Id.* at 286.

void, not voidable.⁵³⁰ Since a state enterprise's authority is established by "law or other legal acts," a contract that violates the charter of a state enterprise falls under Article 168 not Article 173.⁵³¹ Article 173 deals with *ultra vires* contracts of a non-state legal person.⁵³² Under Article 168, a contract that fails to conform to the law is not always void, but in most cases the contract is void.⁵³³

A contract violating public legal order or public morality is deemed void.⁵³⁴ Illegality and immorality are two related but distinctly different grounds for voiding a contract.⁵³⁵ The Code rejects the German method of handling illegality or immorality of a contract under its general clauses, without making a particular reference to the object of the contract or its legal basis.⁵³⁶ Nevertheless, despite differences in methods, both the French and the German Civil Codes recognize two separate grounds for voiding a contract.⁵³⁷

By their nature, illegal contracts violate the law and subvert foundations of legal policy.⁵³⁸ Examples of such contracts include those aimed at tax avoidance,⁵³⁹ contracts violating currency regulations or an *ultra vires* contract where a state enterprise sells off state property granted to it for use in its operations.⁵⁴⁰

A contract violating public morality does not necessarily violate the law. Typically, such contracts fall within loopholes of the law, yet shock the public conscience.⁵⁴¹ Public conscience, as set forth in Article 169, is measured by public morality, not private morality or the morality of a segment of the population.⁵⁴² The basis for any moral judgment under Article 169 is the feeling of the Russian society as a whole.⁵⁴³ An example of such a contract is

530. C. CIV. art. 173 (Russ.).

531. See C. CIV. art. 168 (Russ.).

532. *Id.*

533. *Id.*

534. C. CIV. art. 169 (Russ.).

535. *Id.* The Code follows the French methodology of linking illegality and immorality of contract with the doctrine of *causa*. ZWIEGERT & KOTZ, *supra* note 23, at 63.

536. C. CIV. arts. 166-67 (Russ.).

537. ZWIEGERT & KOTZ, *supra* note 23, at 61-70.

538. C. CIV. art. 169 (Russ.).

539. BRAGINSKII COMM., *supra* note 81, at 289.

540. SADIKOV COMM. ONE, *supra* note 74, at 360.

541. *Id.*

542. *Id.*

543. SADIKOV COMM. ONE, *supra* note 74, at 362.

one for prostitution.⁵⁴⁴ Even though prostitution is not a crime under the 1996 Russian Criminal Code, a contract for prostitution would be deemed immoral under Article 169 of the Civil Code and is, therefore, void.

As a rule, violations of public legal order or public morality are intentional by one or both parties.⁵⁴⁵ If the violation is intentional by both parties and both parties have performed the contract, all items received by both parties are confiscated and turned in to the state coffers.⁵⁴⁶ The courts have interpreted *public morality* under Article 169 to include business custom.⁵⁴⁷ As such, a contract violating business ethics may be declared void.⁵⁴⁸

A mock contract is when parties enter a contract for the sake of appearance without intent to create legal consequences.⁵⁴⁹ This differs from a sham contract, defined as concealing another transaction.⁵⁵⁰ Both mock contracts and sham contracts are void.⁵⁵¹ In a feigned contract, however, the real contract that the parties seek to conceal may also be deemed voidable or valid.⁵⁵² The contract seeking to conceal another transaction is void.⁵⁵³ The concealed contract can be unmasked and declared voidable or valid.⁵⁵⁴

C. Defenses Affecting Assent

1. Capacity and Ultra Vires

There are several defenses that affect assent and make contracts voidable or invalid. Two contracts that fit the description of an invalid contract under the Code are contracts made by people lacking mental capacity and contracts by infants. A contract signed by a person lacking dispositive capacity by reason of mental incapacity is

544. It is this author's perception that the general Russian public opinion regards prostitution as immoral.

545. C. Civ. art. 169 (Russ.).

546. *Id.*

547. BRAGINSKII, *supra* note 81 at 284-301.

548. See C. Civ. art. 169 (Russ.).

549. C. Civ. art. 170 (Russ.).

550. *Id.*

551. *Id.*

552. *Id.*

553. *Id.*

554. *Id.*

invalid.⁵⁵⁵ Yet, the court can validate this contract at the petition of the guardian or tutor of the mentally ill person if such a contract favors the interest of the mentally ill person.⁵⁵⁶ A contract by an infant⁵⁵⁷ is also invalid, but may be validated at the petition of his parents or legal guardian.⁵⁵⁸ This general rule, however, does not apply to small consumer transactions that an infant, by law, may engage in.⁵⁵⁹ Russian case law draws a fine line between transactions of an infant between the ages of six to fourteen years and those of an infant below the age of six years.⁵⁶⁰ In all situations, contracts of an infant under the age of six years are void.⁵⁶¹

Furthermore, an *ultra vires* contract is one signed by a legal person outside the scope of its purpose as stated in its charter.⁵⁶² Such a contract is voidable by a court, at the petition of the legal person itself, by any one of its founding members, or by a state agency charged with overseeing the operations of such a legal person.⁵⁶³ This rule is not applicable to legal persons endowed with restrictive legal capacity, such as state enterprises.⁵⁶⁴

If an authorized agent signs a contract exceeding his scope of limited authority, such contract is voidable at the petition of an interested party.⁵⁶⁵ To void such a contract, the petitioner must show that the other party to the contract knew, or should have

555. C. CIV. art. 171 (Russ.).

556. *Id.*

557. C. CIV. art. 172 (Russ.).

558. C. CIV. arts. 28, 172 (Russ.).

559. C. CIV. art. 172 (Russ.).

560. C. CIV. art. 28 (Russ.).

561. C. CIV. art. 28 (Russ.); SADIKOV COMM. ONE, *supra* note 74, at 83.

562. C. CIV. art. 173 (Russ.).

563. *Id.*

564. C. CIV. arts. 49, 168 (Russ.). *Ultra vires* contracts by state enterprises are regulated under Article 168. C. CIV. art. 168 (Russ.). Article 173 is intended to apply only to non-state legal entities endowed with the so-called universal legal capacity. "Universal legal capacity" means legal capacity limited only by the stated purpose of the company as long as the purpose is lawful. It is general legal capacity, as opposed to restricted legal capacity in article 173. C. CIV. art. 49 (Russ.); see SADIKOV COMM. ONE, *supra* note 74, at 120. In practice, however, Article 173 is almost never applied to private commercial organizations with universal legal capacity that have allegedly exceeded their authority. SADIKOV COMM. ONE, *supra* note 74, at 366. Such organizations may carry out any activities not forbidden by law. C. CIV. art. 49 (Russ.); SADIKOV COMM. ONE, *supra* note 74, at 120, 366. Typically, Article 173 is used in situations where certain types of contracts require a state license. SADIKOV COMM. ONE, *supra* note 74, at 366. If a legal person concludes a contract without having the requisite license, the contract is voided. C. CIV. art. 173 (Russ.).

565. C. CIV. art. 174 (Russ.).

known, the agent's limited authority.⁵⁶⁶ For example, persons between the ages of fourteen to sixteen years have limited dispositive capacity.⁵⁶⁷ Such minors, without the consent of their parents or legal guardians, may engage only in the transactions listed in the Code.⁵⁶⁸ To enter into a contract outside the Code, a minor must obtain the consent of his parents or legal guardian.⁵⁶⁹ If a minor fails to obtain consent, the contract is voidable at the petition of his parents or legal guardian.⁵⁷⁰

A court can also declare that a person lacks dispositive capacity.⁵⁷¹ When this happens, the person cannot enter into a contract without the consent of his court-appointed tutor.⁵⁷² If he enters into a contract without permission, the tutor can petition the court to declare the contract void.⁵⁷³

Additionally, it is possible that people not lacking dispositive capacity are not able to control their actions, or to comprehend the meaning of their actions, when the contract is formed.⁵⁷⁴ In this case, a person, or any other interested third party, can file a lawsuit to void such a contract.⁵⁷⁵ If a court subsequently adjudges such person incompetent, a court, at the petition of his court-appointed tutor, may void the contract signed prior to the time he was declared incompetent.⁵⁷⁶ This is one situation in which the Code deems a contract voidable and permits parties to void such contracts based on a party's state of mind at the time the contract is signed.⁵⁷⁷

2. Mistake

Another defense to assent is mistake. Mistake vitiates consent to contract.⁵⁷⁸ As such, a contract entered into under the influence

566. *Id.*

567. C. Civ. art. 175 (Russ.).

568. C. Civ. arts. 175, 26 (Russ.).

569. C. Civ. art. 26 (Russ.).

570. C. Civ. art. 175 (Russ.).

571. C. Civ. arts. 29-30 (Russ.).

572. C. Civ. art. 29 (Russ.). See C. Civ. art. 31, 32 (Russ.) for a definition of "court-appointed tutor."

573. C. Civ. art. 176 (Russ.).

574. C. Civ. art. 177 (Russ.).

575. *Id.*

576. *Id.*

577. *Id.*

578. C. Civ. art. 178 (Russ.).

of a mistake is voidable.⁵⁷⁹ To invoke the rule in Article 178, however, the mistake must occur at the time the contract was signed and must be of a substantial character.⁵⁸⁰ The Code provides guidelines to determine what constitutes a substantial mistake, regardless of the reason.⁵⁸¹

Mistake under Article 178 is distinguished from fraud under Article 179.⁵⁸² Mistake is the innocent misunderstanding by one or both parties of the facts, law or consequences of the contract.⁵⁸³ On the other hand, fraud requires intentional conduct of one party aimed at misrepresenting the facts or consequences of the contract to the other party.⁵⁸⁴ While a mistake of the nature or identity of the object of the contract is substantial, a mistake of the motive of the contract is not.⁵⁸⁵ Generally, the right to petition to invalidate a contract signed under the influence of a mistake belongs to the party with the mistaken belief.⁵⁸⁶

3. Fraud, Coercion and Threat

Article 179 is an omnibus provision covering five different defenses: fraud, coercion, threat, bad-faith collusion between the agent of one party with the other party and unconscionability.⁵⁸⁷ In contrast to mistake, fraudulent misrepresentation of facts or consequences of a contract by one party grants the other party a right to petition to void the contract.⁵⁸⁸ Fraud relates to specific elements of the contract, as well as to factors outside the confines of the contract, such as motive.⁵⁸⁹

Fraud requires knowledge of the facts by one party, absence of knowledge of the facts by the other party and conduct including failure to disclose facts.⁵⁹⁰ Fraud takes the form of action or nonaction.⁵⁹¹ Thus, deliberate silence about a critical fact that would affect the decision of another party to participate in a

579. *Id.*

580. *Id.*

581. C. Civ. art. 179 (Russ.).

582. *Id.*

583. SADIKOV COMM. ONE, *supra* note 74, at 370-72.

584. *Id.* at 373.

585. C. Civ. art. 178 (Russ.).

586. *Id.*

587. C. Civ. art. 179 (Russ.).

588. *Id.*

589. SADIKOV COMM. ONE, *supra* note 74, at 373.

590. *Id.*

591. *Id.*

contract is fraudulent concealment of the facts.⁵⁹² What this rule demands is not merely honesty, but full candor.

Article 179 does not clarify whether fraudulent misrepresentation of the law by one party grants the other party the right to seek avoidance of the contract. The law presumes that all persons know the law, or have a constructive knowledge of it.⁵⁹³ As such, one party cannot plead fraudulent misrepresentation of the law by the other party.⁵⁹⁴ It is this author's belief that fraudulent misrepresentation of the law does not fall within the intended meaning of Article 179.

Another defense covered by Article 179 is coercion.⁵⁹⁵ Coercion can be physical or psychological.⁵⁹⁶ In many situations, coercion takes the form of a criminal act and is an action, rather than a non-action.⁵⁹⁷

Threat is a form of unlawful pressure on the will of the other party.⁵⁹⁸ Threat is similar to psychological coercion. Unlike physical coercion that involves action, however, a threat merely threatens to resort to action.⁵⁹⁹ Unlike psychological coercion that always involves an illegal action, a threat can be a form of legal or illegal action.⁶⁰⁰

There is no distinction between the fraud, coercion or threat carried out by a party to the contract, by a third person acting for a party to the contract, or by a third party interested in the formation of the contract.⁶⁰¹ In all three forms, the consent of the aggrieved party is vitiated.⁶⁰² A contract formed under the

592. SADIKOV COMM. ONE, *supra* note 74, at 373.

593. *Id.* at 372-74.

594. *Id.* at 371.

595. *Id.*

596. *Id.* at 373; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27.

597. *See* SADIKOV COMM. ONE, *supra* note 74, at 373; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27.

598. SADIKOV COMM. ONE, *supra* note 74, at 373; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27.

599. SADIKOV COMM. ONE, *supra* note 74, at 373; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27.

600. SADIKOV COMM. ONE, *supra* note 74, at 373; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27.

601. SADIKOV COMM. ONE, *supra* note 74, at 373; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27.

602. SADIKOV COMM. ONE, *supra* note 74, at 373; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27. The two grounds separately listed as coercion and threat under Russian law are subsumed by the concept of duress in U.S. law. ROHWER & SCHABER, *supra* note 6, at 203-208.

influence of bad-faith collusion is always formed on terms that are quite unfavorable to the aggrieved party.⁶⁰³ Such collusion is typically intentional, but not necessarily profitable, to the colluding agent of the aggrieved party.⁶⁰⁴

4. Unconscionability

The last ground for defense in Article 179 is unconscionability.⁶⁰⁵ Unconscionability is a novel concept to Russian civil law.⁶⁰⁶ To void a contract as unconscionable, the following five elements must be present: (1) the aggrieved party voluntarily concluded the contract; (2) the aggrieved party is aware the terms are to his disadvantage, but he accepted due to necessity and not because of mistake or fraud; (3) the terms of the contract are extremely favorable to the other party; (4) the aggrieved party formed the contract under the influence of harsh circumstances relating to either the object of the contract or to himself; and (5) the other party acted unconscionably by taking undue advantage of the helplessness of the aggrieved party.⁶⁰⁷

To qualify as unconscionable, it is not necessary that the wrongful conduct take an active form.⁶⁰⁸ The mere fact that a contract was concluded under the foregoing circumstances renders it *per se* unconscionable.⁶⁰⁹ For example, the sale of a television set worth \$400 to a refugee who willingly paid \$1,500 is unconscionable even if the refugee initiated the transaction. It is also possible that the unconscionable benefit from the contract flows to a third party who is not a party to the contract.⁶¹⁰ In such instances, the requirement is that a contracting party has an

603. SADIKOV COMM. ONE, *supra* note 74, at 372-74; *See also* GUEV COMM. ONE, *supra* note 8, at 325-27.

604. SADIKOV COMM. ONE, *supra* note 74, at 372-74; *See also* GUEV COMM. ONE, *supra* note 8, at 325-27.

605. SADIKOV COMM. ONE, *supra* note 74, at 374; *See also* GUEV COMM. ONE, *supra* note 8, at 325-27.

606. SADIKOV COMM. ONE, *supra* note 74, at 374; *See also* GUEV COMM. ONE, *supra* note 8, at 325-27.

607. SADIKOV COMM. ONE, *supra* note 74, at 374; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27.

608. SADIKOV COMM. ONE, *supra* note 74, at 374; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27.

609. SADIKOV COMM. ONE, *supra* note 74, at 374; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27.

610. SADIKOV COMM. ONE, *supra* note 74, at 372-74; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27.

interest in such benefit from the contract flowing to the third party.⁶¹¹ If all five elements are present, the aggrieved party may move to void the contract. The unconscionability provision is intended to protect consumers, not commercial organizations or sole proprietors.⁶¹²

5. Statute of Limitations

The statute of limitations for filing a lawsuit to void a contract or to invoke the consequences of invalidity of a contract is in Article 181.⁶¹³ With regard to contracts that are *void ab initio*, a lawsuit to declare them void is not subject to statute of limitations.⁶¹⁴ A lawsuit to invoke the remedies of a void contract, however, must be filed within ten years from the time performance under the contract commenced.⁶¹⁵

With voidable contracts, a lawsuit to void or invoke the remedies may be filed within one year from the time the coercion or threat ceased, or one year from the time the aggrieved party knew, or should have known, of the grounds on which the contract may be voided.⁶¹⁶ The statute of limitations established under Article 181 differs from the general three-year statute of limitations under Article 196.⁶¹⁷ Article 181 qualifies as a special statute of limitations as defined in Article 197.⁶¹⁸

6. Remedies

Depending on which grounds a contract is voided and the conduct of the parties in the contract, the Code contemplates three sets of legal consequences referred to as bilateral restitution, unilateral restitution and no restitution.⁶¹⁹ Under a bilateral restitution, each party returns everything received under the contract to the other party.⁶²⁰ If a party is unable to return such

611. SADIKOV COMM. ONE, *supra* note 74, at 372-74; *see also* GUEV COMM. ONE, *supra* note 8, at 325-27.

612. C. CIV. art. 179 (Russ.). A commercial organization or a sole proprietor is not permitted to file a contract avoidance lawsuit. SADIKOV COMM. ONE, *supra* note 74, at 374.

613. C. CIV. art. 181 (Russ.).

614. *Id.*; *see* BRAGINSKII COMM., *supra* note 81, at 301, n. 409.

615. *Id.*

616. *Id.*

617. C. CIV. arts. 181, 196 (Russ.).

618. C. CIV. arts. 181, 197 (Russ.).

619. BRAGINSKII COMM., *supra* note 81, at 287.

620. C. CIV. art. 167 (Russ.).

things, the monetary value is paid to the party entitled to receive compensation.⁶²¹ Under unilateral restitution, one party returns to the other everything received under the contract and the other party transfers or pays the monetary value of the thing received to the coffers of the state.⁶²² Under a no restitution regime, if the contract has been performed, each party turns over to the state everything received under the contract or pays the monetary value to the state coffers.⁶²³ No restitution is equivalent to total confiscation in favor of the state, whereas unilateral restitution is partial confiscation in favor of the state.⁶²⁴

XI. DEVICES FOR SECURING THE PERFORMANCE OF A CONTRACT

A. General Principles

The Code contains several methods of compelling the performance of an obligation.⁶²⁵ One widely available method requires a party who fails to perform or improperly performs an obligation to pay damages.⁶²⁶ Two practical considerations, however, make it difficult for the aggrieved party to seek damages.⁶²⁷ First of all, it can be difficult to measure damages. Secondly, it can be even more difficult to prove a causal connection between damages and breach. For these reasons, the law establishes other supplementary methods of compelling performance.⁶²⁸

One method is generically known as security devices.⁶²⁹ To secure the performance of an obligation, the Code places at the creditor's disposal six enumerated devices—liquidated damages, mortgage, withholding, suretyship, bank guaranty and earnest

621. *Id.*

622. BRAGINSKII COMM., *supra* note 81, at 287.

623. *Id.*

624. *Id.*

625. C. CIV. art. 329 (Russ.). A summary restatement of modern Russian law governing the methods for securing the performance of a contract may be found in: BRAGINSKII COMM., *supra* note 81, at 402-74; SADIKOV COMM. ONE, *supra* note 74, at 577-628; GUEV COMM. ONE, *supra* note 8, at 538-615; OSAKWE, *supra* note 20, at 142-52.

626. C. CIV. art. 393 (Russ.).

627. For example, even if a creditor successfully litigates his claims against a defendant, enforcement of the judgment could be frustratingly slow and grossly inefficient. See SADIKOV COMM. ONE, *supra* note 74, at 576.

628. C. CIV. arts. 329-381 (Russ.).

629. C. CIV. art. 329 (Russ.).

money.⁶³⁰ Furthermore, Article 329 concludes its list of security devices with the open-ended phrase “and other means provided by a statute or contract.”⁶³¹ This suggests that there are statutory security devices other than the ones listed. It also means that parties in a contract are free to devise other forms of security devices to fit their needs as long as it is consistent with the law.⁶³²

One example of “other devices specified by law or by contract” under Article 329 is found in Article 824.⁶³³ Article 824 states that “[t]he monetary claim against the debtor may also be assigned by the client to the finance agent for the purpose of providing security for the performance of an obligation of the client to the finance agent.”⁶³⁴ Accord and satisfaction also qualifies.⁶³⁵

The creditor has discretion to select any security device. Typically, a selection depends on several factors including, but not limited to, the nature of the obligation to be secured and debtor conduct.⁶³⁶ Of the six security devices enumerated in Article 329, liquidated damages, mortgage, suretyship and earnest money were derived from Roman law.⁶³⁷ They were received into modern Russian law through continental European civil law by way of pre-revolutionary Russian law.⁶³⁸ Bank guaranty and withholding were first introduced in the 1994 Code and are new to Russian law.⁶³⁹ These six devices are deployed to secure performance of a principal obligation. They create a secondary or accessory legal relationship between the debtor and the principal.⁶⁴⁰

For example, to secure a monetary obligation, the creditor enters into a secondary mortgage relationship with the debtor. To

630. *Id.*

631. *Id.*

632. One example of a non-article 329 security device is found in Article 824, which permits the assignment to the creditor of the monetary claim against its debtor. SADIKOV COMM. ONE, *supra* note 74, at 576.

633. See C. CIV. arts. 329, 824 (Russ.) as discussed in BRAGINSKII CONTRACT 1998, *supra* note 82, at 385.

634. C. CIV. art. 824 (Russ.).

635. C. CIV. art. 409 (Russ.). Article 329 allows parties to a contract to select and stipulate any other devices they wish. C. CIV. art. 329 (Russ.). Article 396 allows the parties to stipulate liquidated damages in the form of accord and satisfaction. C. CIV. art. 396 (Russ.).

636. BRAGINSKII CONTRACT 1998, *supra* note 82, at 384.

637. *Id.* at 383-84.

638. *Id.*

639. Makovsky & Khokhlov, *supra* note 24, at 106.

640. SADIKOV COMM. ONE, *supra* note 74, at 577.

secure the performance of compensated services or a work contract, the creditor enters into an accessory liquidated damages relationship with the debtor. In both examples, there are two sets of legal relationships between the creditor and the debtor: the primary obligation and the security or secondary obligation.⁶⁴¹

Three consequences flow from the relationship between the primary and secondary obligations.⁶⁴² First, if the principal obligation is invalid, so is the secondary obligation.⁶⁴³ Conversely, the invalidity of the secondary obligation does not entail the invalidity of the primary obligation. Second, the fate of the secondary obligation follows the principal obligation.⁶⁴⁴ If the creditor assigns his rights under the primary obligation to a third party, the new creditor under the primary obligation acquires all rights of the outgoing creditor under the secondary obligation. Third, termination of the primary obligation entails termination of the secondary obligation.⁶⁴⁵

An important question is whether the Code permits cumulative use of two or more devices to secure the same obligation. Cumulative use of security devices to secure the same obligation is permissible if the devices combined are compatible.⁶⁴⁶ For example, suretyship and mortgage could be used to secure one obligation.⁶⁴⁷ The following section examines each of the six security devices enumerated in Article 329.

B. Nominate Security Devices

1. Liquidated Damages (Neustoika)

Liquidated damages is the most widely used security device listed in Article 329.⁶⁴⁸ Of the six security devices enumerated,

641. BRAGINSKII CONTRACT 1998, *supra* note 82, at 317.

642. *Id.* at 384-85.

643. *Id.*

644. *Id.*

645. *Id.*; C. CIV. art. 352 (Russ.).

646. See SADIKOV COMM. ONE, *supra* note 74, at p. 643.

647. C. CIV. arts. 329, 334, 361 (Russ.).

648. C. CIV. art. 329 (Russ.). Liquidated damages are referred to in three different sections of the Code. Article 12 designates liquidated damages as one of the eleven methods of civil law rights protection. C. CIV. art. 12 (Russ.). Article 329 lists liquidated damages as one of the six nominate devices for securing obligation performance. C. CIV. art. 329 (Russ.). Article 394 denominates liquidated damages as a form of civil liability for violation of an obligation. C. CIV. art. 394 (Russ.).

only liquidated damages⁶⁴⁹ and earnest money⁶⁵⁰ serve both as a security device and a form of civil liability.⁶⁵¹ Unlike damages (*ubytki*), liquidated damages (*neustoika*) do not require proof of damages subject to compensation.⁶⁵²

The Russian law device of liquidated damages traces its origins to the Roman law device known as *stipulatio poenae*.⁶⁵³ It stands in stark contrast to its U.S. analogue. The differences between the U.S. and Russian legal approaches to liquidated damages are staggering. Specifically, these differences are reflected in the purpose and form of liquidated damages.

Under U.S. law, liquidated damages is the sum of money a contract party agrees to pay if he breaks a promise.⁶⁵⁴ U.S. law distinguishes liquidated damages from penalties.⁶⁵⁵ Liquidated damages, calculated by a good faith effort to estimate actual damages likely to ensue from breach, are recoverable as agreed if the breach occurs.⁶⁵⁶ In other words, liquidated, or stipulated damages, are damages reasonably ascertainable at the time of breach. These damages are measured by fixed or established external standards, or by standards apparent from documents on which plaintiffs base their claim.⁶⁵⁷ By contrast, the purpose of a penalty under U.S. law is to secure performance.⁶⁵⁸ The essence of a penalty is a stipulation *in terrorem*, while the essence of liquidated damages is a genuine covenanted pre-estimate of such damages.⁶⁵⁹

Russian law combines the twin U.S. concepts of liquidated damages and penalties into one omnibus security device called

649. C. CIV. arts. 329, 330, 394 (Russ.); see also BRAGINSKII COMM., *supra* note 81, at 404.

650. C. CIV. arts. 329, 380, 381 (Russ.). Thus, while earnest money is a security device, under article 381, the breaching party forfeits the earnest money unless the parties agree otherwise. The forfeiture of the earnest money shall be the only form of liability for breach of the contract.

651. Thus, liquidated damages are both a security device in Articles 329 and 330, and a form of civil liability in Article 394. See C. CIV. arts. 329, 330, 394 (Russ.).

652. See SADIKOV COMM. ONE, *supra* note 74, at 577-78.

653. NOVITSKII & PERETERSKII, *supra* note 246, at 314-16.

654. BLACK'S LAW DICTIONARY 391 (1990).

655. See generally UCC Article 2-718.

656. ROHWER & SCHABER, *supra* note 6, at 273-75; JOHN D. CALAMARI & JOSEPH M. PERILLO, CONTRACTS 309-10 (2d ed. 1990; Black Letter Series, West Publishing Co.).

