MODERN ISSUES OF CORPORATE LEGISLATION AND THE WAYS OF THEIR SOLUTION IN THE REPUBLIC OF ARMENIA

Vahram D. Avetisyan[1]

The legal regulation of market relations, which are in the formation process in the Republic of Armenia, was put on a new qualitative level through the RA Civil Code (hereafter: the Code) adopted on May 5, 1998. However, the 14 years of its application allowed revealing various shortcomings and gaps in the Code and in the laws adopted on its basis. A certain part of those shortcomings and gaps do not allow clearly fixing the factual frames of social relations which are regulated by civil legislation, and the other part hinders the normal process of market relations' development. The legislation[2] regulating corporate legal relations stands out with its abundance of such issues.

It was tried to regulate both the "trivial" or classic civil relations arising between physical individuals or by their participation and the relations arising between the persons who are engaged in business activities or by their participation, in essence, through the Code and a range of laws adopted on its basis, excluding dualism of private legal relations.

As a result, Article 1 and Article 2 of the Code stipulate the scope of relations which are regulated by the civil legislation, in particular, it defines that the civil legislation, as well as the decrees of the President of the Republic of Armenia and the decisions of the Government of the Republic of Armenia containing norms of civil law (hereinafter referred to as "other legal acts") determine the legal status of the participants in civil circulation, the grounds for arising

[1] Doctor of Legal Sciences, Head of the Chair of Civil Law of the Yerevan State University. E-mail: vahram.avetisyan@mail.ru.

[2] Within the framework of the present study, the issues existing in this field are mainly discussed on the basis of the Code and the legislation on joint-stock companies as this sphere is one of the most regulated fields.

and the procedure for the exercise of the right of ownership and other property rights, exclusive rights to the results of intellectual activity (intellectual property), regulate contractual and other obligations as well as other property relations and personal non-property relations related to them.

The application and study of the Code and other laws adopted based on it, with respect to different organizational-legal forms of legal entities allow stating that the scope of relations regulated by the Code is not entirely reflected in the above-mentioned norm. In particular, the civil legislation regulates an independent group of social relations which have received the name "corporate legal relations" in theoretical literature.

The RA legislation does not actually clarify the concept of the term "corporation", but, in essence, it uses the term "organization" as a synonym for that concept. But there are certain manifestations of the use of the term "corporation" in the RA legislation: for example, the Convention on Transnational Corporations, the RA Law "On investment funds", the Article 3 of which defines the concept of corporate funds, etc. The study of foreign legislation allows us to point out the circumstance that recently some countries which formed their civil legislation based on the CIS model of civil code try to give the formulation of corporate legal relations and clarify the concept of corporate organizations.

For example, the corporate relations in the Civil Code of the Russian Federation, with amendments made on December 30, 2012, are characterized as relations linked to participating in corporate organizations or managing them (Article 1 of the Civil Code of the Russian Federation)[3], The Economic Code of the Republic of Ukraine, Article 167(1) gives the definition of corporate rights, characterizing it as the rights of the person having his or her share in the charter fund (property) of the economic organization, including authority to participate in the management of the economic organization, receipt of certain part of profit (dividends) of this organization and assets in case of its liquidation pursuant to the law,

[3] http://base.garant.ru/10164072/

and other authorities prescribed by the law and statutory documents[4].

We share the opinion of those theorists of continental legal system who find that the definition of corporation covers all the organizational-legal forms of ***private law*** legal entity prescribed by legislation: joint-stock companies, companies of limited and supplementary liability[5], limited and full partnerships[6], cooperatives, as well as the unions of commercial organizations (associations, concerns, holdings, etc.) [7].

The organizational relations specific to modern market economy principally differ from the organizational relations of the Soviet period economy. Nowadays, the subjects of civil law act in favor of their interests, make decisions concerning the creation, reorganization and liquidation of the corporation; the management bodies of the corporation adopt decisions and ensure their exercise, determine the development policy of the relevant corporation, distribute the profit or create additional mechanisms for exercising their social, cultural or non-commercial profits, that is to say they organize and manage the activity of the corporation by the civil-legal renewed principles.

Thus, we can note that corporate relations have independent nature and can be characterized as an independent type of civil legal relations, complex legal relations which regulate property relations

[4] http://www.yurist-online.com/uslugi/yuristam/kodeks/016/165.php

[5] We find that the organizational-legal form of supplementary liability company is artificial and not viable in RA legal system. In particular, during 14 years no legal entity of such organizational-legal form was created in Armenia, hence we suggest not to envisage this organizational-legal form of legal entity in the Code.

[6] The legal regulation of the Code regarding partnerships is also quite incomplete as a result of which during 14 years of the Code's operation no partnership has been created in Armenia. In order to exclude such situation, it is necessary to make relevant changes regarding the subject and founding document of partnerships which will, in our opinion, contribute to the increase in the number of partnerships of such organizational-legal form in Armenia.

[7] See Corporate Law. Textbook (I.S. Shishkina eds.), Moscow 2007, p.7; Kashanina T.V. Corporate Law. Textbook. Moscow 1999, P. 1. [Корпоративное право: Учебник /Под ред. И.С. Шишкина. М. 2007, С. 7, Кашанина Т. В., Корпоративное право, Учебник, М. 1999, С. 1].

and organizational-management relations[8] closely related to them, concerning values of non-property nature.