657. BLACK'S LAW DICTIONARY 391 (6th ed. 1990).

658. *Id.*

659. *Id.*

liquidated damages.⁶⁶⁰ The difference between the type of liquidated damages in U.S. and Russian law will be discussed later in this analysis. Against this backdrop, we now examine the governing Russian law of liquidated damages.

Under Russian law, liquidated damages are "a monetary sum determined by a statute or contract that a debtor must pay to the creditor in case of nonperformance or improper performance of an obligation," such as "in case of a delay in performance."⁶⁶¹ The following attributes characterize Russian liquidated damages: a prior determination by the parties of liability upon conclusion of the contract; the amount of liability in the event of breach; the possibility of collecting liquidated damages; and the possibility granted to the contracting parties to formulate, at their discretion, all critical aspects of the liquidated damages to be paid, including the payment amount, relationship between liquidated damages and actual damages and the method of computing the liquidated damages amount.⁶⁶² The method of computing the amount owed varies. It can be a percentage of the total contract amount or of the unperformed part of the contract.⁶⁶³ Alternatively, it could be a fixed amount for each day, week or month of the delayed performance, or a fixed lump sum for the breach.⁶⁶⁴ It can also be a fixed amount of money.⁶⁶⁵ Liquidated damages can be collected in full, along with the full damages collection.⁶⁶⁶

The Code distinguishes two forms of liquidated damages: fine (*shtraf*) and penalty (*pena*).⁶⁶⁷ A fine is imposed in the event of obligation nonperformance.⁶⁶⁸ A penalty is imposed in the event of improper performance, especially for delayed performance.⁶⁶⁹

660. ROHWER & SCHABER, *supra* note 6, at 273-75; CALAMARI & PERILLO, *supra* note 656, at 309-10.

661. C. CIV. art. 330 (Russ.).

662. C. CIV. art. 394 (Russ.).

663. SADIKOV COMM. ONE, *supra* note 74, at 577-80; *see also* GUEV COMM. ONE, *supra* note 8, at 540-44.

664. *Id.* SADIKOV COMM. ONE, *supra* note 74, at 577-80; *see also* GUEV COMM. ONE, *supra* note 8, at 540-44.

665. SADIKOV COMM. ONE, *supra* note 74, at 577-80; *see also* GUEV COMM. ONE, *supra* note 8, at 540-44.

666. SADIKOV COMM. ONE, *supra* note 74, at 577-80; *see also* GUEV COMM. ONE, *supra* note 8, at 540-44.

667. SADIKOV COMM. ONE, *supra* note 74, at 577-80; *see also* GUEV COMM. ONE, *supra* note 8, at 540-44.

668. C. CIV. art. 330 (Russ.).

669. *Id.*

As a rule, penalty is calculated as a percentage on the obligated amount not performed on time.⁶⁷⁰ It is a type of revolving liquidated damage imposed for each day of delayed performance.⁶⁷¹

The Code further distinguishes between statutory and contractual liquidated damages.⁶⁷² When parties fail to stipulate liquidated damages in their contract, the courts may impose statutory liquidated damages.⁶⁷³ Any contractual liquidated damages agreement must be in writing, irrespective of the principal obligation form.⁶⁷⁴ Failure to adhere to this requirement renders the contract invalid.⁶⁷⁵

Even further, the Code classifies liquidated damages into four types: discounted, alternative, exclusive and punitive.⁶⁷⁶ Discounted liquidated damages occur when liquidated damages paid exceed actual damages.⁶⁷⁷ Under these circumstances, the sum of the damages is then deducted from the stipulated liquidated damages amount.⁶⁷⁸ Alternative liquidated damages takes place when the contract posits only the payment of actual damages or liquidated damages as possible choices.⁶⁷⁹ Liquidated damages are termed exclusive if the contract dictates liquidated damages over damages.⁶⁸⁰ Under this selection, the debtor pays only the liquidated damages.⁶⁸¹ Liquidated damages are deemed punitive, or cumulative, if in addition to paying full damages, the debtor also pays full liquidated damages.⁶⁸²

Russian law takes the position that contractual liquidated damages, when invoked as a security device, perform two functions: deters breach through punishment and compensates the creditor for a breach. The deterrent and punitive aspects distinguish the Russian model of liquidated damages from the U.S.

670. *Id.*; see also GUEV COMM. ONE, *supra* note 8, at 540.

671. See C. CIV. art. 405 (Russ.).

672. C. CIV. arts. 330, 332 (Russ.).

673. C. CIV. art. 332 (Russ.).

674. C. CIV. art. 331 (Russ.).

675. *Id.*

676. See C. CIV. art. 394 (Russ.); SADIKOV COMM. ONE, *supra* note 74, at 643; GUEV COMM. ONE, *supra* note 8, at 630-32; BRAGINSKII COMM., *supra* note 81, at 403-06.

677. SADIKOV COMM. ONE, *supra* note 74, at 642-43.

678. *Id.* at 643.

679. *Id.*

680. *Id.*

681. See *id.* at 642.

682. *Id.* at 642-43.

approach.⁶⁸³ Under U.S. law, the security device of liquidated damages does not purport to deter or punish contract breach. Any such manifest purpose voids the liquidated damages clause in a contract.

U.S. liquidated damages law differs quite remarkably from Russian law. The Russian distinction between fine and penalty is not present in U.S. law. Also, the Russian distinction between contractual and statutory stipulated damages is unknown in U.S. law where liquidated or stipulated damages are only contractual. Finally, the Russian classification into discounted, alternative, exclusive and punitive liquidated damages is alien in U.S. law. U.S. law recognizes only exclusive liquidated damages. In other words, under U.S. law, a contractual stipulation of liquidated damages is equivalent to a party's decision to forego claims for any other types of damages in the event of a breach. Ironically, U.S. law, premised on the freedom of parties to agree to their own terms and stipulate remedies for breach, denies the parties freedom to agree on the terms of liquidated damages. Presumably, the underlying rationale for this U.S. legal policy is that parties to a contract are not free to decide the question of penalty for breach of their promises.⁶⁸⁴

On the contrary, Russian law grants the parties freedom to determine the form, type and amount of liquidated damages.⁶⁸⁵ Under Russian law, however, if the court feels the stipulated amount is clearly incommensurate with the consequences of the breach, the unbridled freedom of the parties to set the amount of liquidated damages may be interfered with.⁶⁸⁶

In deciding whether to reduce the amount of stipulated damages under Article 333, the Presidium of the Supreme Arbitration Court ruled that courts might take into consideration the amount of interest paid or payable to the plaintiff by the defaulting party.⁶⁸⁷ In this ruling, a bank filed suit against a defaulting commercial organization, seeking to collect the full loan amount, \$100 million rubles in interest and \$120 million rubles in

683. ROHWER & SCHABER, *supra* note 6, at 273-75; CALAMARI & PERILLO, *supra* note 656, at 309-10.

684. See generally SADIKOV COMM. ONE, *supra* note 74, at 642-43, GUEV COMM. ONE, *supra* note 8, at 630-32, BRAGINSKII COMM., *supra* note 81, at 403-06.

685. See C. CIV. art. 394 (Russ.).

686. C. CIV. art. 333 (Russ.).

687. C. CIV. ANN., *supra* note 55, at 322-23.

liquidated damages.⁶⁸⁸ The trial court ruled for the plaintiff, stating that the consequences for breach of the loan agreement are substantially mitigated by the interest payment the plaintiff sought.⁶⁸⁹ The trial court, however, reduced the amount of punitive damages by thirty percent.⁶⁹⁰ Plaintiff appealed, contending the trial court erred in deciding to reduce stipulated damages by taking into consideration the defendant's paid interest on the bank loan.⁶⁹¹ The Supreme Arbitration Court disagreed with the appellant and affirmed the lower court's judgment.⁶⁹² In its opinion, the Supreme Arbitration Court interpreted Article 333 as authorizing the courts to reduce the amount of liquidated damages.⁶⁹³

Courts have also reduced the amount of liquidated damages when the creditor did not receive property or money that he was entitled to under the contract and suffered damages, including lost profits.⁶⁹⁴ The interest that the defendant is ordered to pay compensates, to a given measure, the consequences of the breach.⁶⁹⁵ Accordingly, the court acted properly by taking into consideration that the defendant was ordered to pay interest.

Article 333 has been interpreted to assert that the arbitration court shall reduce the amount of stipulated damages on its own motion.⁶⁹⁶ Consequently, regardless of whether an interested party petitions for a reduction, a gross disproportion between stipulated damages and consequences for breach constitutes grounds for the reduction.⁶⁹⁷ The party petitioning for a reduction, however, bears the burden of producing evidence showing the gross disproportion.⁶⁹⁸ The fact that parties agreed to raise the amount of statutory liquidated damages does not *per se* constitute grounds for a judicial reduction of liquidated damages.⁶⁹⁹ Thus, the provision will not be triggered by the plaintiff's actions. The

688. *Id.*

689. *Id.*

690. *Id.*

691. *Id.*

692. *Id.*

693. *Id.*

694. *Id.*

695. *Id.*

696. TIKHOMIROV, *supra* note 69, at 30-31.

697. *Id.* at 30.

698. TIKHOMIROV, *supra* note 69, at 32-33.

699. *Id.* at 34-35.

provision will not come into effect even when a legal person is at fault by failing to perform a contractual obligation⁷⁰⁰.

In conclusion, Russian courts retain the power to reduce the amount of any type of liquidated damages stipulated by the parties in a contract.⁷⁰¹ Thus, the imposition of liquidated damages on the breaching party is not predicated upon debtor fault.⁷⁰² The harshness of this rule, however, is tempered by Article 401, which allows *force majeure*⁷⁰³ to be an absolute defense against liquidated damages payment.⁷⁰⁴ Thus, if the debtor shows that non-performance or improper obligation performance is attributable to forces beyond his control, he is not liable for liquidated damages.⁷⁰⁵

2. History and Explanation of Mortgage (*Zalog*)

a. Background

A technical discussion of Russian mortgage law⁷⁰⁶ requires a basic knowledge of key terms. First, the Russian word *zalog* is used generally to encompass three separate and distinct doctrines in U.S. law: mortgage,⁷⁰⁷ chattel mortgage⁷⁰⁸ and pledge.⁷⁰⁹ Since

700. *Id.* at 36. In such a case, although the legal person would be released from liability under provisions of Article 401 of the Code, non-negligent compliance with contractual obligations is not grounds for a reduction of liquidated damages under Article 333. *Id.*

701. C. CIV. art. 333 (Russ.).

702. *See* C. CIV. art. 401 (Russ.).

703. TIKHOMIROV, *supra* note 69, at 36.

704. *Id.*

705. *Id.*

706. *See generally* SADIKOV COMM. ONE, *supra* note 74, at 580-610; GUEV COMM. ONE, *supra* note 8, at 544-90; BRAGINSKII COMM., *supra* note 81, at 406-43; OSAKWE, *supra* note 20, at 143-436. Under the Russian Civil Code of 1994, modern Russian law of mortgage traces its roots to the Roman law security device where at different stages in the development of Roman law it was known as *fiducia*, *pignus*, *hypotheca* or *antichresis*. NOVITSKII & PERETERSKII, *supra* note 246, at 316-25.

707. STEVEN H. GIFIS, LAW DICTIONARY 308 (3d ed. 1996). For example, "conveyance of a conditional fee of a debtor to his creditor, intended as a security for the repayment of a loan, usually the purchase price or (a part thereof) of the [real] property so conveyed." *Id.*

708. *Id.* at 309. For example, "conveyance of an interest in personal property, generally made as security for the payment of money, such as the purchase price of the property, or for the performance of some other act." *Id.* Chattel mortgage allows the mortgagor to retain possession of the mortgaged thing. *Id.*

709. *Id.* at 357. For example, "a deposit of personal property as security for a debt" or "delivery of goods by a debtor to a creditor until the debt is repaid." *Id.* Chattel mortgage "is thus distinguished from a pledge, which establishes a bailment and which therefore

the Russian security device known as *zalog* is classified into four types, two of which include chattel mortgage and pledge, *zalog* translates as mortgage here.⁷¹⁰

Under Russian law, a mortgage is a commonly used method for securing obligation performance. Its appeal is, unlike liquidated damages, that the debtor's financial capacity does not affect the mortgage reliability.⁷¹¹ For certain types of actors in the new Russian marketplace, individual types of mortgages are more popular. Enterprises, for example, more commonly use chattel mortgages, the so-called mortgage of goods in the stream of commerce.⁷¹²

Mortgages were substantially revamped in 1992 when the law "On Mortgage," was adopted.⁷¹³ This new law laid the foundation for drafting the provisions of Articles 334-358.⁷¹⁴ It was virtually displaced, however, when the Code was eventually adopted.⁷¹⁵ "On Mortgage" continues to operate, albeit only to the extent that it does not conflict with the Code.⁷¹⁶

b. Mortgage Defined (*Zalog*)

Mortgage is a security device giving a creditor the right, in case of a debtor's non-performance, to obtain satisfaction from the mortgaged property's value.⁷¹⁷ This right supercedes those of other creditors, although it is subject to exceptions established by law.⁷¹⁸

In an important joint *Postanovlenie*,⁷¹⁹ the Supreme Arbitration Court and Supreme Court of the Russian Federation, declared that a mortgage agreement does not convey the right of ownership of the mortgaged thing from the mortgagor to the

establishes the pledgee as bailee and grants him possession of the personal property." *Id.* at 309.

710. C. CIV. art. 334 (Russ.).

711. SADIKOV COMM. ONE, *supra* note 74, at 580-81.

712. *Id.*

713. *Id.* at 581. See the full text of the 1992 statute in V.V. SMIRNOV & Z.P. LUKINA, KOMENTARIJ K FEDERALNOMY ZAKONY OB IPOTEKE (ZALOG NEDEVIZHIMOSTI) [COMMENTARY ON THE FEDERAL LAW ON MORTGAGE] (Fond "Pravovaia Kultura" 1999).

714. SADIKOV COMM. ONE, *supra* note 74, at 581.

715. *Id.*

716. *Id.*

717. C. CIV. art. 334 (Russ.).

718. *Id.*

719. C. CIV. ANN., *supra* note 55, at 335.

mortgagee.⁷²⁰ Thus, any agreement allowing the conveyance of the right of ownership is void unless such agreement constituted an "accord and satisfaction" (*otstupnoe*) or a "novation" (*novatsiia*).⁷²¹

The Code contemplates two methods of creating a mortgage: by operation of law (either statutory or legal mortgage) or by virtue of contract (contractual or conventional mortgage).⁷²² The rules of the Code governing contractual mortgage apply (*mutatis mutandis*)⁷²³ to statutory mortgage unless the applicable statute states otherwise.⁷²⁴

Against this backdrop, an explanation of the detailed rules of a contractual mortgage is necessary. In the joint *Postanovlenie*, the courts held that the value of a mortgage, the existence and terms of a primary obligation and the mortgagee who has possession of the object are significant conditions of a mortgage contract.⁷²⁵ Consequently, the contract is incomplete if the parties fail to reach an agreement or if the contract does not include a stipulation on any of the conditions.⁷²⁶ Ultimately, the object of a mortgage must be defined with specificity to avoid any confusion as to its identity.⁷²⁷

In the same ruling,⁷²⁸ the Court interpreted several other Code provisions dealing with mortgages. First, only a realty mortgage contract (*ipoteka*), in accordance with Articles 339 and 130, are subject to a state registration requirement.⁷²⁹ Second, included within the category of 'immovable things' are aircrafts, marine crafts, vessels of internal waterways and spacecrafts.⁷³⁰ Because an automobile is not listed under Article 130 or by any other law as "immovable property", it is not subject to the state

720. *Id.*

721. *Id.*

722. C. CIV. art. 334 (Russ.).

723. With due alteration of details; by simply substituting "statutory" for contractual in the appropriate places. See THE CONCISE OXFORD DICTIONARY OF CURRENT ENGLISH 781.

724. C. CIV. art. 334 (Russ.).

725. C. CIV. ANN., *supra* note 55, at 336.

726. *Id.*

727. *Id.*

728. The full text of the Informational Letter of January 15, 1998 may be found in TIKHOMIROV, *supra* note 69, at 64.

729. TIKHOMIROV, *supra* note 69, at 64.

730. C. CIV. art. 130 (Russ.).

registration requirement.⁷³¹ Third, the object of a mortgage cannot be “money held in a bank account”⁷³² because money, by its nature, is not sellable and does not qualify as a mortgagable object.⁷³³ Fourth, the mortgagee’s right arises when the mortgagor acquires the relevant object.⁷³⁴ Fifth, if a court levies execution on a mortgaged object, it must stipulate the starting price for the object when sold at auction.⁷³⁵

A mortgage creates two parallel sets of legal relationships. The first is between the creditor and the debtor, while the second is between the mortgagee and the mortgaged thing.⁷³⁶ A mortgage serves as a device for securing the performance of an obligation and for establishing a direct, legal connection between the mortgagee and the mortgaged thing.⁷³⁷ The legal connection between the mortgagee and the mortgaged thing, however, does not create a mortgagee’s right *in rem* in the mortgaged property.⁷³⁸

c. Four Types of Mortgages

The Code recognizes four types of mortgages: the mortgage of realty and other property similar in status to realty (*ipoteka*);⁷³⁹ the mortgage of personal property at a pawnshop (*zaklad*);⁷⁴⁰ the mortgage of property rights, including the mortgage of rights of claim and securities;⁷⁴¹ and the mortgage of goods in the stream of

731. TIKHOMIROV, *supra* note 69, at 64–65.

732. *Id.* at 67.

733. Here, the Court apparently is speaking of money as a medium of payment, not of money as a commodity, e.g., coin collection. Without any doubt, money in the form of coin collection - a commodity - is sellable and, as such, can be the object of mortgage.

734. See generally C. CIV. art. 340 (Russ.).

735. TIKHOMIROV, *supra* note 69, at 68. When determining the starting price, the court shall take into consideration the prevailing market price for the object. *Id.* at 69. Realistically, however, the court will only determine the starting price if the mortgagor and mortgagee fail to reach an agreement on what it should be. Ultimately, any claims by the mortgagee against a third party mortgagor will be limited to the amount received from the object’s sale. *Id.* at 70. Thus, if the proceeds from the sale of a mortgaged object are less than the amount of the debt secured by a third party mortgagor, the mortgagee has no right to collect the shortfall from other property belonging to the third party mortgagor.

736. BRAGINSKII COMM., *supra* note 81, at 407.

737. *Id.*

738. *Id.* at 407–08.

739. *Id.* at 435–43. It roughly corresponds to the contract of hypothecation in English. Hereinafter, it will be called *ipoteka* or hypothecation.

740. *Id.* *Zaklad* roughly corresponds to a pledge in English. Black’s Law Dictionary 1153 (6th ed. 1990). Hereinafter, it will be denominated as pledge.

741. See BRAGINSKII COMM., *supra* note 81, at 416–17.

commerce.⁷⁴²

There are several distinguishing features inherent in each type of mortgage. In hypothecation, the mortgaged object is typically realty such as land, minerals and buildings, but can be other property similar to realty like aircraft, spacecraft or sailing vessels.⁷⁴³ The mortgaged property remains in the possession and use of the mortgagor.⁷⁴⁴ To be valid, the hypothecation contract must be notarized and in writing, as it is subject to state registration.⁷⁴⁵ Failure to register the contract with the proper state authorities renders the hypothecation contract void.

A fundamental difference between hypothecation and other nominate mortgage forms is that levying execution on the object of hypothecation is permissible only through a court action, such as judicial foreclosure of the mortgage.⁷⁴⁶ The only exception to this rule is when grounds for levying have arisen, and the parties have reached an agreement to permit non-judicial levying.⁷⁴⁷ Either party, or any third party whose rights are adversely affected, however, may challenge such *ex post facto* agreements in court.⁷⁴⁸ In all other forms of mortgage, non-judicial executions can be levied solely on the basis of an execution order (*ispolnitel'naya nadpis*) issued by a notary public.⁷⁴⁹

In a pledge, the mortgaged property is exclusively personal property and the mortgaged property remains in the pledgee's possession.⁷⁵⁰ The contract does not need to be in writing since a receipt issued by the pledgee provides ample evidence of its existence.⁷⁵¹ In contrast to hypothecation, the contract of pledge is not subject to state registration.⁷⁵²

The subject of mortgaged property rights is the property right itself, such as the right of claim or any form of security.⁷⁵³ Either a mortgagee or a notary public can hold equivalent possession rights

742. *Id.* at 435.

743. *See* C. CIV. art. 130 (Russ.).

744. BRAGINSKII COMM., *supra* note 81, at 436.

745. *See id.* at 437.

746. *Id.*

747. *Id.*

748. BRAGINSKII COMM., *supra* note 81, at 435-43.

749. *Id.*

750. *Id.* This is a form of possessory mortgage. *Id.*

751. *Id.*

752. *Id.* at 416.

753. *Id.*

to the property right.⁷⁵⁴ Depending on the form of the property right at issue, the mortgage may or may not be subject to state registration.⁷⁵⁵

A chattel mortgage always involves the mortgagor's personal property.⁷⁵⁶ The chattel mortgage contract is typically in writing, though not necessarily subject to state registration, or certification by a notary.⁷⁵⁷

d. Two Schools of Thought

Commonwealth of Independent States' legal literature has two schools of thought on the nature of mortgage, the Russian school and the Kazakhstan school.⁷⁵⁸ The Russian school contends that mortgage is a part of the law of obligations, albeit with certain features of property rights law (*institut ob'lizatel'stvennogo prava s nekotorymi veshchno-pravovymi elementami*).⁷⁵⁹ The Kazakhstan school argues that mortgage is a part of property rights law, albeit with certain features of the law of obligations (*veshchno-pravovoi institut s nekotorymi elementami ob'iazatel'stvennogo prava*).⁷⁶⁰ Professor Vitrianskii vigorously defends the former position,⁷⁶¹ while Professors Suleimenov and Osipov endorse the latter.⁷⁶² Except for this doctrinal debate on the nature of mortgage, there is unanimity between Russian and Kazakhstan writers on all other aspects of this very important security device.⁷⁶³

In one notable argument, Russian law identifies the object of a mortgage as a thing (real or personal property) or a property right.⁷⁶⁴ Not all rights, however, may be mortgaged. The Code specifically precludes the mortgage of rights that are intimately connected with the individual.⁷⁶⁵ The non-mortgageable rights include alimony payment and compensation for personal injury.⁷⁶⁶

754. SADIKOV COMM. ONE, *supra* note 74, at 587.

755. BRAGINSKII COMM., *supra* note 81, at 435-43.

756. *Id.* This is a form of non-possessory mortgage. *Id.*

757. *Id.*

758. BRAGINSKII COMM., *supra* note 81, at 407-08, 436.

759. *Id.*

760. *Id.*

761. *See id.* at 406-07.

762. *See id.* at 407.

763. *See id.*

764. C. CIV. art. 336 (Russ.).

765. *Id.*

766. C. CIV. art. 383 (Russ.).

Only the owner of the right may mortgage the property right.⁷⁶⁷ Also, not all property may be mortgaged.⁷⁶⁸ The object of a mortgage is not limited, however, to previously owned possessions. It may include a thing or a right that the debtor may acquire in the future.⁷⁶⁹

Another debate raging between Russian and Kazakhstan civil law scholars is the distinguishing feature between hypothecation and all the other nominate forms of mortgage.⁷⁷⁰ The Russian school of thought argues correctly that the object of hypothecation is realty and other property considered realty as defined in the Code.⁷⁷¹ The Kazakhstan school, represented by Professors Suleimenov and Osipov, however, contends that the object of hypothecation is always left in the possession of the mortgagor.⁷⁷² In effect, this latter school of thought equates hypothecation with possessory mortgage.⁷⁷³ Under this theory, both chattel mortgage and property rights mortgage would fall under hypothecation.⁷⁷⁴

e. Effects of Mortgage

A third party that faces the threat of losing rights to a thing or of losing a mortgage by a debtor as a result of levying by a creditor

767. BRAGINSKII COMM., *supra* note 81, at 413.

768. *See id.* at 414.

769. C. CIV. art. 340 (Russ.). For example, A may borrow money from a bank in order to buy an apartment or a house, and mortgage such apartment or house as security for repaying the loan. Because A has yet to buy the house, and ownership of the house will pass to A only after he has bought it, A is mortgaging to the creditor-bank property he will acquire in the future. The Code, unlike the Civil Code of Kazakhstan (C. CIV. art. 301 (Rep. of Kazakhstan 1994)) does not specifically list money as a mortgageable thing. *See* C. CIV. art. 336 (Russ.). Since the law does not specifically preclude mortgaging money, Russian commentators accept money as an object of mortgage. *See* SADIKOV COMM. ONE, *supra* note 74, at 585. The Supreme Court of Arbitration (July 2, 1996 issued by the Presidium) however, countered that money cannot be an object of mortgage because it cannot be sold. *See id.* Professor Sadikov criticizes this Supreme Court decision because it uses the wrong test for determining whether money can be an object of mortgage. *See id.* Professor Sadikov believes the correct test would depend on whether the subject is removed from the stream of commerce or specifically deemed non-mortgageable by statute. *See id.* It is hard to completely agree with Professor Sadikov here. If money is considered a commodity, such as a coin collection, then maybe, Professor Sadikov notes, money can be the object of mortgage. Yet, money as a medium of payment cannot be perceived as the object of mortgage.

770. *See* BRAGINSKII COMM., *supra* note 81, at 436.

771. *See* C. CIV. art. 130 (Russ.); BRAGINSKII COMM. *supra* note 81, at 436.

772. BRAGINSKII COMM., *supra* note 81, at 436.

773. *See id.*

774. *See id.*

of execution, or mortgagee, on such property or right, may satisfy the claims under such levy without the debtor's consent.⁷⁷⁵ Subject to rules governing the assignment of rights,⁷⁷⁶ a mortgagee may assign his rights under a mortgage contract to a third party.⁷⁷⁷ If the object of a mortgage perishes, the mortgagor has the right to substitute another object of equal value.⁷⁷⁸ The Code regulates the manner in which claims of the mortgagee may be satisfied.⁷⁷⁹ The mortgagee is not permitted to acquire the right of ownership of the mortgaged property.⁷⁸⁰ Selling the mortgaged property at a public auction must satisfy the claims of the mortgagee.⁷⁸¹

In the event of liquidation of a debtor's property, including liquidation under bankruptcy proceedings, a mortgaged property is not excluded from the general inventory of the debtor's property that is subject to distribution to its creditors.⁷⁸² Rather, the secured claims of the creditor are satisfied in a preferential order of priority at the expense of any property of the debtor, including property not mortgaged to the creditor.⁷⁸³ If the object of a mortgage is an industrial or production plant, the rights of the creditor extend to all components of the plant, including claims and exclusive rights acquired during the time that the mortgage was in effect.⁷⁸⁴ Russian law permits mortgaging the same property to a second mortgagee (second mortgage) and a third mortgagee (third mortgage), as long as the first mortgage contract does not specifically preclude otherwise. Additionally, the prior mortgage must be fully disclosed to all subsequent mortgagees.⁷⁸⁵

A mortgagee with possessive rights of the mortgaged object can reclaim such property from the unlawful possession of any third party, including unlawful possession of the mortgagor.⁷⁸⁶ The

775. C. Civ. art. 313 (Russ.).

776. See C. Civ. arts. 382-90 (Russ.).

777. C. Civ. art. 313 (Russ.).

778. C. Civ. art. 345 (Russ.).

779. C. Civ. art. 350 (Russ.).

780. C. Civ. arts. 348-50 (Russ.); see also GUEV COMM. ONE, *supra* note 8, at 592. The only situation where the mortgagee is permitted to acquire ownership rights of the mortgaged property is set forth in article 350.

781. C. Civ. art. 350 (Russ.).

782. C. Civ. art. 64 (Russ.).

783. *Id.*

784. C. Civ. art. 340 (Russ.); see also GUEV COMM. ONE, *supra* note 8, at 555.

785. C. Civ. art. 342 (Russ.).

786. C. Civ. art. 347 (Russ.).

mortgagee must follow procedures set forth in the Code.⁷⁸⁷ The mortgagee has the right to demand that all unlawful violations of the right of possession by any third party cease, including those by the mortgagor.⁷⁸⁸ This remains true even if such violation does not entail depriving the mortgagor's possession of the mortgaged property.⁷⁸⁹

In principle, Russian law provides that only the property owner may mortgage such property.⁷⁹⁰ The Code, however, carves out exceptions to this general rule. For example, a legal entity that possesses and uses property belonging to another may mortgage such property with the owner's consent.⁷⁹¹ Similarly, a state enterprise possessing and using state property under the right of economic management may mortgage such property with the owner's consent.⁷⁹² Typically, mortgages secure the debtor's obligation to the creditor. The Code, however, permits an exception to this general rule. For example, a third party C may mortgage his property to secure the obligation of B (the debtor) to

787. C. CIV. arts. 301-05 (Russ.).

788. C. CIV. art. 347 (Russ.).

789. *Id.* The provisions on the law of mortgage are embodied in Section 3 (Pledge) of Chapter 23 (Security for Performance of Obligations) of Subdivision I (General Provisions on Obligations) of Division 3 (General Part of the Law of Obligations) of the Civil Code. See table of contents of Russian Civil Code. By contrast, Division 2 (The Right of Ownership and Other Rights in Things) does not contain even a single provision on the law of mortgage. See table of contents of Russian Civil Code. This deliberate choice of the location of the law of mortgage within the organizational structure of the Civil Code would tend to support the position of those commentators (i.e., the Russian school of thought) who argue that mortgage is an institution of the law of obligations, not of the law of property and other rights *in rem*. See discussions above.

790. C. CIV. art. 335 (Russ.).

791. *Id.* There are two sets of rules: one for mortgage of a thing, the other for the mortgage of a right. It is a four-part rule where: (1) an owner can mortgage his property without anyone's consent; (2) a holder of property under the right of economic management can mortgage the property without the consent of the property owner in instances stipulated in Art. 295 para. 2 of the Civil Code (C. CIV. art. 335 (Russ.)); (3) an enterprise that holds immovable property under a right of economic management cannot mortgage it without the owner's consent (C. CIV. art. 295 (Russ.)); and (4) a holder of a legal right to the property of another person cannot mortgage such right without the owner's consent or the consent of the person who has the right under the right of economic management if law or contract prohibits the disposition of such right without the consent of the persons named herein. (C. CIV. art. 335 (Russ.)).

792. C. CIV. art. 295 (Russ.). The Code, however, does not allow a budget-supported state enterprise possessing and using state property under the right of operational administration the right to mortgage such property, even with the owner's consent. C. CIV. arts. 296-97 (Russ.).

A (the creditor of B).⁷⁹³ Under this triangular arrangement, the relationship between C and B is governed by other principles of law.⁷⁹⁴ Since a state enterprise possesses only special powers,⁷⁹⁵ as opposed to the general powers of private legal entities,⁷⁹⁶ any contract it enters that violates the purpose or threatens the continued existence of the enterprise will be deemed void.⁷⁹⁷ When applied to the law of mortgage, this principle means that a state enterprise voids the contract when it mortgages its production funds or other assets without which it cannot fully perform its charter purpose.⁷⁹⁸

The Code contemplates special rules regarding the mortgage of land or a building.⁷⁹⁹ Under Russian law, ownership of land is separate and distinct from the ownership of a building located on such land. First, the mortgage of a building is permissible if the mortgage contract also grants the land upon which the building is situated.⁸⁰⁰ This rule prevents mortgaging a building that "hangs in the air." Absent a conveyance of the ancillary mortgage right or land lease, the mortgage contract is deemed invalid.⁸⁰¹

Second, if the subject of a mortgage concerns a parcel of land, the mortgage does not affect a building belonging to the mortgagor and located on such land unless the mortgage contract states otherwise.⁸⁰² In such a case, the mortgagee's right applies only to the mortgaged parcel of land.⁸⁰³ Consequently, a servitude

793. See C. CIV. art. 335 (Russ.).

794. The applicable rules in this case are discussed under Suretyship on page 88 *infra*.

795. GUEV COMM. ONE, *supra* note 8, at 96-97. As a rule, to which there are no exceptions, all state-owned legal persons have restricted legal capacity typically limited to the conduct of transactions in furtherance of the purpose stated in their charter. C. CIV. art. 49 (Russ.). All private enterprises operate under this general legal capacity in Article 49, whereas all non-private (i.e., state) enterprises operate under the restricted legal capacity in Article 168. Because the charter of state-owned enterprises is typically in the form of law or other normative act, contracts entered into by a state-owned enterprise in violation of restrictions imposed on it by its charter shall be deemed void under Article 168 of the Civil Code, rather than voidable under Article 173 of the Civil Code. GUEV COMM. ONE, *supra* note 8, at 315-16, 96-97.

796. GUEV COMM. ONE, *supra* note 8, at 96-97. The scope of the legal capacity of private legal persons is regulated under the Civil Code. C. CIV. art. 49 (Russ.).

797. C. CIV. art. 168 (Russ.).

798. BRAGINSKII COMM., *supra* note 81, at 412.

799. C. CIV. art. 340 (Russ.).

800. *Id.*

801. BRAGINSKII COMM., *supra* note 81, at 418.

802. C. CIV. art. 340 (Russ.).

803. *Id.*

encumbers the parcel of land.⁸⁰⁴

The third set of rules applies to buildings that are located on mortgaged parcels of land but do not belong to the owner of the land.⁸⁰⁵ In such an event, if the mortgagee levies execution on the mortgaged parcel of land and sells it at a public auction, the purchaser acquires the rights and duties of the mortgagor in regard to the building's owner.⁸⁰⁶

A contract concludes upon an agreement between the parties on all the essential terms of the contract.⁸⁰⁷ "Essential terms" means, among other things, any such conditions named in a statute or other legal acts.⁸⁰⁸ With regard to mortgage contracts, essential terms mean: the object of the mortgage and its valuation; the nature, amount and term of the primary obligation secured by the mortgage, as well as an indication of the party that will retain possession of the mortgaged object.⁸⁰⁹ For example, a mortgage contract that fails to identify the subject of the mortgage prevents any agreement between the parties on this significant condition of the contract. This particular rule applies to mortgaging future acquisitions.⁸¹⁰ In such a case, the mortgage contract must specifically define the subject's nature.⁸¹¹ A mortgage contract must be in written form, and is always subject to notarial certification and state registration.⁸¹² A contract is rendered void by a failure to comply with any of the three requirements.⁸¹³

Russian law carves out special situations permitting only a judicial levying of execution on an object of a mortgage: (1) when the signing of the mortgage contract itself requires the consent of a third party or a state agency⁸¹⁴; (2) when the object of the mortgage represents significant cultural, historical, artistic or other

804. *Id.*

805. BRAGINSKII COMM., *supra* note 81, at 418. The parcel of land on which execution was levied shall be encumbered by servitude. *Id.*

806. *Id.*

807. C. CIV. art. 432 (Russ.).

808. *Id.*

809. C. CIV. art. 339 (Russ.).

810. *See* BRAGINSKII COMM., *supra* note 81, at 418.

811. *Id.*

812. *Id.* at 423-24.

813. *Id.* at 423-24; C. CIV. art. 339 (Russ.).

814. For example, a state enterprise cannot mortgage state-owned realty transferred to its possession and use without the consent of the owner of such property, i.e., the state, but it may mortgage personal property without the consent of the state. C. CIV. art. 295 (Russ.).

similar value to society in general; and (3) when the mortgagee's right to sell the mortgaged property arises while the mortgagor is absent and whose whereabouts are impossible to determine.⁸¹⁵

The rule that the mortgagee's claim can be satisfied only at the expense of proceeds received from a sale of the mortgaged object at a public auction is subject to one exception.⁸¹⁶ After two abortive attempts to hold a public auction, the mortgagee may agree with the mortgagor to acquire the mortgaged property.⁸¹⁷ If the sale proceeds exceed the debt owed under the principal obligation, the mortgagor receives the difference.⁸¹⁸ If the proceeds are less than the owed amount, the creditor retains the right to collect the balance from any other property owned by the mortgagor.⁸¹⁹

There are three specific grounds upon which the mortgagee may demand premature performance of the principal obligation secured by a mortgage.⁸²⁰ In any of the three events, the mortgagee can demand premature performance by the mortgagor. If the mortgagor refuses, the mortgagee can levy execution on the object of the mortgage.⁸²¹

The Suleimenov - Osipov approach names two nominate forms of mortgage under the Code: hypothecation (*ipoteka*) or possessory mortgage, and pledge (*zaklad*) or non-possessory mortgage.⁸²² Russian law predominately views chattel mortgage and the mortgage of rights as different and distinct from hypothecation.⁸²³ Also, Russian law views the "object factor" as the core distinguishing feature of hypothecation, rather than the "possession" element.⁸²⁴

There are four grounds for terminating mortgages.⁸²⁵ A mortgage shall terminate if: (1) the principal obligation secured by the mortgage is terminated; (2) at the demand of the mortgagor,

815. C. Civ. art. 349 (Russ.).

816. C. Civ. art. 350 (Russ.).

817. *Id.* In such a case, the creditor's claims under the principal obligation is discounted from the sale price, and the sale price is less than ten percent below the starting asking price at the second abortive public auction. *Id.*

818. *Id.*

819. *Id.*

820. C. Civ. art. 351 (Russ.).

821. *Id.*

822. *See id.*

823. *See id.*

824. *See id.*

825. C. Civ. art. 352 (Russ.).

upon any of the grounds listed in Article 343; (3) in the event of loss of the mortgaged item or the mortgaged right and the refusal of the mortgagor to exercise his rights under Article 345⁸²⁶; and (4) in the event of selling the object of a mortgage at a public auction.⁸²⁷ This fourth ground includes situations where selling the mortgaged object is impossible after repeated attempts to hold a public auction.⁸²⁸

With regard to the mortgage of personal property at a pawnshop (pledge), the Code imposes four stringent requirements that are skewed in favor of the pledgor (the consumer).⁸²⁹ The first rule requires the pledgee (the pawnshop) to insure, at the expense of the pledgor, the pledged object at its full market price in favor of the pledgor.⁸³⁰ The second rule holds the pledgee to strict liability for the loss or damage of the pledged object.⁸³¹ This rule exempts the pledgee from liability for loss or damage of the pledged object only if he can show that the loss or damage is attributable to an insurmountable force.⁸³² The third rule states that the pawnshop's sale of the pledged object shall terminate the pledge and ipso facto terminate all claims by the pawnshop against the pledgor.⁸³³ This applies even when sale proceeds are insufficient to cover the amount owed under the principal obligation.⁸³⁴ The fourth rule states that if a contract of pledge limits or takes away any of the rights granted to a pledgor under the Code, such provisions shall be deemed void.⁸³⁵ To this list of pledgor's rights that are protected may be added a final rule that states that a pledgee has no right to use or dispose of a pledged thing in its possession.⁸³⁶

In contrast to the four rules stated above, the corresponding rules regarding other forms of mortgage are as follows. First, unless the mortgage contract provides otherwise, the mortgagee

826. For example, if the mortgagor refuses to exercise his right to substitute an item of equal value for the one that perished. See C. CIV. art. 345 (Russ.).

827. C. CIV. art. 352 (Russ.).

828. C. CIV. art. 350 (Russ.).

829. C. CIV. art. 358 (Russ.).

830. *Id.*

831. *Id.*

832. *Id.*

833. *Id.*

834. *Id.*

835. *Id.*

836. C. CIV. art. 358 (Russ.).

shall insure the mortgaged item in favor of the mortgagor and at the expense of the mortgagor.⁸³⁷ Second, since in most cases the mortgagor has possession, the mortgagee is not liable for the loss of the mortgaged item.⁸³⁸ Third, unless the mortgage contract stipulates otherwise, if the proceeds from the sale of a mortgaged item at a public auction are insufficient to cover the amount owed to the creditor under the principal obligation secured by the mortgage, the mortgagee shall retain the right to proceed against the debtor's other property in an effort to recover the amount owed.⁸³⁹ Fourth, it is at the discretion of the parties to a mortgage contract to agree on the terms of the transaction.⁸⁴⁰ In this regard, the Code contains only dispositive norms. The only imperative norm of the Code relates to a list of issues on which the contracting parties must reach agreement, the so-called essential terms of a mortgage.⁸⁴¹

The Code recognizes a statutory or legal mortgage as one that operates by law rather than by virtue of a contract.⁸⁴² One such example is where goods sold on credit are presumed mortgaged to the seller until the goods are fully paid for by the purchaser.⁸⁴³ This would be tantamount to a non-possessory mortgage. Also, as security for the performance of an obligation to pay rent, the recipient of the rent acquires the right of mortgage on the parcel of land or other realty transferred under the condition of payment of rent until full performance.⁸⁴⁴

3. Withholding (Uderzhanie Imushchestva Dolzhnika)

Russian civil law recognizes a novel security device known as "withholding."⁸⁴⁵ The withholding concept was not present in Roman law, the Russian Civil Codes of 1922 and 1964 or the 1991

837. C. CIV. art. 343 (Russ.).

838. C. CIV. art. 344 (Russ.).

839. C. CIV. art. 350 (Russ.).

840. The principle of freedom of contract that is enshrined in articles 1 and 421 of the Code applies equally to mortgage contracts. C. CIV. arts. 1, 421 (Russ.). That freedom is limited only by the provisions of article 421, 422 and 339. C. CIV. arts. 421, 422, 339 (Russ.).

841. C. CIV. art. 339 (Russ.).

842. C. CIV. art. 334 (Russ.).

843. C. CIV. art. 488; *see also* SADIKOV COMM. ONE, *supra* note 74, at 582.

844. C. CIV. art. 587 (Russ.).

845. C. CIV. arts. 359, 360 (Russ.); *see generally* BRAGINSKII COMM., *supra* note 81, at 443-48; SADIKOV COMM. ONE, *supra* note 74, at 610-13; GUEV COMM. ONE., *supra* note 8, at 590-92.

Fundamental Principles of Civil Legislation of the U.S.S.R. and the Union Republics.⁸⁴⁶ Withholding involves a creditor with possession of an item subject to transfer to a debtor or to a designated third party.⁸⁴⁷ The creditor has the right to withhold that item under limited circumstances.⁸⁴⁸ The item can be withheld in the absence of the debtor's timely payment for the item, or in compensation to the creditor for costs or other damages until the obligation is fully performed.⁸⁴⁹

Withholding may be used to secure obligations remotely connected with the withheld item if the parties to the obligation are merchants.⁸⁵⁰ The Code requires three conditions before applying this security device: (1) the withheld object should belong to the debtor and should have been transferred to him or to a designated third party; (2) the withheld object acts as security for performance of the obligation in connection with payment or damages and other associated costs; and (3) the debtor failed to fully perform the said obligation on time.⁸⁵¹ If the parties to the obligation are merchants, however, the second condition is waived.⁸⁵² The creditor's right to withhold an item does not depend on whether a contract stipulates such a right.⁸⁵³ Rather, the right flows from the law.⁸⁵⁴ The parties may stipulate, however, that the creditor may not withhold property that belongs to the debtor.⁸⁵⁵

A typical creditor is a bailee holding delivered merchandise for bailment by the bailor.⁸⁵⁶ In this situation, either the bailee or the bailor may withhold the debtor's property until the latter fully performs his obligations to the creditor.⁸⁵⁷ If the parties are commercial organizations or individual entrepreneurs, withholding can be used to secure an obligation unrelated to the withheld item.

846. See BRAGINSKII COMM., *supra* note 81, at 402.

847. C. CIV. art. 359 (Russ.).

848. *Id.*

849. *Id.*

850. *Id.*

851. *Id.*

852. GUEV COMM. ONE, *supra* note 8, at 591.

853. *Id.*

854. *Id.*

855. C. CIV. art. 359 (Russ.).

856. BRAGINSKII COMM., *supra* note 81, at 443-44. This is much like a transport organization entrusted with the transportation of goods or a construction company that has contracted to build a house. *Id.*

857. *Id.* at 443.

⁸⁵⁸ Even if rights to the withheld item pass to a third party after the item enters the creditor's possession, the latter does not lose the right to withhold.⁸⁵⁹ The creditor holds *in rem* rights to the item.

In the event the debtor fails to perform within a reasonable time, even after repeated demands by the creditor, the creditor has the right to levy execution on the item.⁸⁶⁰ With regard to certain nominate contracts, the Code specifically contemplates the right of withholding by one of the parties.⁸⁶¹ Withholding is available as a security device in some nominate contracts that do not specifically mention this device.⁸⁶² In summary, withholding is available to any creditor in any contract situation, unless the contract in question specifically precludes it as a security device.⁸⁶³

Since the law does not specify a limit on which objects can be withheld, anything that the stream of commerce law does not exclude can be withheld, including money.⁸⁶⁴ Thus, the Code recognizes a bank's right to deduct its due commission, as well as compensation for its expenses.⁸⁶⁵

Not all Russian commentators endorse this new security device.⁸⁶⁶ Some opponents view it as a form of an unlawful seizure of another person's property.⁸⁶⁷ In their view, the property withheld by the creditor belongs to the debtor and should be returned to him, regardless.⁸⁶⁸ Under this argument, the creditor should not take the law into his own hands. Rather, he should resort to the courts to collect any money owed to him by the

858. *Id.*

859. *Id.*

860. C. CIV. art. 360 (Russ.); *see also* C. CIV. art. 348 (Russ.).

861. BRAGINSKII COMM., *supra* note 81, at 444. For example, under Article 712, a construction company has the right to withhold the completed work product, equipment, building materials or other things belonging to the customer until the latter has fully performed its obligations to the construction company. C. CIV. art. 712 (Russ.). An agent acting in the capacity of a commercial representative has the right to withhold items that are subject to return to the principal, as security for the satisfaction of his claims. C. CIV. art. 972 (Russ.). In a commission agency, the agent has the right to withhold the amount of money due to him, from the funds transferred to him that are intended for the principal. C. CIV. art. 996 (Russ.).

862. BRAGINSKII COMM., *supra* note 81, at 444.

863. C. CIV. art. 359 (Russ.).

864. *See id.* The Russian notion of withholding is similar to the common law device known as distress, which in most U.S. jurisdictions has been superseded by statutory provisions for the enforcement of security interests. *See* U.C.C. §1-201(37) (2001).

865. C. CIV. art. 875 (Russ.).

866. BRAGINSKII COMM., *supra* note 81, at 445.

867. *Id.*

868. *Id.*

debtor.⁸⁶⁹ Professor A. A. Rubanov is an ardent proponent of this viewpoint, calling withholding a form of "legalized robbery."⁸⁷⁰

4. Suretyship (Poruchitelstvo)

Suretyship is one of the most ancient security devices recognized in European civil law.⁸⁷¹ Its roots trace to the security device of Roman law.⁸⁷² Since its Roman origins, the essence of suretyship has remained the same.⁸⁷³ A third party, a surety, bears responsibility for the debtor if the debtor fails to perform his obligations to the creditor.⁸⁷⁴ In Soviet practice, suretyship manifested itself in a variation called guaranty or *garantiia*.⁸⁷⁵ This was evident in relations among state enterprises, where a superior state organization served as a guaranty for the obligations of its subordinate organizations.⁸⁷⁶ In 1994, the Code modernized suretyship law.⁸⁷⁷

On its face, a suretyship is quite similar to a mortgage contract, where the mortgagor is someone other than the debtor, such as a third-party mortgage. The core difference between these two arrangements is that in the latter case, the third-party mortgagor puts up the mortgaged property as security for the performance of the obligation of the debtor.⁸⁷⁸ In the case of suretyship, the surety secures the performance of the debtor's obligation by his naked promise.⁸⁷⁹ Typically, however, a surety has deep pockets, which are relied upon by the creditor. The fact that these two devices can be combined to secure the same obligation suggests that they are quite compatible, and even complementary.⁸⁸⁰

Another important difference between suretyship and third party mortgage is that whereas a third-party mortgage

869. *Id.*

870. *See id.*

871. BRAGINSKII CONTRACT 1998, *supra* note 82, at 451.

872. NICHOLAS, *supra* note 296, at 149-51.

873. *See id.*

874. BRAGINSKII COMM., *supra* note 81, at 448. Suretyship was featured both in the 1922 and 1964 Russian Civil Codes, as well as in the FP Civil Law of 1991. *See id.* at 449.

875. *Id.*

876. *Id.*

877. *Id.* at 450.

878. C. CIV. art. 334 (Russ.).

879. C. CIV. art. 361 (Russ.).

880. ROHWER & SCHABER, *supra* note 6, at 273-275; CALAMARI & PERILLO, *supra* note 656, at 309-10.

arrangement is a tripartite contract requiring the participation of the creditor, mortgagor and debtor (principal), the surety is usually bound in a separate two-party undertaking with the creditor that the principal does not join.⁸⁸¹ A suretyship contract is also usually entered into before or after the contract between the principal and the creditor, and is often founded on a separate consideration from that supporting the contract of the principal with the creditor.⁸⁸²

U.S. law delineates a contract of suretyship from a contract of guaranty.⁸⁸³ Both a surety and a guarantor are bound to another person, but a surety is “usually bound with his principal by the same instrument, executed at the same time and on the same consideration.”⁸⁸⁴ He is the original promisor and debtor from the start, and held liable for every known default of his principal.⁸⁸⁵ By contrast,

[t]he contract of guarantor is his own separate undertaking, in which the principal does not join. It is usually entered into before or after that of the principal and is often founded on a separate consideration from that supporting the contract of the principal. The original contract of the principal is not the guarantor’s contract, and the guarantor is not bound to take notice of its nonperformance.⁸⁸⁶

What the Code calls a contract of suretyship resembles more closely the U.S. contract of guarantor.⁸⁸⁷ The UCC term “surety,” however, encompasses a guarantor.⁸⁸⁸

Under the Code, a suretyship is a unilateral contract involving the surety and the creditor of the principal obligation.⁸⁸⁹ A suretyship contract must be in writing.⁸⁹⁰ Failure to comply with this form renders the contract invalid.⁸⁹¹ In 1998, the Supreme Arbitration Court ruled that a written instrument drawn up by the debtor and the surety satisfies the writing requirement of

881. See GUEV COMM. ONE, *supra* note 8, at 593.

882. These are two separate onerous contracts between different parties in which different considerations are exchanged.

883. BRAGINSKII COMM, *supra* note 81, at 449.

884. BLACK’S LAW DICTIONARY 1441 (6th ed. 1990).

885. *Id.*

886. *Id.*

887. See C. CIV. art. 361 (Russ.); U.C.C. § 1-201(40) (2001).

888. U.C.C. § 1-201(37) (2001).

889. C. CIV. art. 361 (Russ.).

890. C. CIV. art. 362 (Russ.).

891. *Id.*

suretyship.⁸⁹² The writing requirement includes the terms of the primary obligation between the debtor and the creditor, and the creditor's endorsement and acceptance of the suretyship.⁸⁹³ Article 362 does not require separate signatures from the surety and the creditor; rather the intent of both the surety and the creditor must be clearly expressed in writing.⁸⁹⁴

Under the new law, the surety is liable jointly and severally, and to the same extent as the debtor for the principal obligation, including any applicable interests, court costs and other related expenses.⁸⁹⁵ This rule differs substantially from the previous rule in the FP Civil Law of 1991, where the surety was only secondarily liable for the debtor's obligation.⁸⁹⁶ Although in practice, suretyship is primarily formed by contract, the law also recognizes statutory or legal surety.⁸⁹⁷

By its nature, a suretyship contract is executory because its performance is separated in time from its formation.⁸⁹⁸ It is also a unilateral contract under Russian law because one party has all the rights and the other party has only duties.⁸⁹⁹ For example, the creditor has the right to demand payment from the surety in the event of the debtor's nonperformance⁹⁰⁰ and the surety must perform the principal obligation for the creditor.⁹⁰¹ Because a suretyship contract is an accessory contract, its fate depends on the principal contract.⁹⁰² Therefore, if the principal contract is invalid, the suretyship is automatically invalid, and if the statute of limitations has tolled on the principal claim, the creditor will not be able to pursue its claim against the surety.⁹⁰³

If the rights to the principal obligation are assigned to a third party, the surety's obligations will remain unaffected, leaving him

892. C. CIV. ANN., *supra* note 55, at 360.

893. *Id.*

894. *Id.*

895. C. CIV. art. 363 (Russ.).

896. BRAGINSKII COMM., *supra* note 81, at 451.

897. *Id.* For example, a contract that supplies goods for government needs under Article 532 recognizes the government as the guaranty of the purchaser's obligation to pay when the buyer pays for the goods. C. CIV. art. 532 (Russ.).

898. See C. CIV. art. 361 (Russ.).

899. See *id.*

900. C. CIV. art. 363 (Russ.).

901. *Id.*

902. See C. CIV. art. 367 (Russ.).

903. See *id.*

to perform.⁹⁰⁴ A suretyship can be used to secure not only an existing obligation, but also any future obligations.⁹⁰⁵ Thus, stipulations as to the creditor's identity, the specific nature of the principal obligation and the amount owed under the principal obligation are significant conditions of a suretyship.⁹⁰⁶

Doctrine and case law⁹⁰⁷ further suggest that failure to stipulate the terms of a suretyship do not affect the contract's validity. Multiple sureties, in which case all will be held jointly and severally liable for the principal obligation, may secure a principal obligation.⁹⁰⁸ Furthermore, where two separate security devices can secure one principal obligation, the creditor retains the discretionary right to proceed against either the surety or the mortgagor.⁹⁰⁹ The creditor may act simultaneously or in any order preferred by the creditor.⁹¹⁰ The surety's obligation to perform arises only if the debtor fails to perform under the primary obligation.⁹¹¹ The surety's liability may be modified, which may provide for subsidiary liability of the surety.⁹¹² A surety who performs the debtor's obligations has the right to seek indemnification from the principal debtor.⁹¹³ Upon performance of the debtor's obligations, the creditor will turn over all evidentiary documents to the surety, as well as documents securing the performance of such obligations by the debtor to the creditor.⁹¹⁴

Suretyship is also subject to termination on five separate grounds:⁹¹⁵ termination of the principal obligation; ⁹¹⁶ modifying

904. C. CIV. art. 382 (Russ.). Article 382 generally governs the assignment of the rights of a creditor to a third person. For example, A owes B money, the debt is secured by C as surety for A, B assigns his rights of claim against A to D. The assignment of the rights from B to D does not affect the suretyship of the debt owed by A. None of the grounds in Article 367 apply here because the assignment was the right of B, not the debt of A. C. CIV. art. 367 (Russ.).

905. C. CIV. art. 361 (Russ.).

906. See Letter of January 26, 1994 by the Supreme Arbitration Court as cited in R.F. Civil Code Annotated 360-61; see also SADIKOV COMM. ONE, *supra* note 74, at 614.

907. C. CIV. ANN. *supra* note 55, at 360.c

908. C. CIV. art. 363 (Russ.).

909. SADIKOV COMM. ONE, *supra* note 74, at 616.

910. *Id.*

911. C. CIV. art. 363 (Russ.).

912. *Id.*

913. C. CIV. art. 365 (Russ.).

914. *Id.*

915. C. CIV. art. 367 (Russ.).

916. *Id.*

the principal obligation in a manner that increases the surety's responsibility or entails other adverse consequences for the surety without his consent;⁹¹⁷ delegating the duty to perform the principal obligation from the original debtor to a third party if the surety refuses to accept responsibility for the new debtor;⁹¹⁸ the creditor's failure to accept proper performance of the obligation from either the debtor or the surety;⁹¹⁹ and the expiration of the suretyship's term, accompanied by failure of the creditor to file suit against the surety within this time period.⁹²⁰ Without the debtor's consent, or over his objection, the surety may raise any objections to the creditor's claims.⁹²¹

Although there are two different time limits for the statute of limitations and the suretyship term in Russian legal literature⁹²² and in the Code,⁹²³ there are four core distinctions. First, the suretyship's term is the time period for which it was granted, during which the creditor may make demands on the surety.⁹²⁴ By contrast, the statute of limitations is the period during which a plaintiff may file a claim in court to defend the legal rights and protected interests against a person who violated such rights or interests.⁹²⁵ Second, the general statute of limitations is three years, which may be extended or reduced in special cases.⁹²⁶ More importantly, the statute of limitations is established by law and not by agreement of the parties.⁹²⁷ Conversely, the term of suretyship is fixed by contract not by law.⁹²⁸ Third, the surety is not the person who violated the rights of the creditor.⁹²⁹ Therefore, the

917. *Id.*

918. *Id.*

919. *Id.*

920. *Id.*

921. See C. CIV. art. 364 (Russ.).

922. BRAGINSKII COMM., *supra* note 81, at 481.

923. C. CIV. arts. 195, 361-67 (Russ.).

924. C. CIV. art. 367 (Russ.).

925. C. CIV. art. 195 (Russ.).

926. C. CIV. arts. 196, 197 (Russ.).

927. C. CIV. art. 198 (Russ.).

928. C. CIV. art. 367 (Russ.). If a term was not established by contract, "the surety shall terminate unless the creditor brings suit against the surety within a year from the day of occurrence of the time for performance of the obligation secured by the surety. When the term for performance of the basic obligation is not indicated and cannot be determined or is determined by the time of demand, the surety shall be terminated unless the creditor brings a suit against the surety within two years from the day of conclusion of the contract of suretyship." *Id.*

929. See C. CIV. art. 363 (Russ.).

statute of limitations does not apply when the creditor files claims against the surety.⁹³⁰ Fourth, the statute of limitations bars court action only by an affirmative assertion by an interested party.⁹³¹ By contrast, the expiration of a suretyship's term is an absolute bar to a judicial action.⁹³²

Modern Russian suretyship law can be reduced to the following proposition: a contract of suretyship is bilateral, accessory, unilateral and executory.⁹³³

In 1998, the Supreme Arbitration Court fleshed out the practical details of the current suretyship law.⁹³⁴ The Court held that because the Code requires that the obligation's term be determined by the calendar date or the expiration of a period of time,⁹³⁵ a provision of a suretyship setting the obligation's term as of the time of its actual performance cannot be deemed to be an acceptable stipulation on the term of the suretyship, as it is inconsistent with Article 190 of the Code.⁹³⁶ Parties may form a suretyship to secure an obligation that arises in the future.⁹³⁷ A stipulation in a suretyship that confines the liability of the surety to repayment of the principal debt, as well as the payment of any applicable interests, will be construed as limiting the liability of the surety to only these two amounts.⁹³⁸ If a suretyship stipulates a term for which suretyship is given, the suretyship will terminate if, during this term, the creditor fails to file claims against the surety.⁹³⁹ If changes to the principal obligation were made without the surety's consent, and these changes lead to an increase in liability or other unfavorable consequences to the surety, the surety will terminate from the time when such changes were

930. See C. CIV. art. 367 (Russ.).

931. C. CIV. art. 199 (Russ.).

932. See C. CIV. art. 367 (Russ.). The Code requires the filing of a court claim within the stipulated period. *Id.*

933. It is bilateral in the sense that there are two parties, but also unilateral because one party has all the rights and the other party has all the obligations.

934. TIKHOMIROV, *supra* note 69, at 77-87.

935. C. CIV. art. 190 (Russ.). Computed in years, months, weeks, days or hours, or by the indication of an event certain to occur. *Id.*

936. Article 190 states that the time limit (term) of a contract must be stated as a calendar date, expiration or a time period, or by indication of an event which must inevitably occur. As such, the Supreme Court held that the term stating "the time of actual performance of contract" is too vague to fit under article 190. See TIKHOMIROV, *supra* note 69, at 78.

937. C. CIV. art. 361 (Russ.).

938. See C. CIV. art. 363 (Russ.).

939. *Id.*

made.⁹⁴⁰ If the debtor fails to make a payment directed by a court decision, the creditor has the right to resort to the surety for such payment.⁹⁴¹ If the debtor defaults on his debt and the creditor sues him, but is unable to collect a judgment in his favor, the creditor may sue the surety for the original obligation.⁹⁴² The suit may go forward only on the theory that both the debtor and the surety are solidarily liable for the debt until fully paid by the debtor and the entry of an earlier judgment of the debt in favor of the creditor does not extinguish the obligation of the surety as long as the creditor has not collected payment on that earlier judgment.⁹⁴³ A contract of surety may stipulate that the surety will be liable for a new debtor in the event of a delegation of duty under the secured obligation.⁹⁴⁴ Since the surety is not a party to the principal obligation, it cannot institute a court action seeking to invalidate the contract from which the secured obligation arises.⁹⁴⁵

5. Bank Guaranty (Bankovskaia Garantiia)

As a security device, bank guaranty is new to Russian law.⁹⁴⁶ It was borrowed from continental European law.⁹⁴⁷ In formulating the rules in Articles 368-379, the Code drafters relied heavily on the Uniform Rules for Demand Guaranties adopted in 1992 by the International Chamber of Commerce.⁹⁴⁸ A "bank guaranty" corresponds to the U.S. Uniform Commercial Code's "letter of credit."⁹⁴⁹ A widely available Russian translation of the UCC, however, translates "letter of credit" as "*akkreditiv*" rather than "*bankovskaia garantiia*."⁹⁵⁰

The UCC defines letter of credit as "a promise by a bank or other issuer that it will honor on behalf of one of its customer's demands for payment, upon compliance with specified

940. *Id.*

941. See C. Civ. art. 363 (Russ.).

942. TIKHOMIROV, *supra* note 69, at 82.

943. TIKHOMIROV, *supra* note 69, at 82.

944. *Id.* at 83.

945. *Id.* at 84.

946. BRAGINSKII COMM., *supra* note 81, at 463.

³ *Id.*

948. *Id.*; SADIKOV COMM. ONE, *supra* note 74, at 620.

949. THE AMERICAN LAW INSTITUTE AND THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS, UNIFORM COMMERCIAL CODE, OFFICIAL TEXT 1990 258 (S.N. Lebedev et al. trans., Int'l Ctr. Of Fin. & Econ. Dev. 1996) [hereinafter UCC IN RUSSIAN].

950. *Id.*

conditions.”⁹⁵¹ The device acts as a solemn promise that the guarantor, or a credit institution, which issues a written obligation undertakes to pay the beneficiary at the request of the principal. This is in accordance with the conditions stipulated by the guarantor and in a fixed amount of money upon the beneficiary’s presentation of a written demand for payment.⁹⁵²

The Presidium of the Supreme Arbitration Court of the Russian Federation ruled that the absence of a written agreement between the principal and the guarantor would not invalidate the guaranteed obligation before the beneficiary.⁹⁵³ The reason for the court’s ruling was primarily because the guaranteed obligation arises between the two parties on the basis of the guarantor’s unilateral written obligation.⁹⁵⁴ According to the case, the bank-guarantor issued a bank guaranty to the beneficiary in which it guaranteed the principal’s obligation.⁹⁵⁵ When the event stipulated in the bank guaranty occurred, the beneficiary demanded performance of the obligation under the bank guaranty, but the guarantor refused, arguing there was no written agreement between the bank-guarantor and the principal.⁹⁵⁶ The Court’s ruling rejected the bank-guarantor’s argument.⁹⁵⁷

Failure to stipulate the name of the beneficiary in whose interest the guaranty was issued does not invalidate the obligation before the beneficiary.⁹⁵⁸ When the principal-debtor defaulted on the debt, the beneficiary demanded payment from the bank. Payment was refused, however, because there was no valid guaranty obligation between the bank and the beneficiary.⁹⁵⁹ Again, the Court rejected the bank’s argument.⁹⁶⁰ In the Court’s opinion, “it does not follow from Article 368 that a bank guaranty must stipulate a specific beneficiary. In the absence of such stipulation, the guaranty obligation shall be performed in favor of the creditor (beneficiary) who tenders the guaranty in its original

951. U.C.C. § 5-103(1) (2001); GIFIS, *supra* note 707, at 289.

952. C. CIV. art. 368 (Russ.).

953. C. CIV. ANN., *supra* note 55, at 303.

954. *Id.*

955. *Id.* at p. 303.

956. C. CIV. ANN., *supra* note 55, at 303.

957. *Id.*

958. *Id.* at 304.

959. *Id.*

960. *Id.*

form" [author's translation].⁹⁶¹

The Court also handed down binding interpretations of other aspects of this security device. The term of a guaranty letter is a significant condition of a guaranty obligation. When a guaranty letter fails to stipulate the time period the guaranty is given, the guaranty obligation will be deemed as not being created.⁹⁶² If there is evidence of termination of the principal obligation due to proper performance and the beneficiary was notified of it prior to presentation of a written claim against the guarantor, the court may reject the beneficiary's claim on the basis of "abuse of rights."⁹⁶³ Unless otherwise provided in the guaranty letter, the guarantor's obligation does not depend on the relations between the parties in the principal obligation.⁹⁶⁴ The letter of guaranty is subject to performance at the beneficiary's demand.⁹⁶⁵

Unless the letter of guaranty provides otherwise, the liability of the guarantor is not limited to the amount the guaranty is given and may include any applicable interests.⁹⁶⁶ A lawsuit by the beneficiary against the guarantor seeking payment of monetary claims may be filed within the general statute of limitations.⁹⁶⁷ As such, it is not limited in time to the term of the letter of guaranty.⁹⁶⁸

The device known as a bank guaranty is fundamentally different from the 1964 Russian Civil Code⁹⁶⁹ and 1991 FP Civil Law⁹⁷⁰ versions of guaranty (*garantiia*).⁹⁷¹ As pointed out in the foregoing discussion of suretyship, the Soviet era guaranty was merely a surrogate of suretyship specifically intended for use in the command economy system that prevailed in Russia until 1993.⁹⁷² The 1991 Russian concept of guaranty is different from the bank

961. *Id.*

962. See C. Civ. art. 374 (Russ.).

963. See C. Civ. art. 10 (Russ.). The Code states "[a]ctions of citizens and juridical persons effectuated exclusively with the intention to cause harm to another person, and also abuse of a right in other forms, shall not be permitted." *Id.*

964. C. Civ. art. 370 (Russ.).

965. C. Civ. art. 374 (Russ.).

966. C. Civ. art. 377 (Russ.).

967. TIKHOMIROV, *supra* note 69, at p. 76.

968. *Id.*

969. SADIKOV COMM. ONE, *supra* note 74, at 620.

970. *Id.*

971. See BRAGINSKII COMM., *supra* note 81, at 462.

972. See *id.* at 448-49. See also my discussion of suretyship above.

guaranty under the 1994 Russian Civil Code.⁹⁷³ Nevertheless, several Russian commentators take different viewpoints on the nature of bank guaranty.⁹⁷⁴ Professor Vitrianskii's⁹⁷⁵ view that a bank guaranty is a novel form of a security device, which first surfaced in Russian civil law with the adoption of the 1994 Civil Code, prevails today.⁹⁷⁶

The most prominent feature of a security device is that it is independent of the primary obligation. If the primary contract it secures is declared invalid, the obligation arising from the bank guaranty is not terminated.⁹⁷⁷ A review of Russian legal literature and Supreme Court of Arbitration of the Russian Federation case law⁹⁷⁸ yields the following bank guaranty interpretation: only a credit institution can issue a bank guaranty⁹⁷⁹ and only a debtor in a principal obligation can request a bank to issue a written bank guaranty to secure that obligation.⁹⁸⁰

A bank guaranty is a unilateral obligation in which the guarantor becomes obligated to make payment to the beneficiary of the principal obligation, and the latter acquires the right to demand such payment from the guarantor.⁹⁸¹ The right of the beneficiary under the principal obligation may be realized by presenting a written demand for payment to the guarantor and the demand will correspond to the terms stipulated in the bank guaranty.⁹⁸² To receive payment, Article 374 requires only that the beneficiary file a written demand (*trebovanie*) with the guarantor. Thus, there is no need to file a lawsuit (*isk*).⁹⁸³ A guarantor will

973. SADIKOV COMM. ONE, *supra* note 74, at 620.

974. Malamed opines that bank guaranty under the 1994 Civil Code is the same thing as guaranty under the 1964 Civil Code and the 1991 Fundamental Principles of Civil Legislation of the USSR and the Union Republics. See BRAGINSKII COMM., *supra* note 81, at 462; E.A. Pavlodskii opines that bank guaranty is not at all a security, but is more like an insurance policy taken out against the risk of non-payment by a debtor. See *id.*

975. See BRAGINSKII COMM., *supra* note 81, at 462.

976. See *id.*

977. C. CIV. art. 370 (Russ.).

978. C. CIV. arts. 368-379 (Russ.). See generally BRAGINSKII COMM., *supra* note 81, at 462-71; SADIKOV COMM. ONE, *supra* note 74, at 620-27; GUEV COMM. ONE, *supra* note 8, at 601-12.

979. C. CIV. art. 368 (Russ.).

980. *Id.*

981. *Id.*

982. C. CIV. art. 374 (Russ.).

983. See *id.* This is in stark contrast to the rule in Article 367 stating the creditor is required to file not just a written demand, but also a lawsuit against a surety. See C. CIV. art. 367 (Russ.).

issue a bank guaranty only upon receipt of consideration from the principal,⁹⁸⁴ and the terms of the consideration shall be based in agreement between the guarantor and the principal.⁹⁸⁵

Russian doctrine and case law⁹⁸⁶ further note that upon payment to the beneficiary of the sum stipulated in a bank guaranty, the guarantor has the right to seek indemnification from the principal.⁹⁸⁷ Because the relationship between the beneficiary and the guarantor is founded on a written unilateral obligation assumed by the guarantor, the validity of this obligation does not depend on whether or not there exists a written agreement between the principal and the beneficiary.⁹⁸⁸

As a general rule, a bank guaranty is irrevocable because the issuing guarantor cannot revoke it.⁹⁸⁹ The beneficiary's rights under a bank guaranty are not transferable to a third party.⁹⁹⁰ Both of these foregoing rules, however, are not dispositive since the bank guaranty itself may stipulate that it is revocable and/or transferable.⁹⁹¹ Upon receipt of a written demand for payment, the guarantor will immediately notify the principal and submit a copy of the demand, along with all accompanying documents.⁹⁹² Upon receipt of the written demand for payment from the beneficiary, within a reasonable time the guarantor will determine whether the written demand conforms with the terms stipulated in the bank guaranty.⁹⁹³

The independence of the bank guaranty from the principal obligation means, among other things, that the only reason the guarantor may refuse payment is if the written demand for payment by the beneficiary does not meet the terms stipulated in the bank guaranty.⁹⁹⁴ It may not be on grounds related to the principal obligation.⁹⁹⁵ The Presidium of the Supreme Arbitration Court ruled that under the provisions of Article 373 of the Code,

984. C. Civ. art. 369 (Russ.).

985. See C. Civ. art. 368 (Russ.).

986. C. Civ. art. 368 (Russ.).

987. C. Civ. art. 379 (Russ.).

988. See C. Civ. art. 370 (Russ.).

989. C. Civ. art. 371 (Russ.).

990. C. Civ. art. 372 (Russ.).

991. C. Civ. arts. 371, 372 (Russ.).

992. C. Civ. art. 375 (Russ.).

993. *Id.*

994. C. Civ. art. 376 (Russ.).

995. See *id.*

the guarantor must be notified of the beneficiary's acceptance of the guaranty for a bank guaranty obligation to arise, unless the text of the letter of guaranty specifically states otherwise.⁹⁹⁶

The Code lists the grounds on which a bank guaranty terminates.⁹⁹⁷ These include: payment to the beneficiary of the amount for which the guaranty was issued; expiration of the term for which the guaranty was issued; relinquishment by the beneficiary of his rights under the bank guaranty and his return of the guaranty to the guarantor; and written relinquishment by the beneficiary of his rights under the guaranty and his release of the guarantor from its obligation.⁹⁹⁸ Upon termination of the guaranty, the guarantor must immediately notify the principal.⁹⁹⁹

6. Earnest Money (*Zadatok*)

The last of the nominate security devices enumerated in Chapter 23 of the Code is earnest money.¹⁰⁰⁰ Earnest money traces its origins to the Roman law security device known as *arra*.¹⁰⁰¹ Under Russian law, earnest money performs four functions: security, evidence, payment and civil liability for breach.¹⁰⁰² A prominent feature of earnest money is that a defaulting party, in addition to paying earnest money, remains liable for damages from breach.¹⁰⁰³ Russian law separates the notions of earnest money (*zadatok*) from accord and satisfaction (*otstupnoe*).¹⁰⁰⁴ The former secures the performance of an obligation while the latter releases the defaulting party, thereby terminating an obligation.¹⁰⁰⁵

Earnest money is a monetary sum given by a contracting party to be credited towards the amount owed under a payment contract. It is evidence of the conclusion of the contract and acts as security for performance.¹⁰⁰⁶ Russian legal scholarship and case law interprets earnest money as money to be paid only in

996. C. CIV. ANN., *supra* note 55, at 375.

997. C. CIV. art. 378 (Russ.).

998. *Id.*

999. *Id.*

1000. C. CIV. arts. 380, 381 (Russ.).

1001. See BRAGINSKII COMM., *supra* note 81, at 471.

1002. See *id.* at 472-74.

1003. C. CIV. art. 381 (Russ.).

1004. See C. CIV. art. 380 (Russ.).

1005. BRAGINSKII COMM., *supra* note 81, at 472.

1006. C. CIV. art. 380 (Russ.).

monetary form, not in kind.¹⁰⁰⁷

On its face, earnest money resembles a down payment but differs fundamentally from the latter. Like a down payment, earnest money performs both evidentiary and payment functions.¹⁰⁰⁸ Unlike earnest money, however, a down payment does not secure the performance of an obligation.¹⁰⁰⁹ Moreover, the law requires an earnest money agreement to be in writing. An agreement on a down payment, however, can be oral.¹⁰¹⁰ Where there is any doubt as to whether payment made is earnest money or a down payment, and the contract is silent on the point, the law presumes it to be a down payment unless shown otherwise.¹⁰¹¹

Earnest money can be used to secure only a contractual obligation (not a noncontractual obligation such as an obligation arising from tort).¹⁰¹² Earnest money payment serves as prima facie evidence that a contract was formed between the parties, especially if none of the parties contests the fact that earnest money was paid.¹⁰¹³ It also serves as conclusive evidence that a contract was entered into if the contract does not stipulate the payment of earnest money, one of the parties contests the fact that earnest money was paid and the other proves by means of other evidence that earnest money was paid.¹⁰¹⁴

If a contract provides that one party will pay the earnest money, the contract will be deemed formed after payment is made.¹⁰¹⁵ Earnest money may be used to secure only a monetary obligation.¹⁰¹⁶ Regardless of what amount is involved, an agreement for earnest money must be concluded in writing.¹⁰¹⁷ Failure to conclude the earnest money contract in writing,

1007. See generally BRAGINSKII COMM., *supra* note 81, at 471-74; SADIKOV COMM. ONE, *supra* note 74, at 627-28; GUEV COMM. ONE, *supra* note 8, at 612-15.

1008. C. CIV. art. 380 (Russ.). However, whereas earnest money serves as proof positive (i.e., conclusive evidence) of the formation of a contract, a down payment does not. A down payment is treated merely as one of many other admissible evidence to prove the existence of a contract. See SUKHANOV 2(1), *supra* note 83, at 61.

1009. See BRAGINSKII COMM., *supra* note 81, at 472.

1010. C. CIV. art. 380 (Russ.).

1011. *Id.* In Russian commercial law practice, earnest money is used most commonly in public bids. SADIKOV COMM. ONE, *supra* note 74, at 627.

1012. BRAGINSKII COMM., *supra* note 81, at 472.

1013. *Id.* at 472-73.

1014. C. CIV. art. 380 (Russ.).

1015. See *id.*

1016. BRAGINSKII COMM., *supra* note 81, at 473.

1017. *Id.*

however, would not necessarily make it invalid.¹⁰¹⁸ An oral earnest money agreement must state that the parties may not prove earnest money payment through witness testimony, but must do so by providing some sort of documentary evidence.¹⁰¹⁹ Earnest money can be used to secure an obligation either between two individuals, two legal entities or between a legal entity and an individual.¹⁰²⁰ If an obligation secured by earnest money terminates on one of the grounds established by law prior to commencement of performance, the earnest money must be returned to the party that paid it.¹⁰²¹

One of the purposes of earnest money is to deter nonperformance of the obligation.¹⁰²² This purpose is reflected in the rules governing the consequences of nonperformance of an obligation secured by earnest money.¹⁰²³ If the defaulting party is the one that paid the earnest money, the other party must retain the money.¹⁰²⁴ If the defaulting party is the one that received the earnest money, it must pay to the other party twice the earnest money amount.¹⁰²⁵ This rule applies only in the situations where the defaulting party did not perform the obligation at all.¹⁰²⁶ It does not apply if the defaulting party performed the obligation improperly.¹⁰²⁷

Nonperformance of an obligation entails the payment of damages.¹⁰²⁸ In this regard, the Code establishes a relationship between the earnest money paid and the damages to be paid.¹⁰²⁹ If the contract does not stipulate otherwise, damages will be paid in an amount that discounts the earnest money.¹⁰³⁰ Thus, if the defaulting party paid the earnest money, it must pay damages in an

1018. See C. CIV. art. 329 (Russ.). As it would in the case of liquidated damages, mortgage or suretyship. See C. CIV. arts. 331, 339, 362 (Russ.).

1019. C. CIV. art. 162 (Russ.).

1020. BRAGINSKII COMM., *supra* note 81, at 473.

1021. C. CIV. art. 381 (Russ.).

1022. See *id.*

1023. *Id.*

1024. *Id.*

1025. *Id.*

1026. *Id.* Article 381 specifically limits its scope to nonperformance and does not cover partial, improper, or delayed performance. See *id.*

1027. *Id.*

1028. C. CIV. art. 381 (Russ.).

1029. *Id.*

1030. *Id.*

amount that exceeds the earnest money.¹⁰³¹ Liability for breach of the obligation secured by earnest money is determined by the general rules in Article 401.¹⁰³²

The Russian notion of earnest money resembles, but should be clearly distinguished from, five related concepts in U.S. law: advance payment, down payment, earnest money, deposit payment and prepayment. Under U.S. law, advance payment is money paid before payment is legally due, such as to an author of a book yet to be written.¹⁰³³ Down payment is the portion of a purchase price that is generally required to be paid in cash at the time a purchase and sale agreement is signed.¹⁰³⁴ This payment represents only a part of the total cost. Earnest money is a sum paid by a buyer at the time of entering a contract to indicate the buyer's intention and ability to carry out the contract.¹⁰³⁵ Often the contract provides for forfeiture of this sum if the buyer defaults.¹⁰³⁶ In U.S. practice, earnest money is the same as a deposit payment.¹⁰³⁷ Deposit payment is "money placed with a person as an earnest or security for the performance of some contract, to be forfeited if the depositor fails in his undertaking. It may be deemed a part payment and, to that extent, the purchaser may be deemed the actual owner of the estate."¹⁰³⁸

In real estate transactions, the term earnest money is used to denote a comparatively small sum paid as an assurance that the party is acting in earnest and good faith.¹⁰³⁹ If his being in earnest and good faith fails, the payment will be forfeited.¹⁰⁴⁰ Thus, unlike earnest money that is, by definition, forfeited on breach of the contract, down payment is not forfeited.¹⁰⁴¹ Prepayment is

1031. *Id.* For example, if the earnest money was \$100 and the damages are computed to be \$150, it shall pay \$50 to the other party. If the defaulting party received \$100 in earnest money, the other party would be entitled to demand payment of twice the amount of earnest money, \$200, in addition to damages in an amount that exceeds the earnest money. Thus, if the damages are estimated at \$150, this would come to \$50 on top of \$200. Such party would then recover \$250 from the defaulting party.

1032. C. Civ. art. 401 (Russ.).

1033. C. Civ. art. 487 (Russ.).

1034. C. Civ. art. 380 (Russ.).

1035. *See id.*

1036. C. Civ. art. 381 (Russ.).

1037. BLACK'S LAW DICTIONARY 508 (6th ed. 1996).

1038. *Id.* at 438.

1039. *Id.* at 508.

1040. *Id.*

1041. GUEV COMM. ONE, *supra* note 8, at 615.

payment of a debt obligation or expense before it is due.¹⁰⁴²

Against this backdrop, it seems that the Russian concept of "avans"¹⁰⁴³ corresponds to the U.S. concept of "down payment," not an "advance payment." It also follows that the Russian notion of "zadatok"¹⁰⁴⁴ is different from a U.S. down payment, and rather, approximates "earnest money" in U.S. law. The U.S. notion of advance payment would correspond to the Russian form of payment called "*predoplata*."¹⁰⁴⁵ The Russian term "*predoplata*," however, may also mean prepayment depending on the context used. Whereas prepayment applies to any type of contract, advance payment typically applies in authorship contracts where an author is advanced a portion of his royalty that normally would be at the time of sale of his book by the publisher.¹⁰⁴⁶

XII. REMEDIES: LIABILITY FOR BREACH OF CONTRACT

A. Nature, Functions and Classification of Civil Liability

Russian doctrine defines civil liability as a remedy for the violation of a civil law right¹⁰⁴⁷ that creates for the violator negative consequences in the form of new or additional civil law responsibilities.¹⁰⁴⁸ Chapter 25 regulates liability for breach of contract.¹⁰⁴⁹ The provisions of this chapter are aimed at protecting the rights of an aggrieved party in a contractual relationship.¹⁰⁵⁰ All of the measures contemplated in this chapter are applied by a

1042. *Id.* at 1182.

1043. See SUKHAREV, *supra* note 70, at 3.

1044. C. Civ. arts. 380-81 (Russ.).

1045. In common usage the Russian term *predvaritelnaia oplata* is abbreviated as *predoplata*. This form of payment is regulated by C. Civ. art. 487 (Russ.).

1046. GIFIS, *supra* note 707, at 12.

1047. The meaning of "civil law right" under Russian law differs from a "civil right" as it is understood in the United States; in Russian law it means a right under a civil law obligation. C. Civ. arts. 8-12 (Russ.). So as not to confuse the two meanings in the mind of the reader, the author uses "civil law right." The corresponding Russian term is "*grazhdanskie prava*."

1048. BRAGINSKII COMM., *supra* note 81, at 483. Russian law does not use the term "remedies" to mean "remedies for breach of contract", which is purely common law terminology. Rather, Russian law speaks of "*grazhdansko-pravovaia otvetstvenost za narushenie dogovora*", which means "civil-legal liability for breach of contract. This meaning distinguishes it from other types of legal liability, like criminal, administrative, etc.

1049. C. Civ arts. 393-406 (Russ.).

1050. C. Civ. arts. 395-99, 401 (Russ.).

court decision at the petition of the aggrieved party.¹⁰⁵¹ The provisions of Chapter 25 are related to, and should be read against, the backdrop of the general provisions in Articles 10-16. The provisions establish the general principles relating to the protection of violated civil rights.

Even though the measures discussed in Chapter 25 may be referred to generically as remedies for breach of contract, some of the measures do not qualify as civil remedies.¹⁰⁵² The Russian concept of "*sanktsiia*" corresponds to the U.S. law approach to remedy or relief.¹⁰⁵³ Russian law gives the creditor a choice of remedies for breach of contract.¹⁰⁵⁴ There are two general categories of remedies for breach of contract in the Code: Chapter 25 remedies and remedies under Articles 10-16 and 381. The selection of which particular remedy to apply to a given situation depends on the nature of the violation. The general rule is that for each violation a single remedy form applies. As an exception to this rule, however, the law permits the application of two compatible forms of remedies, e.g. damages and liquidated damages.¹⁰⁵⁵

In breach of contract cases, where there is nonperformance or improper performance, the debtor is liable to the creditor.¹⁰⁵⁶ The form of liability varies with each case, but the most common is payment of damages.¹⁰⁵⁷ The grounds for the imposition of damages, the amount of damages and the conditions for the payment of damages are regulated by Articles 15 and 393.¹⁰⁵⁸ A few preliminary matters must be examined before we look at the specific remedies available under Russian law. These preliminary matters include: the nature of civil liability, types of civil liability, functions of civil liability and the conditions required for civil liability under the Code.¹⁰⁵⁹

1051. SADIKOV COMM. ONE., *supra* note 74, at 639.

1052. *Id.* For example, this chapter discusses the possessory remedy (*replevin*) contemplated under Article 398. See C. CIV. art. 398 (Russ.).

1053. The individual forms of civil liability denominated as "*sanskiia*" (sanction) in Russian law are traditionally discussed under "remedies" in U.S. law. See ROHWER & SCHABER, *supra* note 6, at 248-288.

1054. C. CIV. art. 394 (Russ.).

1055. See BRAGINSKII COMM., *supra* note 81, at 483.

1056. C. CIV. arts. 393, 401 (Russ.).

1057. See C. CIV. arts. 15, 393 (Russ.).

1058. *Id.*

1059. This structural approach to organizing this topic is adopted in OSAKWE, *supra* note 20, at 139-40.

Under Russian law, the nature of civil liability is characterized by the following six features: exacted in a monetary form, imposed by a court decision, enforceable against the person who breached his contractual obligation, enforceable liability in the sense that its payment is not left to the discretion of the offending party, imposed uniformly in similar situations and imposed within limits established by law.¹⁰⁶⁰

The first of these six features calls for additional clarification. The exacted-in-money-form feature means that civil liability is in the form of money and in favor of the creditor.¹⁰⁶¹ Only in exceptional situations is civil liability exacted in favor of the state.¹⁰⁶² This occurs in circumstances when a breach of contract is so serious as to affect the general interest of the state or public interest.¹⁰⁶³ In that case, civil liability is exacted from the offending party (or parties) and turned over to the state.¹⁰⁶⁴ For example, a contract that violates public policy is void.¹⁰⁶⁵ If both parties to such a contract are equally guilty, anything received by the parties from each other shall be confiscated and turned over to the state coffers.¹⁰⁶⁶

The monetary form of civil liability also means that the amount of civil liability is measured to reflect the full amount of damage suffered by the creditor.¹⁰⁶⁷ This principle of full compensation may be modified in either direction (i.e., compensation may be exacted in an amount that is less than or exceeds the losses actually suffered by the creditor) depending on the totality of circumstances of each case.¹⁰⁶⁸ The exaction of damages in an amount that exceeds the losses actually suffered is tantamount to punitive damages.¹⁰⁶⁹ Punitive damages are permitted in tort law, but not in contract law.¹⁰⁷⁰ Under Russian contract law, civil liability is typically exacted in the form of

1060. *Id.*

1061. BRAGINSKII COMM., *supra* note 81, at 483.

1062. *Id.* at 483-84.

1063. *Id.* at 484.

1064. *Id.*

1065. C. CIV. art. 169 (Russ.).

1066. See BRAGINSKII COMM., *supra* note 81, at 287.

1067. *Id.* at 484.

1068. See discussion of quantum of damages in XII(B)(1) *infra*.

1069. See *id.*

1070. See *id.*

money.¹⁰⁷¹

The classification of civil liability into types depends on the criteria used for such classification. If the yardstick for classification is the basis for civil liability, Russian law classifies civil liability into two types, contractual (conventional) and statutory (legal).¹⁰⁷² A contractual civil liability is agreed to by the parties and stipulated in a contract.¹⁰⁷³ Statutory civil liability is imposed by operation of law.¹⁰⁷⁴ Statutory civil liability may be imposed either in lieu of contractual liability (e.g., when the contract is silent on the matter of civil liability) or on top of contractual liability.¹⁰⁷⁵ More commonly, civil liability is contractual. If the criterion for classification is the share of several participants in the overall liability, civil liability is divided into solidary, several, subsidiary, mixed and by way of indemnification.¹⁰⁷⁶

Solidary liability means that all debtors are liable jointly and severally.¹⁰⁷⁷ The creditor may proceed against all of the debtors jointly or against individual debtors separately.¹⁰⁷⁸ If the creditor chooses to proceed against one of the debtors separately and recovers from him only a portion of the debt owed, he may proceed against the other debtors jointly or separately until the full amount of debt is recovered.¹⁰⁷⁹ If one of the debtors pays the full debt to the creditor, he will be entitled to proceed against the other debtors to collect in excess of his own share of the joint debt.¹⁰⁸⁰ This is done by an indemnification action against his co-debtors.¹⁰⁸¹

Solidary liability under Russian law corresponds to joint and several liability under U.S. law.¹⁰⁸² Liability is several if the share of each debtor is separate and distinctly apportioned. In this case, the creditor may proceed against each debtor for his apportioned

1071. See BRAGINSKII COMM., *supra* note 81, at 483.

1072. *Id.* at 486.

1073. *Id.*

1074. *Id.*

1075. *See id.*

1076. *Id.* at 488. *See also* OSAKWE, *supra* note 20, at 139.

1077. BRAGINSKII COMM., *supra* note 81, at 488.

1078. C. CIV. art. 323 (Russ.).

1079. *Id.*

1080. C. CIV. art. 325 (Russ.).

1081. *Id.*

1082. BLACK'S LAW DICTIONARY 914 (6th ed. 1996).

share of the total liability. Under this scenario, the creditor is not entitled to recover from any one of the several debtors an amount in excess of that debtor's share of the total debt.¹⁰⁸³

Subsidiary liability is where the creditor must first proceed against a primary debtor in an effort to recover a debt.¹⁰⁸⁴ If after such first recourse to the primary debtor the creditor is unable to recover all or a portion of the debt, he may proceed against the secondary debtor to recover the rest of the debt.¹⁰⁸⁵ The clear implication of this rule is that the creditor may not resort to the secondary debtor until he has exhausted his efforts to recover the debt from the primary debtor.¹⁰⁸⁶ If the secondary debtor pays the creditor all or a portion of the debt, he will be entitled, in some situations, to seek indemnification from the primary debtor for that amount.¹⁰⁸⁷

Mixed liability occurs where there is contributory fault on the part of the creditor, which in turn constitutes a basis for a proportionate reduction in the civil liability of the debtor.¹⁰⁸⁸ Thus, if the creditor's fault contributed twenty percent to the liability of the debtor, the amount of recovery from the debtor shall be reduced proportionately by twenty percent. In other words, mixed liability takes into account the contributory fault of the creditor.¹⁰⁸⁹ Finally, liability through indemnification (*regressnyi isk*) allows the creditor to proceed against the debtor based on the performance of the obligation owed by the debtor to another person.¹⁰⁹⁰

Under Russian law, the system of remedies for breach of contract performs four distinct but overlapping functions. First, it compensates the creditor for his losses in an amount that restores his financial situation to where it would have been had the contract been properly performed (restorative function).¹⁰⁹¹ Second, it deters a breach of the contract (deterrence function).¹⁰⁹² Third, it stimulates the debtor to perform his contractual obligations in

1083. BRAGINSKII COMM., *supra* note 81, at 488.

1084. C. CIV. art. 399 (Russ.).

1085. *Id.*

1086. *See id.*

1087. *Id.*

1088. *See* C. CIV. art. 404 (Russ.).

1089. *Id.*

1090. SUKHAREV, *supra* note 70, at 855.

1091. OSAKWE, *supra* note 20, at 140.

1092. *Id.*

good faith (educational function).¹⁰⁹³ Lastly, it punishes breach of contract (punitive function).¹⁰⁹⁴ Russian law stresses the first three functions of civil liability, but permits the fourth function as an exception to the general rule.¹⁰⁹⁵ In other words, the primary purpose of contract remedies is not only to compensate the aggrieved party for his losses resulting from the breach of contract by the other party, but it seeks to compel the promisor not to breach the contract, to punish him if he does breach the contract, to serve as a warning to others as to the consequences of a breach of contract, and only incidentally, to compensate the aggrieved party for his losses.¹⁰⁹⁶ In effect, this Russian rule stands on its head the policy considerations that govern U.S. contract law remedies.

The law regulates situations and conditions in which punitive civil liability will be imposed on an offending obligor.¹⁰⁹⁷ Russian civil law doctrine places heavy emphasis on the notion that the purpose of civil liability is to compensate the aggrieved party for his material losses; it is not to compensate for any moral injury that he may suffer as a result of breach of contract by the other party.¹⁰⁹⁸ An unwavering rule of Russian contract law is that damages for moral injury are not recoverable in commercial contract remedies.¹⁰⁹⁹ This contrasts sharply with U.S. law, which permits the recovery of damages for emotional distress as a result of a breach of contract.¹¹⁰⁰

Generally speaking, under the Code, the imposition of civil liability requires the concurrence of four conditions: unlawful conduct on the part of the offending party, the creditor is harmed, a causal connection between the unlawful conduct and the occurrence of harm and the offending party is at fault.¹¹⁰¹ In the context of a contractual relationship, unlawful conduct may take the form of nonperformance or improper performance of a contractual obligation. In other words, the mere fact that a

1093. *Id.*

1094. *Id.*

1095. The only form of punitive civil liability permitted in Russian contract law is punitive liquidated damages discussed in section XII(B)(2) *infra*.

1096. OSAKWE, *supra* note 20, at 140.

1097. See discussion of punitive liquidated damages in XII(B)(2) *infra*.

1098. See *id.*

1099. See *id.*

1100. ROHWER & SCHABER, *supra* note 6, at 266.

1101. OSAKWE, *supra* note 20, at 140.

contractual duty was breached is per se unlawful conduct.¹¹⁰² Such conduct is deemed unlawful in the sense that it breaches a general duty imposed by law, a duty to properly perform a contractual obligation undertaken freely and voluntarily.¹¹⁰³ Public policy requires that anyone who voluntarily enters into a contract must perform his obligations under such contract or else face the legal consequences of failing to do so.¹¹⁰⁴

Harm suffered as a result of breach of a civil obligation could be material or moral.¹¹⁰⁵ The requirement of harm as an element of civil liability is traditionally associated with tort liability, not with contractual liability.¹¹⁰⁶ For breach of contractual obligation, the Code permits recovery only for material loss (damages), never for moral injury (harm).¹¹⁰⁷ It is this fine point that sets apart recovery of damages in contract from compensation of damages in tort under the Code.¹¹⁰⁸ In tort law, damages may be sought under the Code both for material loss and for moral injury.¹¹⁰⁹ The rationale for denying recovery in contract for moral harm is that, according to the Code, the grounds for moral harm are the infliction of physical pain or mental anguish, both of which are absent in the case of breach of contract.¹¹¹⁰

1102. See C. Civ. art. 401 (Russ.).

1103. See *id.*

1104. See *id.*

1105. SUKHAREV, *supra* note 70, at 153.

1106. See Braginskii Contracts 1998, *supra* note 82, at 638.

1107. BRAGINSKII COMM., *supra* note 81, at 487.

1108. Compensation for moral harm in Russian tort law is permitted under several provisions of its Civil Code including, but not limited to articles 151-152, 1099-1101. C. Civ. arts. 151-152, 1099-1101 (Russ.).

1109. C. Civ. art. 1064 (Russ.). The general principle of tort liability for causing material as well as moral harm is in the Code. *Id.* In addition to Article 15, which regulates the compensation of material loss in contract and tort cases, Article 151 governs compensation of moral harm in tort cases. C. Civ. art. 151 (Russ.). Moral harm includes physical and mental suffering, for which this provision of the Civil Code permits monetary compensation. *Id.* Most importantly, compensation for moral harm is permitted under Russian law only in those instances specifically provided by law. *Id.* Subject to one exception, all of such instances (i.e., Articles 151, 152, 1100 of the Civil Code, Article 15 of the Law of the Russian Federation "On the Protection of the Rights of Consumers", Article 7 of the Law of the Russian Federation "On Petition to the Courts for a Review of Actions and Decisions that Violate the Rights and Freedoms of Citizens", etc.) deal with torts. BRAGINSKII COMM., *supra* note 81, at 71. The one notable exception is Article 15 of the Law "On the Protection of the Rights of Consumers", which permits compensation for moral harm suffered by a consumer in connection with the breach of certain types of consumer contract. See *id.*

1110. C. Civ. art. 150 (Russ.).

The general rule is that for an obligor to be liable for breach of contract, his conduct must be accompanied by fault.¹¹¹¹ In the absence of fault, there cannot be civil liability for breach of a contract.¹¹¹² Russian law, however, requires fault only in a breach of a consumer contract.¹¹¹³ If breach of contract occurred in the course of conduct of commercial transactions, liability shall arise regardless of fault.¹¹¹⁴

In other words, under Russian law, fault-based liability applies only to consumer transactions. For commercial transactions, the governing rule is one of strict liability.¹¹¹⁵ Against this backdrop, we will examine the specific rules of the Code relating to the following issues: grounds for civil liability and forms of civil liability, liability for specific types of breach of contract, grounds for release from civil liability, grounds for reduction of civil liability, and limitation of liability by a contractual stipulation.¹¹¹⁶

B. Grounds For and Specific Forms of Civil Liability

Article 401 of the Code denominates two specific grounds for civil liability, nonperformance and improper performance. Nonperformance is normally non-action, but could also be incomplete action.¹¹¹⁷ For example, a painter, who contracted to paint a portrait for a creditor, commenced painting, but, while painting, lost inspiration and did not complete the portrait. Consequently, he failed to deliver a finished product and, thus, failed to perform the obligation. Improper performance takes different forms, such as delivery of poor quality goods, poor construction and failure to make an installment payment on time.

Civil liability requires fault in consumer transactions.¹¹¹⁸ Fault may take one of three forms, intent (regardless of whether intent is specific or general), ordinary negligence, or gross negligence.¹¹¹⁹ The distinction in Russian criminal law between direct (specific)

1111. C. Civ. art. 401 (Russ.).

1112. *Id.*

1113. *Id.*

1114. *Id.*

1115. *Id.*

1116. The author adopted this structural approach as the best way to manage the discussion of this complex topic.

1117. See C. Civ. art. 401 (Russ.).

1118. *Id.*

1119. See *id.*

and general (indirect) intent¹¹²⁰ is not relevant in Russian civil law.¹¹²¹ Because the law presumes fault, the plaintiff does not have to prove it. Rather, the defendant bears the burden of showing lack of fault.¹¹²² In cases where liability does not require fault, the degree of fault is still important in determining damages.¹¹²³ In cases where strict liability applies, the burden falls upon the defendant to show that breach of contract is attributable to an insurmountable force.¹¹²⁴

The general rule under Russian law is that the party that breached a contractual duty shall be liable for his conduct.¹¹²⁵ There are two prominent situations, however, in which the law imposes liability on a third party for the breach of contract or vicarious liability.¹¹²⁶ First, if a principal debtor delegates a duty to a third party, the delegator shall be liable to the creditor for a breach by the delegatee.¹¹²⁷ Second, an employer is liable for the conduct of his employee.¹¹²⁸ The definition of employee includes persons working for an employer under a labor law contract or under a fixed-term employment contract. It also includes members of a production cooperative, partners in a general or limited partnership, and any members of a business organization who are authorized to act on behalf of the organization.¹¹²⁹

Russian doctrine¹¹³⁰ defines employee as a physical person employed by the employer, but does not include a sole proprietor

1120. C. CRIM. art. 25 (Russ.). The Russian Criminal Code stipulates that fault may take the form of intent of negligence. C. CRIM. art. 24 (Russ.). There are two forms of intent: specific (direct) and general (indirect). C. CRIM. art. 25 (Russ.). Negligence is classified into two forms: ordinary and gross. See C. CRIM. art. 26 (Russ.).

1121. See C. CIV. art. 401 (Russ.).

1122. OSAKWE, *supra* note 20, at 188.

1123. See GUEV COMM. ONE, *supra* note 8, at p. 646. Guev also cross-references to article 1083, which deals with its impact of the degree of fault in computing damages in tort law.

1124. *Id.*

1125. *Id.*

1126. See C. CIV. arts. 402, 403 (Russ.).

1127. C. CIV. art. 403 (Russ.). It should be noted in passing that under Russian law delegation of duty (*vozlozhenie ispolneniia obiazatelstva*) under Art. 403 is distinctly different from delegation of duty (*perevod dolga*) under Arts. 391, 392, which is discussed in Section IX(C) *supra*. Under Art. 403, the principal obligor merely entrusts performance of his duty to a third person without actually stepping out of the original obligation.

1128. C. CIV. art. 402 (Russ.).

1129. SADIKOV COMM. ONE, *supra* note 74, at 654.

1130. See generally GUEV COMM. ONE, *supra* note 8, at 648-49; SADIKOV COMM. ONE, *supra* note 74, at 654-55.

operating as an independent contractor.¹¹³¹ The principle of respondeat superior is based on the notion that an employee is an instrumentality and an extension of the employer.¹¹³² Nonperformance or improper performance of a contract by an employee is legally tantamount to nonperformance or improper performance by his employer.¹¹³³

The Code contemplates five forms of remedies for breach of contract.¹¹³⁴ These include damages, liquidated damages, payment of interests, forfeiture or doubling of earnest money and specific performance.¹¹³⁵ The first three remedies in this listing are generally referred to as Chapter 25 remedies, the latter two fall into the category of "other remedies."¹¹³⁶

1. Damages (*Ubytki*)

Damages are a form of universal remedy for breach of contract in that they may be combined with other remedies and may be imposed in any situation, regardless of whether the payment of damages is stipulated by law or contract.¹¹³⁷ To receive damages, the creditor must prove unlawful conduct on the part of the debtor, that he suffered a material loss, a causal connection between the debtor's unlawful conduct and the loss suffered and the amount of the loss suffered.¹¹³⁸ In computing damages, the amount sought may not exceed the amount that restores the creditor to where he would have been had the obligation been performed by the debtor.¹¹³⁹ In other words, Russian law does not

1131. GUEV COMM. ONE, *supra* note 8, at 648-49; see SADIKOV COMM. ONE, *supra* note 74, at 654-55.

1132. See C. CIV. arts. 1005, 420 (Russ.).

1133. C. CIV. art. 402 (Russ.).

1134. See C. CIV. arts. 330, 381, 393, 395-96 (Russ.).

1135. *Id.*

1136. These other remedies are governed by Code provisions located outside of Chapter 25. Russian civil law draws a subtle but significant distinction among the interlocking notions of *ubytki* (damages), *vred*, (harm/injury) and *ushcherb* (actual losses). BRAGINSKII COMM., *supra* note 81, at 489. Russian doctrine defines *ubytki* as the negative material consequences suffered by a victim as a result of an unlawful conduct. See *id.* By contrast, *ushcherb* (actual losses) is a component of *ubytki* (damages). *Id.* As far as the concept of *vred* (harm) is concerned, the sphere of its use is limited to tort liability. *Id.* If reference is to *vred* (harm) as a condition of liability, the Civil Code prefers to speak of the consequences of the violation of an obligation (See, for example, Article 333). *Id.*

1137. C. CIV. art. 394 (Russ.).

1138. OSAKWE, *supra* note 20, at 140. See also BRAGINSKII COMM., *supra* note 81, at 491.

1139. See C. CIV. art. 15 (Russ.).

permit punitive damages for breach of contract. Thus, the concept of restitution in U.S. law is built into the notion of lost profit under Russian law.¹¹⁴⁰

The definition of damages encompasses actual losses and lost profit, both of which are classified as direct damages.¹¹⁴¹ Actual losses, in turn, include expenses and loss of, or damage to, property.¹¹⁴² Specifically, actual losses include costs incurred by a creditor in obtaining from a third party performance of the non-performed or improperly performed, obligation.¹¹⁴³ For example, if a house is poorly constructed, the creditor may retain the services of a third party to correct the defects and charge the costs of such corrective work to the obligor.

Lost profits are any and all gains that the creditor would receive if the contract had been performed properly.¹¹⁴⁴ If, however, the debtor derived any gains from his breach of the obligation, the amount of lost profits may not be less than such gains received by the debtor.¹¹⁴⁵ Compensation for lost profits requires proof of a high degree of certainty and foreseeability.¹¹⁴⁶

In calculating lost profits, the creditor may include costs of measures undertaken for obtaining profit, as well as measures undertaken in preparation for making profit.¹¹⁴⁷ Although courts may take inflation into consideration, the prevailing price at the time when the obligation was to have been performed shall serve as the basis for any computation of lost profits.¹¹⁴⁸ If a judgment for damages is not paid in time, the court may increase the amount in a subsequent enforcement judgment.¹¹⁴⁹

1140. OSAKWE, *supra* note 20, at 140. Even though Russian contract law does not per se permit punitive damages, it tacitly endorses the notion of punitive compensation for breach of contract by permitting the recovery of full damages and liquidated damages in the same breach of contract. C. CIV. arts. 330, 394 (Russ.). See *infra* on the discussion of liquidated damages.

1141. OSAKWE, *supra* note 20, at 187. Russian contract law does not permit recovery for indirect damages. C. CIV. art. 15 (Russ.).

1142. OSAKWE, *supra* note 20, at 187.

1143. C. CIV. art. 397 (Russ.).

1144. BRAGINSKII COMM., *supra* note 81, at 490.

1145. *Id.*

1146. See *id.* at 493.

1147. *Id.*

1148. *Id.* at 490.

1149. *Id.*

As a general rule, Russian law does not permit recovery for moral harm suffered as a result of the breach of contract.¹¹⁵⁰ This general rule, however, refers only to commercial contracts.¹¹⁵¹ A consumer is entitled to compensation for moral harm suffered as a consequence of breach of certain types of contracts.¹¹⁵² Recovery for such moral harm in addition to any compensation he may have received for material loss caused by the same breach of contract.¹¹⁵³

2. Liquidated Damages (*Neustoika*)

The punitive, deterrent and educational functions of Russian law of contract remedies are fully reflected in the rules governing liquidated damages.¹¹⁵⁴ There are four distinct types of liquidated damages: discounted, alternative, exclusive and punitive.¹¹⁵⁵ The general rule is that unless the parties specifically stipulate any one of the other forms of stipulated damages, the discounted form of stipulated damages shall apply.¹¹⁵⁶ Regardless of the form of stipulated damages selected by the parties, a court has discretion to reduce the amount of stipulated damages if it determines that the stipulated amount is not commensurate with the losses suffered by the creditor.¹¹⁵⁷

A peculiar feature of Russian contract law is that liquidated damages may be collected in addition to damages (punitive liquidated damages) or in combination with actual damages (discounted liquidated damages).¹¹⁵⁸ For example, if the amount of direct damages is determined to be 10,000 rubles and the parties stipulated liquidated damages in the amount of 25,000 rubles, a court would permit the plaintiff to recover from the breaching party either 35,000 rubles (i.e., full direct damages plus the full amount of the stipulated damages) or 15,000 rubles (i.e., the amount left from the liquidated damages after discounting the

1150. *Id.* at 487.

1151. *Id.*

1152. Article 15 of the 1992 Federal Law "On the Protection of the Rights of Consumers."

1153. *Id.*

1154. C. CIV. arts. 330, 394 (Russ.). See generally BRAGINSKII COMM., *supra* note 81, at 495-99; OSAKWE, *supra* note 20, at 187.

1155. See C. CIV. art. 394 (Russ.); see also BRAGINSKII COMM., *supra* note 81, at 496.

1156. See BRAGINSKII COMM., *supra* note 81, at 496.

1157. *Id.* at 497.

1158. *Id.* at 496.

amount of the direct damages). If the contract stipulated liquidated damages as the exclusive remedy, the plaintiff would recover only 25,000 rubles. If, however, the contract stipulated liquidated damages as an alternative to direct damages, the plaintiff would have the choice of recovering either 25,000 rubles or only 10,000 rubles.

To collect liquidated damages, the creditor does not have to prove that he suffered loss, or the amount of loss suffered.¹¹⁵⁹ The openly acknowledged purposes of liquidated damages include deterrence and punishment of breach of contract; two purposes that would render a liquidated damages clause in a U.S. contract void.¹¹⁶⁰

3. Payment of Interest

A third specific form of civil liability under Russian contract law is the exaction of interest in the event of breach of a monetary obligation.¹¹⁶¹ There is debate among Russian civil law scholars as to whether interest paid on breach of a monetary obligation is a separate form of civil liability, if it is just another form of payment for the use of funds of another person or if it is a form of damages for breach of a monetary obligation.¹¹⁶² Case law tends to favor the position that it is a separate form of civil liability.¹¹⁶³ As a form of civil liability, interest paid on the breach of a monetary obligation, like liquidated damages, operates in direct relation to damages.¹¹⁶⁴ Damages for breach of a monetary obligation are paid only in the amount by which they exceed interest.¹¹⁶⁵

A party that fails to perform or improperly performs a monetary obligation is liable for interest to the creditor.¹¹⁶⁶ Breach of a monetary obligation may take the form of unlawful withholding of funds, failure to return funds to the lawful owner after demanding their return, failure to pay money owed in time and failure to deliver funds to a third party on the instructions of the creditor.¹¹⁶⁷ In all of these cases the obligor shall, in addition to

1159. BRAGINSKII COMM., *supra* note 81, at 497. See also C. CIV. art. 330 (Russ.).

1160. BRAGINSKII COMM., *supra* note 81, at 495-99.

1161. *Id.* at 499-508.

1162. BRAGINSKII COMM., *supra* note 81, at 501-02.

1163. See *id.* at 500-01.

1164. See generally *id.* at 499-508.

1165. *Id.* at 500.

1166. *Id.* at 500-08.

1167. *Id.* at 500.

returning the amount owed, pay interest on the amount owed.¹¹⁶⁸ The amount of interest payable shall be determined by the prevailing interest rate at the place of residence of the creditor on the day of performance of the obligation.¹¹⁶⁹ If the creditor is a legal entity, its registered seat shall be the controlling factor in determining the amount of interest due.¹¹⁷⁰ If interest is to be paid based on a court decision, the creditor may request the court to compute the amount of interest based on the rate in effect on the day the lawsuit was filed or on the day of the judgment.¹¹⁷¹

4. Other Remedies

Another form of remedy under Russian law is forfeiture or doubling of earnest money.¹¹⁷² A party that secures the performance of a contract with earnest money shall forfeit his security payment in the event of his breach of the contract.¹¹⁷³ If the party receiving the earnest money is responsible for nonperformance of the contract, he shall pay the other party double the amount of the earnest money.¹¹⁷⁴ Specific performance is also an available remedy.¹¹⁷⁵ The availability of specific performance as an additional remedy for breach of contract depends on whether the breach resulted from improper performance or nonperformance of the contract.¹¹⁷⁶ In the event of improper performance of an obligation, payment of damages and/or liquidated damages does not release the obligor from performance of the obligation in kind.¹¹⁷⁷ There may, however, be situations in which further performance in kind of an improperly performed obligation is not possible.¹¹⁷⁸ In that case, payment of damages and/or liquidated damages shall release the obligor from specific performance.¹¹⁷⁹ Also, in the event of nonperformance of an obligation, payment of damages and/or liquidated damages

1168. *Id.*

1169. *Id.* at 500.

1170. *Id.*

1171. *Id.*

1172. C. Civ. art. 381 (Russ.).

1173. *Id.*

1174. *Id.*

1175. C. Civ. art. 396 (Russ.); *see generally* BRAGINSKII COMM., *supra* note 81, at 508-10.

1176. C. Civ. art. 396 (Russ.); *see also* BRAGINSKII COMM., *supra* note 81, at 508-10.

1177. C. Civ. art. 396 (Russ.); *see also* BRAGINSKII COMM., *supra* note 81, at 510.

1178. *See* BRAGINSKII COMM., *supra* note 81, at 510.

1179. *See id.*

shall release the obligor from specific performance.¹¹⁸⁰

Unlike the three Chapter 25 remedies discussed above, which operate *in rem*, specific performance operates *in personam*.¹¹⁸¹ For this reason, specific performance will only be awarded where the payment of damages would be an inadequate remedy.¹¹⁸² Courts apply three tests in determining whether to order specific performance: (1) the adequacy test – will the payment of money be an adequate substitute for specific performance; (2) the effectiveness test – will the payment of damages be an effective substitute for performance; and (3) the possibility test – is performance of the contract impossible under the given circumstances.¹¹⁸³ If any of the three tests is answered affirmatively a court will not order specific performance.¹¹⁸⁴ Specific performance would require that a contract be performed in accordance with the precise conditions and in the exact form agreed to by the parties.¹¹⁸⁵ All the instances in which the Russian Code contemplates specific performance deal with the delivery of goods.¹¹⁸⁶ None deals with the performance of personal services.¹¹⁸⁷ A mandatory injunction to compel specific performance of a personal services contract would be tantamount to involuntary servitude and constitutionally impermissible.¹¹⁸⁸ In such cases, the interests of the creditor would be adequately served by awarding Chapter 25 remedies.

An obligor is released from specific performance in two other situations.¹¹⁸⁹ He may be released as a result of accord and satisfaction reached between the creditor and debtor¹¹⁹⁰ and where the creditor loses interest in the obligation as a result of delay in performance.¹¹⁹¹ This rule is dispositive, not

1180. *Id.*

1181. *See id.*

1182. *See* C. Civ. arts. 12, 396 (Russ.).

1183. *Id.*

1184. *Id.*

1185. *Id.*

1186. C. Civ. arts. 518-21 (Russ.).

1187. *Id.*

1188. Article 21 of the Russian Constitution recognizes the right of all persons to human dignity that may not be abridged under any circumstance. Russ. Const. Art. 21. Involuntary servitude does violence to any citizen's constitutional right under Article 21. *Id.*

1189. C. Civ. art. 396 (Russ.).

1190. C. Civ. art. 409 (Russ.).

1191. C. Civ. art. 405 (Russ.).

imperative.¹¹⁹² Therefore, it could be modified by law in specific instances or by contract between the parties.¹¹⁹³ For example, payment of damages for nonperformance by the seller of an obligation under a retail sale contract shall not release the seller from specific performance.¹¹⁹⁴

From the standpoint of comparative law, the Russian rule that is described in the foregoing paragraphs differs substantially from the German or the French rule.¹¹⁹⁵ Surprisingly, the Russian rule resembles the U.S. rule as codified in the U.C.C.¹¹⁹⁶ Like the U.C.C., the Russian rule employs the "adequacy test," which neither the German nor the French rule recognizes.¹¹⁹⁷ Moreover, neither rule permits a court to compel the performance of a personal services contract.¹¹⁹⁸ The French and German rules do not make similar blanket exemptions.¹¹⁹⁹ Whereas specific performance is a routine remedy under the German and French rules, it is granted only in exceptional situations under the U.C.C. and Russian rules.¹²⁰⁰

The judicial enforcement of a judgment for specific performance under the Russian system, however, lacks the effectiveness of the U.S. system, where the courts may invoke their power of contempt, and the decisiveness of the German system, where a court may impose criminal punishment (in the form of imprisonment and/or monetary fines) on a reluctant defendant.¹²⁰¹ The Russian mechanism for enforcing an order for specific performance resembles the toothless French concept of *astreinte*, a form of private punishment.¹²⁰²

An obligor who is late in performance of an obligation shall be liable to the creditor for any losses suffered as a result of such delay, as well as for any consequences of an impossibility of performance that may occur during the delay.¹²⁰³ There is a subtle

1192. See C. Civ. art. 396 (Russ.).

1193. *Id.*

1194. C. Civ. art. 505 (Russ.).

1195. ZWEIGERT & KOTZ, *supra* note 23, at 295.

1196. UCC 2-716.

1197. ZWEIGERT & KOTZ, *supra* note 23, at 295.

1198. *Id.*

1199. *Id.*

1200. For a concise comparison of the German, French and UCC rules on specific performance see ZWEIGERT & KOTZ, *supra* note 23, at 157-176.

1201. ZWEIGERT & KOTZ, *supra* note 23, at 295.

1202. See generally ZWEIGERT, *supra* note 23.

1203. C. Civ. art. 405 (Russ.).

distinction between delayed performance and defective on-time performance, both of which qualify as improper performance.¹²⁰⁴ For delay in performance, the obligor is liable to the creditor both for actual losses suffered as well as for lost profit. If, as a result of the delay in performance, further specific performance of the obligation becomes impossible, the obligor shall be liable to the creditor for any consequences of such impossibility of performance. Also, during such delay, the creditor may lose interest in any further performance of the obligation. In this case, the creditor has the right to refuse to accept further performance and demand compensation for his losses.

A creditor is liable for delay in performance in several circumstances. For example, he is liable for refusing to accept a proper performance offered by an obligor, or for failing to perform an act required by law or contract if the performance of such act is required in order for the obligor to perform his duty under the obligation, or for accepting proper performance and then failing to deliver to the obligor a receipt testifying to the fact that performance was received. Delay in performance by a debtor gives the obligor one of several rights. For example, the debtor may withhold performance under the obligation,¹²⁰⁵ or may seek payment of damages¹²⁰⁶ or may refuse to pay interests on a monetary obligation.¹²⁰⁷ Refusal by a creditor to accept an improper performance does not constitute delayed performance.¹²⁰⁸

While on the topic of "Other Remedies," it is important to comment briefly on "injunctive relief" (i.e., mandatory injunction) that is mentioned in Article 398. The rule states that the creditor has the right to file suit to compel a transfer if the debtor fails to perform.¹²⁰⁹ This procedure requires three steps: (1) filing of a

1204. *Id.*

1205. C. Civ. art. 408 (Russ.).

1206. C. Civ. art. 406 (Russ.).

1207. *Id.*

1208. See discussion of public contract remedies in section G-1 above. The remedy contemplated for refusal by an obligated party to sign a public contract is not technically a remedy for breach of contract. C. Civ. art. 426 (Russ.). Article 426 directs the court to enjoin a reluctant party to sign a contract. *Id.* If, however, a public contract was concluded between the parties but on discriminatory terms, the aggrieved party may seek injunction for specific performance of the contract on non-discriminatory terms. See discussion in section G-1.

1209. C. Civ. art. 398 (Russ.).

lawsuit; (2) judgment by a court in favor of the creditor; and (3) enforcement of that judgment by a court bailiff.¹²¹⁰

In Russian legal literature, two questions are raised in connection with this provision: whether injunctive relief is a separate form of civil liability and whether Article 398 is applicable only to individually defined things.¹²¹¹ The uniform answer to the first question is that injunctive relief is not a separate form of civil remedy for breach of contract.¹²¹² On the second question, Russian case law holds that Article 398 may be used to compel the transfer of a thing that is not individually defined.¹²¹³ If a thing has generic qualities, but can be individually identified by the parties or by a court (e.g., a specific thing located in a warehouse belonging to the debtor), its transfer to the creditor may be compelled by a court pursuant to Article 398.¹²¹⁴

C. Grounds For Release From, Reduction of and Limitation of Civil Liability

The Code spells out three specific grounds for releasing an obligor from civil liability for breach of contract. These are lack of fault, insurmountable force and delay in performance by a creditor.¹²¹⁵ The three grounds relate to three different circumstances. The first relates to situations in which fault is required for civil liability. The general rule in Russian contract law is that if fault is required as a prerequisite for civil liability, it is presumed to exist by operation of law.¹²¹⁶ The burden of showing absence of fault lies squarely on the defendant.¹²¹⁷ In such cases, the ground for release of the obligor from liability is absence of fault.¹²¹⁸ Thus, the plaintiff does not bear the burden of proving fault.¹²¹⁹

1210. SADIKOV COMM. ONE, *supra* note 74, at 649.

1211. *Id.* at 650; BRAGINSKII COMM., *supra* note 81, at 511.

1212. BRAGINSKII COMM., *supra* note 81, at 511. According to Braginskii, "the measures contemplated in Articles 397-398 of the Civil Code are sanctions for the violation of obligations; by their nature, however, they cannot be put in the category of forms of civil liability" (my translation). *Id.*

1213. *See* SADIKOV COMM. ONE, *supra* note 74, at 650.

1214. *See id.*

1215. C. CIV. arts. 401, 406 (Russ.). *See generally* BRAGINSKII COMM., *supra* note 81, at 527-35; OSAKWE, *supra* note 20, at 189.

1216. BRAGINSKII COMM., *supra* note 81, at 527.

1217. *See id.*

1218. *See id.* at 527-28.

1219. *See id.*

The second ground relates to circumstances in which fault is not required for civil liability for breach of a contract. In such instances, the principle of strict liability operates.¹²²⁰ Here, the defendant may avoid liability only if he shows that breach of contract occurred as a result of an insurmountable force.

This is not quite the same thing as *force majeure* as understood traditionally in U.S. law.¹²²¹ Article 401 excludes from the meaning of insurmountable force factors events such as shortage of goods necessary for performance, breach of contract by the debtor's contracting partner or financial hardship being experienced by the obligor.¹²²²

The third ground relates to delay in performance by the creditor discussed previously.¹²²³ Article 401 stipulates two forms of fault: intent and negligence.¹²²⁴ As noted above, doctrine has refined this provision to mean three forms of fault: intent (regardless of whether intent was specific or general), ordinary negligence and gross negligence.¹²²⁵ Article 401 negatively defines fault by defining what does not constitute fault. A person is deemed not at fault if, by the degree of care and caution that was required of him by the nature of the obligation and conditions of commerce, he took all necessary measures for the proper performance of the obligation.¹²²⁶

If we reverse the definition of fault under Article 401, a direct definition of fault would look like this: fault is the failure to take all necessary measures for the proper performance of an obligation as measured by the degree of care and caution required by the nature of the obligation and conditions of commerce.

Whether a person is at fault is a question of fact, the determination of which varies from case to case. The form of fault is irrelevant in determining whether there is civil liability. For this purpose, any form of fault will suffice. The form of fault, however, is relevant in two respects. First, the amount of compensation for damages depends on whether fault was intentional or negligent.¹²²⁷ Second, for purposes of reducing the amount of

1220. See *id.* at 527-35.

1221. See *id.*

1222. C. CIV. art. 401 (Russ.).

1223. C. CIV. art. 406 (Russ.).

1224. C. CIV. art. 401 (Russ.).

1225. BRAGINSKII COMM., *supra* note 81, at 527.

1226. C. CIV. art. 401 (Russ.).

1227. See BRAGINSKII COMM., *supra* note 81, at 527.

compensation payable to the obligor, the contributory fault of the creditor must be in the form of gross negligence, not ordinary negligence.¹²²⁸

If prior to the breach of contract the parties agreed to release the obligor from civil liability for intentional breach of contract, such agreement is deemed void under Article 401.¹²²⁹ If such agreement relates to a negligent breach of contract, it is deemed valid.¹²³⁰ Also, if an agreement is reached between the parties after the breach of contract has occurred to release the obligor from liability for intentional or negligent breach of contract, the agreement is valid.¹²³¹

The principle of presumption of fault in Russian civil law deserves special attention. It is embedded in Article 401 (with regard to breach of contract) and in Article 1064 (with regard to tort liability).¹²³² In both situations, the plaintiff does not have to prove fault on the part of the obligor (the party that breached contract or the tortfeasor).¹²³³ The law reverses the traditional burden of proof by calling upon the defendant to show lack of fault.¹²³⁴

Curiously, in Article 10, the presumption is reversed.¹²³⁵ Here, the rule is that, in cases when a statute makes civil law rights dependent upon whether these rights were exercised reasonably and in good faith, the reasonableness of actions and good faith of the participant in civil law relations shall be presumed.¹²³⁶ One wonders why the Code presumes reasonableness and good faith in Article 10, but presumes fault (guilt) in Articles 401 and 1064.¹²³⁷

The principle of strict liability for breach of commercial contracts in Article 401 is consistent with the principle of strict liability for commercial tort in Article 1064.¹²³⁸ In both cases, a merchant can avoid liability by showing that the breach is

1228. *Id.*

1229. *Id.*

1230. *Id.*

1231. *Id.*

1232. C. CIV. arts. 401, 1064 (Russ.).

1233. BRAGINSKII COMM., *supra* note 81, at 527-35.

1234. *Id.*

1235. *Id.*

1236. *Id.*

1237. *Id.*

1238. *Id.* See also C. CIV. arts. 401, 1064 (Russ.).

attributable to an insurmountable force.¹²³⁹ There is disagreement, however, among Russian commentators¹²⁴⁰ as to the meaning of insurmountable force. Specifically, the issue is whether it has the same meaning as traditional *force majeure* in Western law.¹²⁴¹

Under Article 401, in order to qualify as an insurmountable force, two factors must be present: extraordinary character of the event and the occurrence of the event that does not in any way depend on the will of the parties and, thus, is out of the parties' control.¹²⁴² Thus, Russian civil law doctrine uniformly interprets the Code's meaning of insurmountable force to include war, epidemic outbreak of disease, earthquake, volcanic eruption, flood, tornado and revolution.

Certain phenomena that do not qualify as insurmountable force are specifically enumerated in Articles 9 and 401.¹²⁴³ Russian doctrine is divided on the issue of whether the following social phenomena qualify as insurmountable force - industrial actions, governmental actions and unlawful actions by third parties.¹²⁴⁴

Professor Sadikov regards massive strikes and governmental actions as insurmountable force.¹²⁴⁵ By contrast, Professor Guev thinks that the social phenomena listed above do not qualify as insurmountable force.¹²⁴⁶ Russian case law is unsettled on this point, but Professor Sadikov's view reflects the majority opinion among Russian civil law scholars.¹²⁴⁷ In reaching his conclusion, however, Professor Sadikov incorrectly equates "insurmountable force" in Article 401 with traditional *force majeure*.¹²⁴⁸ By contrast, in reaching his minority conclusion, Professor Guev correctly points out that "insurmountable force" in Article 401 is

1239. BRAGINSKII COMM., *supra* note 81, at 527-35.

1240. Professor Sadikov interprets "insurmountable force" expansively to include force majeure (acts of nature) and social phenomena. SADIKOV COMM. ONE, *supra* note 74, at 659. By contrast, Professor Guev interprets insurmountable force as being synonymous with force majeure. GUEV COMM. ONE, *supra* note 8, at 648.

1241. SADIKOV COMM. ONE, *supra* note 74, at 654; GUEV COMM. ONE, *supra* note 8, at 648.

1242. GUEV COMM. ONE, *supra* note 8, at 648.

1243. *Id.*

1244. SADIKOV COMM. ONE, *supra* note 74, at 654; GUEV COMM. ONE, *supra* note 8, at 648.

1245. SADIKOV COMM. ONE, *supra* note 74, at 654.

1246. GUEV COMM. ONE, *supra* note 8, at 648.

1247. See SADIKOV COMM. ONE, *supra* note 74, at 654.

1248. *Id.*

not the same thing as traditional *force majeure*.¹²⁴⁹

The meaning of insurmountable force in Article 401 is more expansive than the traditional meaning of *force majeure* in U.S. law. In U.S. law, the term *force majeure*, which is synonymous with "act of God," refers to a superior or irresistible force, an act occasioned exclusively by forces of nature without the interference of any human agency.

The three grounds for the reduction of compensation for civil liability are as follows: the fault of the creditor contributed to the nonperformance or improper performance of the obligation by the obligor; the intentional or negligent act of the creditor contributed to an increase in the amount of damages caused by the nonperformance or improper performance of the obligation by the debtor; and failure by the creditor to take reasonable measure to reduce the damages caused by nonperformance, or improper performance, of the obligation by the obligor.¹²⁵⁰

Under the rule in Article 404, if fault on the part of the creditor contributed to the non-performance or improper performance of the obligation by the obligor, the court is required to reduce the amount of compensation payable to the creditor.¹²⁵¹ The amount by which compensation shall be reduced depends on the circumstances of each case.

By contrast, if the contributory fault (intent or negligence) of the creditor relates to an increase in the losses, the court is not mandated to reduce the amount of compensation payable to the creditor, but may do so at its discretion.¹²⁵² The same discretion is granted to the court when the creditor fails to take reasonable measures to reduce anticipated damages.¹²⁵³ The rule applies equally to situations in which fault is required for liability, as well as to situations of strict liability.¹²⁵⁴

The rule governing the limitation of liability by law or by a contractual stipulation is engraved in Article 400 of the Code.¹²⁵⁵ A close reading of this rule indicates that it is slanted in favor of the consumer.¹²⁵⁶ The provision of Article 400 should be read in

1249. GUEV COMM. ONE, *supra* note 8, at 648.

1250. C. CIV. art. 404 (Russ.); *See also* OSAKWE, *supra* note 20, at 189.

1251. C. CIV. art. 404 (Russ.); BRAGINSKII COMM., *supra* note 81, at 533, 534.

1252. C. CIV. art. 404 (Russ.); BRAGINSKII COMM., *supra* note 81, at 533, 534.

1253. C. CIV. art. 404 (Russ.); BRAGINSKII COMM., *supra* note 81, at 533, 534.

1254. C. CIV. art. 404 (Russ.).

1255. C. CIV. art. 400 (Russ.).

1256. *Id.*

conjunction with the "Law on the Protection of the Rights of Consumers,"¹²⁵⁷ which fleshes out the governing federal law on consumer protection. Article 400 provides that with regard to certain types of obligations, liability may be limited by statute.¹²⁵⁸

The law, however, confines the possibility of limitation of liability by agreement of the parties to commercial transactions. Specifically, Article 400 states that in any other contract in which the creditor is a citizen-consumer, any provision by which the liability of the debtor is limited is void if the limit of liability for this particular type of obligation, or breach of obligation is established by law and if the agreement on the limitation of liability was concluded before the liability for nonperformance or improper performance of the obligation.¹²⁵⁹

In Russian case law and civil law doctrine¹²⁶⁰ the provisions of Article 400 are interpreted as follows: the imperative norm in Article 400 means that liability may be limited only by statute and not by any other legal norm; statute may limit liability not only for certain categories of obligations, but also for obligations connected with certain categories of activities (one such example is contained in Article 107, which statutorily limits the liability of members of a production cooperative); statutory limitation of liability may take one of several forms, such as limitation on the amount of damages that may be paid after liquidated damages have been paid by a debtor, limitation of damages to only actual damages by excluding payment of lost profit, by limiting liability to the full extent of the contributions of a member in a limited liability company or of a limited partner in a limited partnership, by limiting liability to a fixed amount such as limiting the liability of a bank guaranty to the amount stipulated in the letter of credit as provided in Article 377 of the Code.¹²⁶¹

An adhesion contract is specifically regulated under Article 428 of the Code. The blanket rule under Article 400 is that any provision in an adhesion contract that limits liability of the debtor is void.¹²⁶² Any other provision that limits debtor liability is also

1257. Law of the Russian Federation of February 7, 1992 • 2300-1 "On the Protection of the Rights of Consumers".

1258. C. CIV. art. 400 (Russ.).

1259. *Id.*

1260. See generally SADIKOV COMM. ONE, *supra* note 74, at 651-52; GUEV COMM. ONE, *supra* note 8, at 643-45.

1261. C. CIV. art. 377 (Russ.).

1262. C. CIV. art. 400 (Russ.).

deemed void if the creditor is a citizen-consumer.¹²⁶³ Article 400 requires that the creditor be a citizen-consumer and not a citizen-sole proprietor.¹²⁶⁴ This reading of Article 400 is backed up by the provision of Article 23 that states a citizen (natural person) who conducts business as a sole proprietor is subject to the rules governing commercial transactions by legal entities.¹²⁶⁵ To invoke the rule under Article 400, there must be a concurrence of three requirements: the character of the creditor as a citizen-consumer; the existence of a statutory rule which establishes the scope of liability for obligation of this type; and the agreement to limit liability preceded the occurrence of events which created the liability.¹²⁶⁶

To the provisions of Article 400 should be added the rule under Article 401 according to which an agreement for releasing a debtor from liability or limiting his liability for an intentional breach of an obligation is void if concluded in advance.¹²⁶⁷ The difference between the rules in Articles 400 and 401 is that the latter is directed specifically at the release from, or limitation of, liability for an intentional breach of contract.¹²⁶⁸

D. Election: Tort or Contract Remedies

Where facts permit, it would seem logical to allow the plaintiff to elect to bring his action in either tort or contract. The Russian solution to this problem is a three-part general rule with three exceptions.¹²⁶⁹ The general rule is that a plaintiff must sue in contract in the following three situations: if harm is caused to the property of a physical person as a result of nonperformance or improper performance of contract, if any type of harm (material or moral) is caused to a legal person as a result of nonperformance or improper performance of contract and if bodily harm is caused to an individual as a result of nonperformance of contract.¹²⁷⁰ In the following three situations Russian law grants the plaintiff the choice of an action in tort or contract:¹²⁷¹ if bodily harm is caused

1263. *Id.*

1264. *Id.*

1265. C. CIV. art. 23 (Russ.).

1266. GUEV COMM. ONE, *supra* note 8, at 644-45.

1267. C. CIV. art. 401 (Russ.).

1268. *Id.*

1269. SUKHANOV 2(2), *supra* note 83, at 365.

1270. *See id.*

1271. *See id.*

to an individual as a result of improper performance of contract;¹²⁷² if bodily or property harm is caused to an individual as a result of a defective product;¹²⁷³ and if harm is caused to the property of a legal person as a result of a defective product.¹²⁷⁴ Under this Russian rule, the test for deciding whether to grant the plaintiff an election between tort and contract remedies is not solely whether the tort occurred as a result of nonfeasance or malfeasance; rather the law looks also to the nature of the harm caused and the character of the plaintiff. When given the choice, the Russian plaintiff typically elects to sue in tort and not in contract.

XIII. TERMINATION AND MODIFICATION OF CONTRACT: EXCUSE AND DISCHARGE OF CONTRACTUAL DUTIES

A. General Principles

The essence of a contract lies in the parties' intentions to properly perform their obligations. Proper performance of a contract terminates the obligation.¹²⁷⁵ Termination of a contract is the final phase of a contract;¹²⁷⁶ all legal relations between the contracting parties are extinguished. The termination of a contract term does not per se terminate the obligations of the parties, unless the contract itself stipulates otherwise.¹²⁷⁷ Also, where there is a principal contract and an ancillary contract, the general rule is that the termination of the principal contract automatically terminates the ancillary contract.¹²⁷⁸ The reverse, however, is not always the case.¹²⁷⁹ The termination of an ancillary contract does not automatically terminate a principal contract.¹²⁸⁰

These twin principles of modern Russian contract law were reaffirmed in the Supreme Arbitration Court of the Russian Federation's opinion dated January 30, 1995, that held that the expiration of the term of a contract does not terminate the

1272. See C. CIV. arts. 580, 800, 1084 (Russ.).

1273. See C. CIV. art. 1095 (Russ.).

1274. See *id.*

1275. C. CIV. art. 408 (Russ.).

1276. BRAGINSKII COMM., *supra* note 81, at 536.

1277. C. CIV. art. 407 (Russ.).

1278. SADIKOV COMM. ONE, *supra* note 74, at 658-59.

1279. *Id.*

1280. *Id.*

obligations of parties under the contract unless law or contract provides otherwise.¹²⁸¹ In the same opinion, the Court ruled that a secondary obligation that secures the principal obligation is terminated by virtue of the fact that the term of the primary contract has expired.¹²⁸²

Under Russian law, a contractual obligation may be terminated in full or in part on any ground stipulated by law or contract.¹²⁸³ A common method for termination of a contract is agreement by the parties.¹²⁸⁴ In effect, an agreement by the parties to terminate an existing contract is a contract in itself under the general definition of a contract.¹²⁸⁵ In certain instances specified by law or contract, a contract may be terminated at the demand of one of the parties.¹²⁸⁶ The Code also recognizes certain legal acts as constituting grounds for the termination of a contract.¹²⁸⁷

The Code contemplates two forms for termination of a contract: complete and partial.¹²⁸⁸ Complete termination is possible in all situations.¹²⁸⁹ By contrast, partial termination of a contract is possible only if the contract is divisible into autonomous parts.¹²⁹⁰ For example, a contract for the supply and delivery of goods to the buyer's warehouse by a transportation mode to be provided by the seller is severable into two autonomous parts: supply of goods and delivery of goods. The part of the contract dealing with delivery of goods may be terminated, while the part on supply of goods continues.

If any one of the grounds listed in Chapter 26 of the Code exists, a party to a contract need not do anything in order to terminate the contract.¹²⁹¹ Also, the existence of any one of these facts does not need any additional support to constitute grounds

1281. C. Civ. Ann., *supra* note 55, at 321.

1282. *Id.*

1283. C. Civ. art. 407 (Russ.).

1284. C. Civ. art. 452 (Russ.).

1285. C. Civ. art. 420 (Russ.).

1286. C. Civ. art. 407 (Russ.).

1287. C. Civ. art. 407 (Russ.). Such legal acts are regulated by Chapter 26 of the Code. C. Civ. arts. 407-19 (Russ.). In addition to Chapter 26, rules governing the termination of contracts are in Chapter 29, which deals with the modification and dissolution of contract. C. Civ. arts. 450-53 (Russ.).

1288. C. Civ. art. 407 (Russ.).

1289. *Id.*

1290. *Id.*

1291. C. Civ. arts. 407-19 (Russ.).

for the termination of a contract.¹²⁹² If, however, a lawsuit is filed to contest any of these grounds, the court's role is to corroborate the alleged fact to declare the contract terminated.¹²⁹³ The text of Article 407 suggests that the parties to a contract may also stipulate other grounds for termination.¹²⁹⁴

Article 407 specifically states that a party may unilaterally request a court to terminate a contract only in the instances permitted by law or contract.¹²⁹⁵ The general rule in Article 407 applies to contracts in Article 450, where one party may request that the contract be terminated by a court's decision only in the event of a breach of the contract by the other party, or in other cases permitted by law or contract.¹²⁹⁶ At this point, the grounds for terminating a contract must be separated from the grounds for modification and dissolution of a contract and analyzed sequentially.

B. Termination of Contract

Chapter 26 of the Code lists ten separate legal facts, each of which may constitute grounds for the termination of a contract.¹²⁹⁷ These are proper performance, accord and satisfaction, set-off, merger of debtor and creditor in one person, novation, remission of debt, impossibility of performance, supervening act of a state agency, death of a citizen (natural person) and liquidation of a legal person.¹²⁹⁸ In addition to the foregoing legal facts, other factual grounds for the termination of a contract may be stipulated by other laws or by the contract itself.¹²⁹⁹ Against this backdrop, let us examine each of the Chapter 26 legal facts in detail.

Under Article 408, the debtor's proper performance terminates the obligation.¹³⁰⁰ In some situations, proper performance is evidenced by specific documents emanating from the creditor or by the actions of the creditor.¹³⁰¹ Upon proper performance, the debtor can demand a receipt evidencing

1292. *Id.*

1293. *Id.*

1294. C. Civ. art. 407 (Russ.).

1295. *Id.*

1296. C. Civ. art. 450 (Russ.).

1297. C. Civ. arts. 409-10, 412-19 (Russ.).

1298. *Id.*

1299. C. Civ. art. 407 (Russ.).

1300. C. Civ. art. 408 (Russ.).

1301. *Id.*

performance.¹³⁰² If the creditor possesses any document that evidences the debtor's obligation, the document shall be returned to the debtor at that time.¹³⁰³ Failure by the creditor to issue a receipt or return documentary evidence of an obligation to the debtor grants the debtor the right to withhold performance.¹³⁰⁴ In fact, such action by the creditor may be viewed as delayed performance and subject to the consequences of Article 406.¹³⁰⁵

The general rules governing the performance of contract are set forth in Articles 309-328.¹³⁰⁶ The rules in Articles 309 and 310 deserve special attention. According to Article 309, "obligations must be performed in the proper manner in accordance with the conditions of the obligation and the requirements of the law, other legal acts, and in the absence of such conditions and requirements—in accordance with business custom or other generally accepted requirements."¹³⁰⁷ Under Article 310, a party to a contract may not unilaterally refuse to perform its obligations under the contract or unilaterally alter the terms of the contract, except in instances permitted by law.¹³⁰⁸ The second sentence in Article 310 modifies this general rule as follows: if the contract in question is a commercial contract, as opposed to a consumer contract, any party thereto can unilaterally refuse to perform the contract, as well as unilaterally alter the terms of the contract, if the contract itself so permits and law or the nature of the obligation does not otherwise indicate.¹³⁰⁹ Citing the provisions of Article 424 of the Code, the Supreme Arbitration Court of the Russian Federation in its Letter • C-1-7/OP – 159 of March 20, 1995 entitled "Review of Practice Relating to the Settlement of Disputes Connected with the Setting and Application of Prices" ruled that a party to a commercial contract can unilaterally alter the price stipulated in the contract if the price fixed by a government order for products to be supplied under the contract went up after the contract was concluded.¹³¹⁰

1302. *Id.*

1303. *Id.*

1304. *Id.*

1305. C. Civ. art. 406 (Russ.).

1306. C. Civ. arts. 309-28 (Russ.).

1307. C. Civ. art. 309 (Russ.).

1308. C. Civ. art. 310 (Russ.).

1309. *Id.*

1310. C. Civ. art. 424 (Russ.).

Performance of an obligation shall be deemed proper only if the proper person, performs in the proper manner, to the proper person, at the proper place, with the proper object and at the proper time.¹³¹¹ Article 312 provides that the debtor bears the risk of performance to the proper person.¹³¹² Typically, the creditor is the proper person to receive performance of an obligation.¹³¹³ The creditor may, however, authorize a third person to receive performance.¹³¹⁴ Also, typically, the debtor performs the obligation, but performance may be delegated by the debtor to a delegatee.¹³¹⁵ In such a case, performance by a delegatee is deemed proper performance under Article 313.¹³¹⁶

Articles 317 and 320 require that performance has to be with the proper object.¹³¹⁷ For example, a monetary obligation shall be performed in Russian rubles. For this reason, Article 317 requires that a monetary obligation be expressed in rubles and payable in rubles or other monetary unit that shall be converted into rubles.¹³¹⁸ If the contract grants the debtor the right to choose between alternative objects of performance, Article 320 regards performance by the creditor in any of the alternative forms as proper.¹³¹⁹

According to Article 316, a proper place and time are crucial to performance.¹³²⁰ The place of performance is typically stipulated in the contract by law or business custom. Article 314 defines proper time as that which is either stipulated by contract or by law.¹³²¹ If there is no such stipulation, a contract shall be performed within a reasonable time.¹³²² The provisions of Article 315 regulate the permissibility of a contract's premature performance.¹³²³

1311. OSAKWE, *supra* note 20, at 194-95 (showing diagrams encapsulating the provisions of article 313, 316, 312, 320, 317, 314, 315 and 311 of the Code.) See also BRAGINSKII COMM., *supra* note 81, at 660.

1312. C. CIV. art. 312 (Russ.).

1313. *Id.*

1314. See *id.*

1315. C. CIV. art. 313 (Russ.).

1316. *Id.*

1317. C. CIV. arts. 317, 320 (Russ.).

1318. C. CIV. art. 317 (Russ.).

1319. C. CIV. art. 320 (Russ.).

1320. C. CIV. arts. 314, 316 (Russ.).

1321. C. CIV. art. 314 (Russ.).

1322. *Id.*

1323. C. CIV. art. 315 (Russ.).

Under Article 311, a contract is completed properly if it is carried out in the right manner, which the Code defines as performance in full.¹³²⁴ Article 311 creates a presumption against performance of a contract in part.¹³²⁵ Failure to perform properly creates additional rights for the creditor (e.g., the right to demand from the debtor performance of the original obligation) as well as additional liability for the debtor (e.g., liability for the consequences of nonperformance or improper performance of the original obligation.)¹³²⁶

The second factual ground for termination of a contract is accord and satisfaction.¹³²⁷ In Article 409, the term *otstupnoe* means accord and satisfaction or substituted performance. When placed side by side with the three forms of accord and satisfaction recognized in American law, (i.e., executory bilateral accord, unilateral accord and substituted performance),¹³²⁸ the similarities and differences become readily apparent. All three of the aforementioned American forms are subsumed under the Russian notion of accord and satisfaction. Under Russian law, agreement on accord and satisfaction could be executed or executory;¹³²⁹ it could be entered into either at the time the original contract was signed or in the course of its performance.¹³³⁰

The concept of accord and satisfaction is new to Russian civil law and was first introduced to Russia in the 1994 Civil Code.¹³³¹ Parties may agree that in lieu of performance, an obligation terminates upon payment of a fixed sum of money or transfer of property or performance of service to the creditor by the debtor.¹³³² The essence of accord and satisfaction is that the debtor, with the consent of the creditor, can substitute the object of performance with a different object without changing the nature of the obligation itself.¹³³³ For example, in a contract for the supply of goods, the seller who supplies 90 percent of the goods

1324. C. CIV. art. 311 (Russ.).

1325. *Id.*

1326. C. CIV. arts. 393-97 (Russ.).

1327. C. CIV. art. 409 (Russ.).

1328. CALAMARI & PERILLO, *supra* note 656, at 290-292. See also ROHWER & SCHABER, *supra* note 6, at 396-98.

1329. SADIKOV COMM. ONE, *supra* note 74, at 776.

1330. SADIKOV COMM. ONE, *supra* note 74, at 777.

1331. BRAGINSKII COMM., *supra* note 81, at 537.

1332. C. CIV. art. 409 (Russ.).

1333. BRAGINSKII COMM., *supra* note 81, at 537.

required under the contract but finds himself unable to supply the remaining 10 percent may offer to pay the creditor a sum of money to cover the costs of the undersupplied goods. If the creditor consents to such a deal and payment is made to the creditor, accord and satisfaction takes place.

Accord and satisfaction is distinguishable from novation. Novation terminates one obligation and substitutes a new obligation in its place.¹³³⁴ By contrast, accord and satisfaction extinguishes all obligations between the parties.¹³³⁵ The Code treats liquidated damages as a possible variety of accord and satisfaction.¹³³⁶ There, the parties decide all issues relating to the payment of money or transfer of property from the debtor to the creditor.¹³³⁷ The agreement relates to the amount of payment or value of the property to be transferred to the creditor, time of such payment or transfer and procedure for payment or transfer of property to the creditor.¹³³⁸

Under Russian law, accord and satisfaction requires two elements: agreement on the terms of the payment of money or transfer of property and actual payment or transfer of property to the creditor.¹³³⁹ This means that the original obligation is considered terminated not at the time agreement on accord is reached, but at the time of satisfaction of the accord. The rules governing the form, procedure and significant conditions of accord and satisfaction are some of the other types of contract. Thus, if accord and satisfaction calls for the transfer of an immovable property, it shall require government registration and the accord and satisfaction enters into force at the time of state registration.¹³⁴⁰ Significant conditions of accord and satisfaction include agreement on the amount to be paid or the object to be transferred and specific stipulation of the original obligation to be terminated.¹³⁴¹

As a general rule, an agreement on accord and satisfaction is reached after the obligor fails to perform or improperly performs

1334. C. CIV. art. 414 (Russ.).

1335. SADIKOV COMM. ONE, *supra* note 74, at 662.

1336. See C. CIV. art. 396 (Russ.).

1337. See GUEV COMM. ONE, *supra* note 8, at 657.

1338. *Id.*

1339. BRAGINSKII COMM., *supra* note 81, at 537.

1340. C. CIV. art. 165 (Russ.).

1341. C. CIV. art. 432 (Russ.).

an obligation.¹³⁴² Neither statutory law nor case law, however, precludes the parties from stipulating in the original contract the terms of accord and satisfaction in the event of a breach. If the parties follow this latter procedure, it raises questions regarding the terms of the original contract. Russian case law, in those situations uses accord and satisfaction to secure the performance of the original obligation.¹³⁴³ Thus, if the original obligation is not performed or is improperly performed, completion of the ancillary agreement on accord and satisfaction will terminate the original obligation.

Certain rules of thumb must be kept in mind in order to meet the requirements for "accord and satisfaction" under Article 409.¹³⁴⁴ First, accord and satisfaction may be used to terminate only a contractual obligation and is not applicable to the termination of a noncontractual obligation.¹³⁴⁵ Second, the object of substituted performance may be anything of value such as money, securities, services, property, transfer of property rights or transfer of an intellectual property right.¹³⁴⁶ Third, the object of substituted performance may not be an individually personalized right, which is per se nonassignable.¹³⁴⁷ Finally, the value of the substituted object does not necessarily have to correspond to the value of the obligation to be terminated as long as the parties agree to the object of substituted performance.¹³⁴⁸

A third legal fact that constitutes a ground for the termination of contract is set-off. According to Article 410, an obligation may be terminated fully, or in part, by set-off of a reciprocal obligation the time of performance of which has become due or is defined as the time a demand for performance is made.¹³⁴⁹ Unlike the situation under accord and satisfaction, set-off can be undertaken by the expressed will of one party without the consent of the other party.¹³⁵⁰ In practice, set-off is commonly used as a method of terminating reciprocal monetary obligations. Under a bank

1342. SADIKOV COMM. ONE, *supra* note 74, at 662; BRAGINSKII COMM., *supra* note 81, at 538.

1343. BRAGINSKII COMM., *supra* note 81, at 538.

1344. C. CIV. art. 409 (Russ.); *see also* GUEV COMM. ONE, *supra* note 8, at 657.

1345. *Id.*

1346. GUEV COMM. ONE, *supra* note 8, at 657.

1347. *Id.*

1348. C. CIV. art. 409 (Russ.).

1349. C. CIV. art. 410 (Russ.).

1350. *Id.*

account contract, the customer is obligated to pay the bank for its services in making payments to third parties on the instructions of the client. Reciprocally, the bank is obligated to pay interest to the customer for the use of funds in the latter's bank account. Typically, reciprocal monetary obligations are accomplished by set-off under the provisions of Articles 853 and 409, unless the parties stipulate otherwise in their contract.¹³⁵¹

In some situations, the law may not permit set-off as a method of terminating reciprocal obligations. If the statute of limitations has tolled on an obligation, its reciprocal obligation cannot be set-off against it.¹³⁵² Also, a member of a limited liability company or of a joint stock company may not be released from an obligation to make his contribution to the charter capital of the company by setting off any claims that the member may have against the company.¹³⁵³

The law does specifically grant the debtor the right to set-off any claims that he might have against the creditor. For example, if a creditor assigns his rights to a third party, the debtor has the right to set-off against the new creditor any reciprocal claim that he had against the original creditor subject to the conditions stipulated in Article 412.¹³⁵⁴

In other situations, the law mandates set-off of reciprocal obligations. Under Article 399, a creditor does not have the right to seek satisfaction of an obligation from a secondary person who is liable for the obligations of a primary obligor if the creditor can satisfy such claims by setting off any reciprocal obligation owed to the principal debtor.¹³⁵⁵ In instances when set-off is carried out unilaterally by one party, Article 410 requires that two conditions be observed.¹³⁵⁶ First, set-off may be made only against a reciprocal obligation on which the statute of limitations has tolled or on which the time of performance is defined as the time of demand of performance.¹³⁵⁷ Second, the obligation to be set-off must be of the same type as the reciprocal claim from the original obligation.¹³⁵⁸ The term "of the same type" in this context means

1351. C. Civ. arts. 407, 853 (Russ.).

1352. C. Civ. art. 411 (Russ.).

1353. C. Civ. art. 90, 99 (Russ.).

1354. C. Civ. art. 412 (Russ.).

1355. C. Civ. art. 399 (Russ.).

1356. C. Civ. art. 410 (Russ.).

1357. *Id.*

1358. *Id.*

that the objects of both claims must be the identical, but does not mean that the two contracts must be of the same type or that the objects to be set-off must be the same.¹³⁵⁹

Article 413 of the Code regards the merger of the creditor and the debtor into one person as the fourth ground for the termination of an obligation. Such merger takes place when a lessor purchases a thing that he was renting. More typically, a merger takes place in the event of universal succession, such as in the case of reorganization of a legal person.

The next major factual ground for the termination of obligation is called novation. Under Article 450, novation is in itself a contract that extinguishes an existing obligation between the parties while substituting a new obligation between the same parties.¹³⁶⁰ The new obligation must contemplate either a new object, method of performance or both object and method of performance.¹³⁶¹

Russian law recognizes only objective novation (i.e., one in which only the object and/or method of performance changes, but the parties to the original obligation remain intact).¹³⁶² The parties' intent to novate the original obligation must be externally manifested.¹³⁶³ Intent must be clear and unequivocal; it may not be presumed.¹³⁶⁴ Novation is permissible under any contractual obligation.¹³⁶⁵ The new obligation may contemplate either a new object or a new method of performance or both.¹³⁶⁶ Thus, an agreement between a bank and a customer by which two delinquent notes were consolidated into one new note does not constitute novation under Russian law simply because there is not a substitution of either the object (i.e., note) or method of performance (i.e., payment of the money owed).¹³⁶⁷ All that took place was a mechanical consolidation of two delinquent notes into

1359. *Id.*

1360. C. Civ. art. 414 (Russ.).

1361. *Id.*

1362. *Id.*

1363. *Id.*

1364. *Id.*

1365. *Id.* Thus, for example, an obligation arising from a contract of sales may be set-off against one arising from a contract of independent contract or work; a monetary obligation may be set-off against an obligation for the supply of goods, performance of work or provision of services.

1366. C. Civ. art. 414 (Russ.).

1367. *See id.*

one large note, which is tantamount to a mere modification of an existing obligation.¹³⁶⁸

Article 414 calls for either a difference in the object or in the method of performance in novation.¹³⁶⁹ If the object of the obligations remains the same, the method of performance of the new obligation must be different from that of the old for novation to occur.¹³⁷⁰ Under Russian law, by virtue of novation, the original obligation is terminated along with all ancillary obligations.¹³⁷¹

For novation to take place, both the old and new contract must be valid. If, for any reason the old obligation is deemed invalid, the new contract will also be found invalid. If, however, only the new contract is found to be invalid, novation is deemed not to have taken place and the parties remain bound by the old contract. In the event of a dispute as to whether novation exists, the burden of proving novation rests with the party that asserts its existence.¹³⁷² Hence, the existence of a novation is never presumed.

Remission of debt, a common termination practice in Western law, is a new concept in Russian civil law and on many points tends to follow Louisiana law.¹³⁷³ Under Article 415, a creditor may forgive any debt owed to him at any time and may do so without the consent of the debtor.¹³⁷⁴ Remission of debt may be express or tacit.¹³⁷⁵ But, in all situations, it must be executed and not executory.¹³⁷⁶ A promise to forgive a debt owed at a future time does not operate as remission of debt under Article 415.¹³⁷⁷ If a creditor voluntarily returns to the debtor a written instrument that evidences the obligation, it creates a rebuttable presumption

1368. BRAGINSKII COMM., *supra* note 81, at 541.

1369. C. CIV. art. 414 (Russ.).

1370. *Id.*

1371. *Id.*

1372. SADIKOV COMM. ONE, *supra* note 74, at 665.

1373. LA. CIV. CODE ANN. art. 1888-92 (1987). Louisiana is a U.S. state.

1374. C. CIV. art. 415 (Russ.). There is a split of opinion among Russian scholars as to whether consent of the debtor is required. Guev says it is not required, but Sadikov says it is. GUEV COMM. ONE, *supra* note 8, at 663; SADIKOV COMM. ONE, *supra* note 74, at 666. Under Louisiana Civil Code consent is required, but presumed and may be rebutted by the debtor within a reasonable time. LA. CIV. CODE ANN. art. 1890.

1375. LA. CIV. CODE ANN. art. 1888.

1376. A remission of debt is effective when the obligor receives the communication from the obligee. LA. CIV. CODE ANN. art. 1890.

1377. See C. CIV. art. 415 (Russ.).

that he intended to forgive the debt owed.¹³⁷⁸

Under Russian law, however, as is the case also under the Louisiana Civil Code, "release of a real security given for performance of the obligation does not give rise to a presumption of remission of debt".¹³⁷⁹ A remission of debt requires a gratuitous act of forgiveness by the creditor.¹³⁸⁰ If the creditor receives any reciprocal consideration from the debtor, it ceases to be remission of debt and turns into novation.¹³⁸¹ Remission of debt becomes effective when communicated to and received by the debtor.¹³⁸² Russian law, in the opinion of Professor Guev,¹³⁸³ does not require the consent of the debtor to consummate remission of debt.¹³⁸⁴ A creditor's remission of debt may not adversely affect a third party's right in the creditor's property.¹³⁸⁵

On its face, remission of debt is quite similar to gratuitous contract of donation,¹³⁸⁶ but there are two significant differences between them. Donation requires the consent of the donee to accept the gift and it creates, rather than terminates, an obligation.¹³⁸⁷ The contract of donation obligates the donor to transfer to the donee the thing promised either in the future or immediately.¹³⁸⁸

Impossibility of performance constitutes the seventh factual ground for termination of an obligation. Under Article 416, performance of an obligation is deemed impossible if it can be attributed to circumstances for which the parties are not responsible.¹³⁸⁹ In commercial transactions, such circumstances are referred to as insurmountable force.¹³⁹⁰ Generally speaking, Russian law distinguishes three types of impossibility: physical,

1378. LA. CIV. CODE ANN. art. 1889.

1379. LA. CIV. CODE ANN. art. 1891.

1380. C. CIV. art. 415 (Russ.).

1381. See C. CIV. art. 414 (Russ.).

1382. Louisiana Civil Code art. 1890.

1383. See the discussion in note 1368 *supra*.

1384. GUEV COMM. ONE, *supra* note 8, at 663. In this sense, remission of debt is a unilateral obligation, not a contract, in the opinion of Guev. *Id.*

1385. *Id.* at 663-64. For example, an organization that has been declared bankrupt cannot forgive the debtor for a debt owed to it, for the simple reason that the creditors of the creditor in this case have interests in the property of the bankrupt creditor. *Id.*

1386. C. CIV. art. 572 (Russ.). See my discussion of the nature, types and conditions of the contract of donation in section VIII(C).

1387. *Id.*

1388. *Id.*

1389. C. CIV. art. 416 (Russ.).

1390. C. CIV. art. 401 (Russ.).

economic and legal.¹³⁹¹ Article 416 speaks of physical impossibility of performance.¹³⁹²

Article 416 grounds may be invoked if the circumstance that created the impossibility of performance occurred in the course of performance of the contract, rather than when the contract was signed.¹³⁹³ Impossibility of performance under Article 416 does not apply to monetary obligations.¹³⁹⁴ The performance of an obligation may be rendered impossible by virtue of an order issued by a state agency.¹³⁹⁵ Economic impossibility does not qualify as an insurmountable force under the meaning of Article 416.¹³⁹⁶ Rather economic impossibility falls under Article 451.¹³⁹⁷ The ground for physical impossibility of performance, contemplated under Article 416, is part of the insurmountable forces mentioned in Article 401.¹³⁹⁸

The circumstances that make performance impossible may also be attributable to a supervening intervention by a government agency, which is the eighth factual ground for the termination of an obligation.¹³⁹⁹ A trade embargo would render impossible the performance of an obligation under the contract for the supply of goods to a contracting party in that country. Article 13 grants the parties the right to challenge such a government order in a court of law.¹⁴⁰⁰ If the court finds the order to be unlawful, it shall reverse it and award damages to any parties adversely affected by it.¹⁴⁰¹ Adoption of the order in question, however, would effectively render performance of a contract impossible. What is not clear from Russian case law is its effect on an obligation terminated by an order of a government agency if a court in an action under Article 13 subsequently overturns the order.¹⁴⁰² A subsequent reversal of such a government order would effectively resurrect the terminated obligation unless the contract or nature of the

1391. C. Civ. arts. 416, 451, 417 (Russ.). See generally OSAKWE, *supra* note 20, at 193, 203.

1392. See C. Civ. art. 416 (Russ.).

1393. *Id.*

1394. C. Civ. arts. 401, 416 (Russ.).

1395. C. Civ. art. 417 (Russ.).

1396. See C. Civ. art. 416 (Russ.).

1397. C. Civ. art. 451 (Russ.).

1398. C. Civ. art. 401 (Russ.).

1399. C. Civ. art. 417 (Russ.).

1400. C. Civ. art. 13 (Russ.).

1401. See C. Civ. arts. 12-13 (Russ.).

1402. C. Civ. art. 13 (Russ.).

obligation provides otherwise or the creditor has lost interest in the further performance of the contract.¹⁴⁰³

The ninth factual ground for terminating an obligation is the liquidation of a legal person.¹⁴⁰⁴ Liquidation of a legal person terminates the legal entity without transferring its rights and obligations by universal succession to other persons.¹⁴⁰⁵ Consequently, all obligations of the liquidated organization are terminated.¹⁴⁰⁶ The law, however, recognizes certain exceptions to the rule.

One exception may be found in Article 1002 of the Code governing the termination of a commission agency.¹⁴⁰⁷ Under Article 1002, the liquidation of a legal person is rendered ineffective when recorded in the state register of legal persons.¹⁴⁰⁸

Finally, the Code lists the death of a citizen as a ground for the termination of an obligation.¹⁴⁰⁹ Under these provisions, the term "citizen" includes both the citizen-consumer and the citizen-entrepreneur.¹⁴¹⁰ The individual personalty of the citizen need only be linked with performance of an obligation.¹⁴¹¹ For a citizen's death to terminate an obligation, Article 418 stipulates two conditions.¹⁴¹² First, performance of the obligation is impossible without the personal participation of the deceased creditor or debtor.¹⁴¹³ Second, the obligation is inseparably linked to the individual personalty of the debtor or creditor.¹⁴¹⁴ Here, the same principle applies both to the death of the creditor and to the

1403. C. CIV. art. 417 (Russ.). Perhaps the most important point to bear in mind with regard to Article 417 is that it refers only to "the act of a state agency." C. CIV. art. 417 (Russ.). Under Russian law, the term *gosudarstvennyi* organ (state agency) refers exclusively to a federal agency, not to a local government agency or to the agency of a subject of the Russian Federation. C. CIV. arts. 13, 16 (Russ.). Thus, if an order of a local government or state government agency interferes with the performance of a contract, impossibility of performance would not be invoked. *Id.* The only recourse left to the parties is spelled out in Articles 13, 15, 16 and 393. See C. CIV. arts. 13, 15, 16, 393 (Russ.).

1404. C. CIV. art. 419 (Russ.).

1405. C. CIV. art. 61 (Russ.).

1406. See *id.*

1407. C. CIV. art. 1002 (Russ.).

1408. C. CIV. art. 63 (Russ.).

1409. C. CIV. art. 418 (Russ.).

1410. GUEV COMM. ONE, *supra* note 8, at 667.

1411. See C. CIV. art. 418 (Russ.).

1412. *Id.*

1413. *Id.*

1414. *Id.*

death of the debtor.¹⁴¹⁵

With regard to specific types of obligations, however, the Code carves out exceptions to the general rule in Article 418.¹⁴¹⁶ In the case of the contract of gratuitous use of property under Article 701, the death of the grantee (user) of such property shall terminate obligations arising from the contract unless the parties agree otherwise.¹⁴¹⁷ Also, the Russian Supreme Court of Arbitration has held that the death of a citizen does not terminate a monetary obligation for the simple reason that such obligation is not inseparably linked with the individual personality of the debtor or creditor.¹⁴¹⁸

C. Modification and Dissolution of Contract

The provisions of Chapter 29 of the Code, in Articles 450-453, regulate the grounds for the modification, procedure and dissolution of a contract and its consequences.¹⁴¹⁹ Article 450 lists the following grounds for the modification and dissolution of a contract: agreement of the parties; significant violation of the contract by one of the parties; repudiation of the contract by one of the parties in cases when unilateral repudiation of a contract is permissible by law; and other grounds stipulated in the Code or in any other law.¹⁴²⁰

Article 450 contemplates three separate and distinct procedures for the modification or termination of a contract: by mutual agreement, by court action after unsuccessful out-of-court attempts to settle the terms of a modification or dissolution of the contract and unilateral repudiation in situations where such unilateral action is permitted by law.¹⁴²¹ Generally, parties can agree at any time to terminate the contract.¹⁴²² This principle of contract termination by mutual consent is subject to a few exceptions.¹⁴²³ An example may be found in Articles 370 and 371

1415. *Id.*

1416. Specifically, contract of gratuitous use of property and contract for monetary obligation.

1417. C. CIV. art. 701 (Russ.).

1418. SADIKOV COMM. ONE, *supra* note 74, at 669.

1419. C. CIV. arts. 450-53 (Russ.).

1420. C. CIV. art. 450 (Russ.).

1421. *Id.*

1422. *Id.*

1423. C. CIV. arts. 370-71 (Russ.). Thus, a contract may not be terminated by mutual consent, if the Civil Code specifically disallows such termination. *Id.*

regarding a contract of bank guarantee where a letter of credit is irrevocable.¹⁴²⁴ Another example is the termination of contract by mutual consent found in Article 430.¹⁴²⁵ Such a contract in favor of a third person cannot be terminated by mutual consent of the parties to the contract.¹⁴²⁶ Also, the parties to a contract may stipulate in the contract itself that dissolution of the contract by mutual consent is not permitted.¹⁴²⁷

A second rule under Article 450 is that a contract may be repudiated or modified by a court at the petition of one of the contracting parties under certain circumstances.¹⁴²⁸ For example, in the event of a substantial violation of the contract by the other party, if it is permitted by law to do so, and if the contract itself grants such a right to the parties.¹⁴²⁹ Only a significant violation of the contract by one party grants the other party the right to resort to the courts with a petition to modify or terminate the contract. Significant in this context is a question of fact to be determined by the court on a case-by-case basis.¹⁴³⁰ Russian doctrine defines as significant any violation that is so serious that it denies the other party the gains it reasonably expected to derive from the contract.¹⁴³¹ In some cases, the Code itself specifically lists what it regards as a significant violation of a contract.¹⁴³²

Such violations include the following: the lessee using the leased object for a purpose other than intended; violating the conditions of the lease repeatedly; using the property in a manner leading to its fast deterioration; consecutively failing to pay his rent on time; and failing to timely perform contracted for repair of the leased object.¹⁴³³

1424. *Id.*

1425. C. CIV. art. 430 (Russ.).

1426. *Id.*

1427. *See id.*

1428. C. CIV. art. 450 (Russ.).

1429. *Id.*

1430. SADIKOV COMM. ONE, *supra* note 74, at 731.

1431. GUEV COMM. ONE, *supra* note 8, at 728.

1432. *See* C. CIV. arts. 619, 620, 450 (Russ.).

1433. C. CIV. art. 619 (Russ.). The Presidium of the Supreme Arbitration Court ruled that the failure of a construction company to complete construction on schedule and any subsequent increase in the costs are tantamount to a substantial violation of the contract and, as such, are grounds for a rescission of the contract by the customer under Article 450. TIKHOMIROV, *supra* note 69, at 29-30. In explaining its opinion in this ruling, the Court added that under the provision of Article 743, a contractor is obligated to complete construction work within the schedule and at not more than the costs stipulated in the contract. *Id.* If prices of building materials increase by more than ten percent over those

Unilateral repudiation of a contract under Article 450 is permitted when the law or contract allows.¹⁴³⁴ For example, if a fixed term lease expires and the parties do not intend to terminate the contract, it automatically renews for an indefinite term.¹⁴³⁵ In that case, a party may repudiate the lease unilaterally upon three-month notice to the other party.¹⁴³⁶ Additionally, in an agency contract, the principal may, at any time, unilaterally revoke the authority of the agent and the agent may, at any time, unilaterally reject the authority granted him by the principal.¹⁴³⁷

Substantial change of circumstances is an autonomous ground for the modification or dissolution of a contract.¹⁴³⁸ Russian case law defines "substantial change of circumstances" by looking at four elements: (1) at conclusion of the contract, the parties did not contemplate such a change of circumstances; (2) the change of circumstances could not be reasonably controlled by the interested party after they occurred; (3) performance of the contract under the new circumstances would substantially deny the interested party the gains that he reasonably expected to derive from the contract; and (4) neither business custom nor the contract implies that the adversely affected party assumed the risk of the occurrence of these circumstances.¹⁴³⁹ A substantial change in circumstances grants the interested party the right to approach the other party with the question of modification of the contract.¹⁴⁴⁰ If agreement cannot be reached between them on the terms of the modification, the interested party can move to terminate the contract through the courts.¹⁴⁴¹ Typically, the circumstances contemplated under Article 451 would qualify as an economic impossibility of performance.¹⁴⁴² It is important to remember that the existence of a supervening economic impossibility of

stipulated in the contract, for reasons that are beyond the contractor's control, the contractor has the right to seek the customer's agreement on an upward revision of the costs. *Id.* Any unilateral decision by the contractor to extend the time limit for completion of the construction or to raise the costs of construction shall constitute adequate grounds for rescission of the contract. *Id.*

1434. C. Civ. art. 450 (Russ.).

1435. C. Civ. art. 621 (Russ.).

1436. C. Civ. art. 610 (Russ.).

1437. C. Civ. art. 977 (Russ.).

1438. C. Civ. art. 451 (Russ.).

1439. *Id.*

1440. *Id.*

1441. *Id.*

1442. OSAKWE, *supra* note 20, at 203.

performance does not grant a party to the contract the right to modify or terminate the contract unilaterally.¹⁴⁴³ An interested party may only bring up the question of adjusting the terms of the contract to reflect any new circumstances that occurred after the contract was signed.¹⁴⁴⁴

Absent an agreement between the parties on the modification of the contract, only the court can terminate the contract.¹⁴⁴⁵ If a lawsuit is filed with a court seeking termination of a contract, the court may, as a general rule, terminate the contract or, in exceptional situations, modify the contract.¹⁴⁴⁶ The Court may modify the contract in only two situations: (1) where the termination of the contract would violate public policy, yet it is impossible to let the contract stand and (2) where the termination of the contract would be more expensive than performing it on modified terms.¹⁴⁴⁷ In other words, if the parties do not agree on a modification of the contract, substantial change of circumstances may be grounds for a negotiated modification or a judicial termination of the contract.¹⁴⁴⁸ Judicial modification of a contract on the ground of substantial change of circumstances is an exception to the general rule.¹⁴⁴⁹

The idea of substantial change of circumstances corresponds to the doctrine of frustration of contract in U.S. law.¹⁴⁵⁰ According to the prevailing rule in the United States and Germany, a fundamental change in the economic underpinnings of a contract, which places one party to the contract at a serious disadvantage, may constitute sufficient grounds to permit the disadvantaged party to seek dissolution of the contract.¹⁴⁵¹

Following is the Russian procedure for the modification or dissolution of a contract: (1) unless otherwise provided by law, contract, or custom, an agreement to modify or dissolve a contract shall be in the same form as the original contract and (2) a party may resort to the courts for dissolution of a contract only after it has unsuccessfully attempted to reach a settlement with the other

1443. C. CIV. art. 416 (Russ.).

1444. C. CIV. art. 451 (Russ.).

1445. *Id.*

1446. *Id.*

1447. *Id.*

1448. *Id.*

1449. *See* C. CIV. art. 451 (Russ.).

1450. *See* C. CIV. art. 451 (Russ.).

1451. *See* ZWIEGERT & KOTZ, *supra* note 23, at 220-28.

party.¹⁴⁵² The consequences of the modification or dissolution of a contract are as follows: (1) if the parties reached an agreement on the modification, the obligations of the parties remain in the modified form; (2) if the contract was terminated, the obligations of the parties under the contract are extinguished; (3) unless otherwise stipulated in the agreement itself or otherwise suggested by the nature of the obligation, a contract is considered to have been modified or terminated at the time the agreement was reached between the parties on such modification or termination; (4) if the modification or termination was carried out through the court, it is considered to have taken place at the time the court's decision was rendered; (5) unless otherwise stipulated in the agreement or by law, the parties may not demand the return of things received prior to the time of the modification or termination; and (6) if the ground for the modification or termination was a significant violation of the contract by one of the parties, the other party may seek compensation for damages suffered as a result of the breach.¹⁴⁵³ In other words, it takes a separate contract to modify or dissolve an existing contract. If the parties fail to agree on the terms of a modification or dissolution of a contract, either party may resort to the courts to seek such dissolution or modification. In the event of a unilateral modification or dissolution of a contract, the aggrieved party may seek judicial remedies in the form of damages against the breaching party if the resulting violation of the contract is deemed significant.

XIV. CONCLUSION: THE GREENING OF RUSSIAN CONTRACT LAW

Compared to its pre-1991 version, modern Russian contract law can best be described as a total metamorphosis. The quantum leap from its Soviet character to its present form is attributable to five new developmental trends: creeping Europeanization, substantial de-Sovietization, principled Romanization, elevation of case law as a source of contract law and a shift in Russian legal scholarship from the traditional glossatorial style to the pandectian style.¹⁴⁵⁴

1452. C. CIV. art. 452 (Russ.).

1453. C. CIV. art. 453 (Russ.).

1454. Glossatorial means superficial, unanalytical, noncreative, glossy. Pandectian means analytical, probing, creative.

The most striking feature of modern Russian contract law is the subtle injection of ideas from continental European contract law into Russian law.¹⁴⁵⁵ For example, the authors of the modern Russian Civil Code imported the traditional European law devices of withholding,¹⁴⁵⁶ bank guaranty¹⁴⁵⁷ and earnest money.¹⁴⁵⁸ In addition, the authors replaced the Soviet-era security device (*garantiia*) with the modern European law concept of suretyship.¹⁴⁵⁹ These incremental changes align Russian contract law with continental European contract law, while retaining its uniquely Russian idiosyncrasies. The decision to import the common law trusts into the Code falls within this general trend of europeanization of modern Russian contract law.¹⁴⁶⁰

The removal of certain anti-market principles of Soviet contract law have also made the Code more European in nature. Perhaps the best illustration of this phenomenon is the Code's rejection of the concept of plan contracts, an arrangement by which state enterprises were required to conclude contracts with other state enterprises as a mandatory requirement of their fulfillment of state-mandated economic plans.¹⁴⁶¹ The notion of plan contracts violated the principle of freedom to contract.

Furthermore, modern Russian contract law has evolved through principled romanization. The drafters of the Code had the choice of either re-affirming the Roman roots of Russian civil law or injecting competing ideas of Anglo-American common law. There was a danger that Russian contract law would be "bastardized" by the injection of common law principles because the drafters were surrounded by prominent experts from the common law world.¹⁴⁶² In the final analysis, the Code remained faithful to its civil law origins. The reforms of 1991-1994 reaffirmed modern Russian law's unwavering membership in the family of European contract law with deep roots in Roman private law. For example, modern Russian contract law retains the traditional

1455. In the text that follows, examples are given of ideas borrowed from European law and transposed into Russian law.

1456. C. Civ. arts. 359-60 (Russ.).

1457. C. Civ. arts. 368-79 (Russ.).

1458. C. Civ. arts. 380-81 (Russ.).

1459. C. Civ. arts. 361-67 (Russ.).

1460. Trusts trace their origins to English law and traditionally were not an institution of continental European law.

1461. FARNSWORTH & MOZOLIN, *supra* note 86, at 106-07, 72-73, 132, 66-75, 27-36.

1462. Makovsky & Khokhlov, *supra* note 24, at 58.

continental European distinction between civil and commercial law, as manifested by the division of contracts into civil law and commercial law contracts¹⁴⁶³ and the classical Roman law classification of contracts into nominate and innominate.¹⁴⁶⁴ As a result of the rejection of the common law, especially U.S. law, the Code does not contain many features of the common law such as the requirement of consideration for the formation of a contract, the notion of an option contract, the conception of a counter offer where an acceptance modifies terms of the offer, the classification of a public bid as a unilateral contract rather than as a non-contractual unilateral obligation and the principled rejection of the notion of punitive liquidated damages.¹⁴⁶⁵ The only demonstrable evidence of common law influence on Russian contract law is the nominate contract denominated as trust administration of property.¹⁴⁶⁶ This is a modified version of, but a substantially different institution from, common law trusts.

The elevation of case law to the respectable status of a normative source of contract law is a refreshing development in the evolution of modern Russian contract law. Soviet civil law

1463. The traditional continental European division of private law into civil and commercial culminated in the adoption of two separate private law codes: civil and commercial, as evidenced in France and Germany. See Osakwe, *supra* note 20, at 58-60. There, rules governing civil and commercial law contracts are housed respectively in its separate codes.

Following this continental European tradition, the 1994 Russian Civil Code divides contract rules at two levels into two distinct groups. At the first level there are those rules that apply to purely consumer contracts and those that govern commercial law contracts. Russian law defines a commercial transaction as one between the merchants or involving the participation of a merchant as one of the parties. C. CIV. art. 3 (Russ.). The general rules governing commercial transactions are to be found in the Civil Code's articles 153-181, 307-453, as well as in the provisions of Part Two of the Civil Code. Most of the rules that govern Commercial transactions are hidden in ancillary statutes, notably in the 1992 Law on the Protection of the Rights of Consumers. At the second level, the Code sections governing commercial transactions distinguish those that apply to transactions between merchants from those that govern commercial transactions in which one of the parties is a consumer. This two-tier arrangement subjects merchants to a more stringent standard than non-merchants. Among the Russian Civil Code rules that contemplate double standards for commercial transactions, one may point to the following articles: Articles 310, 315, 322, 258, 401, 428, 469, 481, 492, 506, 548, 709 modifying the general rule in article 733, 730, 838, 891, 907, 972, 995, 1027, 1041, and 1095.

1464. For a discussion of nominate and innominate contracts in Roman law, see NOVITSKII & PERETERSKII, *supra* note 246, at 456-472.

1465. See earlier discussion of liquidate damages *supra* pages 69-75, 116-117.

1466. C. CIV. art. 1012 (Russ.). A core element of the Russian notion of trust administration of property is ownership of the property placed in trust administration does not transfer to the trust administration. *Id.*

rejected any notion of judicial law making.¹⁴⁶⁷ Under this tradition, the role of the courts was reduced to that of a humble and mechanical applier of the law.¹⁴⁶⁸ The courts were viewed as judicial slot machines whose brainless function was to feed in the facts of a given case at one end and crank out the law at the other. Modern Russian law rejects this outdated view.

The new thinking in Russian law is that courts are major partners with the legislature in the joint enterprise of making laws governing contracts.¹⁴⁶⁹ In this partnership, the specific role of the courts is to fill in gaps in statutory law. This is done not in the context of decided cases since the Russian legal system rejects the common law notion of *stare decisis*, but rather in the form of binding advisory judicial opinions denominated respectively as decrees (*postanovleniia*), clarificatory interpretations (*raziasneniia*) and letter rulings (*pisma*) of either the en banc session (*plenum*) or the executive session (*presidium*) of the Supreme Arbitration Court or Supreme Court of general jurisdiction.

The last phenomenon in modern Russian contract law is a bold new trend in Russian civil law scholarship (*doktrina*).¹⁴⁷⁰ The traditional sterile, unimaginative, descriptive glossatorial style of writing moved towards a more analytical, critical and creative pandectian style of legal writing.¹⁴⁷¹ In the past, Russian civil law scholarship was reflected in the commentaries on the civil code—a formalistic recitation of provisions of the code, accompanied by an unimaginative regurgitation of judicial practice connected with such code extracts.¹⁴⁷² The old Soviet civil law textbooks followed the same sterile style.¹⁴⁷³ In contrast, there is an emergence of new analytical writings by Russian civil law scholars especially in the

1467. GLENDON, GORDON & OSAWKE, *supra* note 23, at 960-61; OSAWKE, *supra* note 20, at 355-57.

1468. GLENDON, GORDON & OSAWKE, *supra* note 23, at 960-61; OSAWKE, *supra* note 20, at 355-57.

1469. See the earlier discussion of case law as a source of contract law on pages 5, et. seq.

1470. See the earlier discussion of legal scholarship as an increasingly important source of Russian contract law on pages 9-10. It will be absolutely impossible to understand the full meaning of certain provision of the Civil Code without the clarification offered by commentators in what is know as doctrine (*doktrina*). See *infra* notes 64, 462, 465, 506.

1471. See the earlier discussion of this statement on pages 9-10.

1472. OSAWKE, *supra* note 20, at 70.

1473. *Id.*

field of contract law.¹⁴⁷⁴ The writings of Professors Braginskii, Vitrianskii, Sadikov and Guev represent this new generation of civil law scholarship.¹⁴⁷⁵ Their writings weave case law and statutory law in a way that produces fresh ideas and critical new thinking. They have openly criticized certain decisions of the Supreme Arbitration Court, which they believe are erroneous, and have urged the courts to be more creative in their interpretation and application of the law.¹⁴⁷⁶

Notwithstanding these five progressive trends in the development of modern Russian law of contracts, however, three perennial problems persist; namely, a substantial gap between the law on the books and the law in action, a lack of sophistication by the judges who apply the law and a lack of an effective mechanism for enforcing civil court judgments. The first of these three problems is the most serious.

On the books, modern Russian contract law looks very enlightened and quite continental European, but its application borders on benign neglect by virtually all segments of the Russian society. Enterprises prefer to circumvent the law in their business dealings. Citizens are not enthused about conforming their private and/or business affairs with legal requirements; and the government itself does not always act within the confines of the law. Respect for the sanctity of contracts is not yet an element of Russian legal culture. As a result of virtually universal neglect of the law on the books within Russian society, the Code operates like a potted plant—it beautifies and purifies the room, but does not ecologically blend with its environment.

The fact that current Russian judges lack the sophistication to apply the new laws on the books creates a separate type of problem for contract law. For example, judges routinely ignore the law that requires courts to diminish the defendant's civil liability in proportion to the degree of the plaintiff's contributory fault. Instead, judges diminish it by half.

1474. See the earlier discussion of this statement on pages 9-10.

1475. See the earlier discussion of this statement on pages 9-10.

1476. BRAGINSKII CONTRACT 1998, *supra* note 82; BRAGINSKII CONTRACT 1999, *supra* note 23; BRAGINSKII CONTRACT 2000, *supra* note 82; SUKHANOV 1, *supra* note 23; SUKHANOV 2(1), *supra* note 83; SUKHANOV 2(2), *supra* note 83; EGOROV TEXTBOOK 1, *supra* note 83; EGOROV TEXTBOOK 2, *supra* note 83; EGOROV TEXTBOOK 3, *supra* note 83.

Lastly, the absence of an effective mechanism for enforcing civil judgments is a real problem in Russia. Winning a case in civil court solves only half the problem. The real problem is getting the judgment enforced. Many decades of benign neglect of private law has atrophied the civil courts, whose contempt power and the power to enforce judgments pales in comparison to those of the criminal courts. In the author's conservative estimation, the courts do not enforce approximately seventy-five percent of all civil judgments in Russia. As a result, many civil judgments are enforced through self-help, which, in many instances, means reliance on the services of criminal gangs and bounty hunters. How can a businessman have faith in the system's contract law if he believes that a judgment in hand will not be honored by the losing party or enforced by the courts?

In the final analysis, modern Russian contract law is unmistakably continental European. But Russian civil judgment enforcement practices and general compliance with the written law fall abysmally short of Western expectations. Judged by these latter standards, modern Russian contract law straddles the line between Western and non-Western law. One good thing about this law, however, is that it aspires to be Western and may very well attain that status one day.