Taking into account the above-mentioned, we suggest to make a supplement in Article 1(2) of the Code and within the scope of relations regulated by civil legislation add "(corporate relations) related to participating in organizations and managing them" after the words "other obligations" and make relevant changes in the relevant norms of the Code and other laws regulating corporate relations consistent with the change.

First of all it is necessary to review the framework of civil legal-relations' participants as the imaginary comprehensive listing of civil legal-relations' participants mentioned in Article 1(2)(2) of the Code does not actually reflect the reality of things. Now, in fact, the subjects of civil legal-relations are not only physical persons, legal entities, communities and the Republic of Armenia, but also the international organizations, diplomatic missions, etc., and in corporate relations the subjects who deal with the internal side of corporate relations: the participants of corporation (members, shareholders, etc.), management bodies, as well as the bodies which control the activity of the corporation.

There is no single approach in theory and practice concerning the nature of the decisions adopted by the bodies managing the corporation, any order confirmed by the corporation, regulation, charter, etc., whether they are transactions or legal acts[9]. The practical and theoretical meaning of this question comes up while

[8] We will justify the independent nature of corporate legal relations in more detailed way in our previous works, see Avetisyan V.D. Features of Corporate legal Relations. "Bulleting of the Yerevan State University" 2011, #134.3, pp. 27-38; [Ավետիսյան Վ.Դ., Կորպորատիվ իրավահարաբերությունների առանձնահատկությունները, «Բանբեր Երևանի Համալսարանի 2011, N 134.3, էջ 27-38.]

[9] About this as well as about the particularity of corporate transactions see in more details Avetisyan V.D. Features of Corporate legal Relations. "Bulleting of the Yerevan State University" 2011, #134.3, pp. 27-38. [Ավետիսյան Վ.Դ., Կորպորատիվ իրավահարաբերությունների առանձնահատկությունները, «Բանբեր Երևանի Համալսարանի 2011, N 134.3, էջ 27-38].

examining the question of justifying the requirements of recognizing them as invalid and applying the consequences of the invalidity. The point is that in such situations it is necessary to protect not only the interests of the persons relating to the internal side of corporate legal relations but also, from the perspective of providing the civil legal relations with stability, the interests of the third persons which can be violated by recognizing such decisions as invalid.

Let us imagine a situation when "X" joint-stock company was reorganized in form division and as a result "Y" and "Z" joint-stock companies were created. After three months, the company "Y" was again reorganized in form division, as a result of which "V" and "F" companies were created. And company "Z" was liquidated eight months after the reorganization.

In addition, the shareholders of "V" and "F" companies were changed, bonds were issued and distributed, and different transactions were made. Two years after the reorganization of "X" joint-stock company, shareholder A appears who was abroad for immigrant work and was not aware of the processes taking place in the company and finds out that if he had participated in that meeting and voted against the decision on reorganization made in violation of the law, he would have prevented the process of events described above. Or let us imagine a situation when while making the decision the shareholder voted for it under the influence of violence or threat. Addressing to the court, shareholder A demands to recognize the shareholders' general assembly's decision as invalid.

A question arises here: what will be the consequences of invalidity in case of sustaining the demand? If the court considers the decision of the general assembly and the procedures and other documents confirmed on its basis as a transaction, then it will apply the general rules of transaction's invalidity, and if it recognizes it as a legal act then it is not clear what will be its attitude. Besides, in such situation, the further fate of the obligations of the new organizations created as a result of reorganization as well as the issue of the protection of the persons' interests related to the turnover of the issued securities is unknown.

We would like to mention that in this field the incompleteness of corporate legislation does not allow giving a fair solution to the situations mentioned above and every time the courts decide on the consequences[10] of the invalidity of the mentioned acts within their discretion. And the main reason is that the issue of corporate transaction conditioned by the particularity of corporate relations is not regulated in the Code.

In this regards we would like to highlight that within the meaning of the RA Law "On legal acts", the above-mentioned acts can be characterized as individual or internal legal acts (Article 23(1) of the Law "On legal acts") but this does not exclude that the internal legal acts can be also considered as a transaction with the consequences deriving therefrom.

In our opinion the main reason for such a legal uncertainty is the incomplete definition and legal regulation of transaction in Article 289 of the Code which does not express the essence of modern civil legal relations. In particular, the mentioned norm defines transactions as the actions of citizens and legal entities which are aimed at the establishment, change, or termination of civil law rights and duties. It is obvious that transactions can be made not only by citizens and legal entities but also by all the above- mentioned participants of civil legal relations, including the participants of corporate legal relations.

We find it necessary to mention that several states of continental legal system, mainly the followers of the post-soviet system, the German legal system tried to formulate the concept of transaction, and in the countries of common law system as well as in Roman law this term is not used. For example, Article 50 of the Civil Code of Georgia, defines the transaction as a unilateral, bilateral or multilateral declaration of will aimed at creating, changing or terminating[11] legal relations.

---

[10] See the decision of Cassation Court in the case number YeED/1246/02/09 and the circumstances of the case.

[11] Chanturia L.L. Contract and expression of will in civil law// Journal "Jurist", March, #3, 2006. [Чантурия Л.Л. Сделка и волеизъявление в гражданском праве,// Журнал "Юрист", март, N 3, 2006].

From this definition it is clear that the Georgian legislator avoided listing the subject composition of a transaction, which gives grounds to suppose that all the participants of civil legal relations can be transaction performers.

We suggest amending Article 289 of the Code to read as follows: "Transactions shall be the actions of the participant (participants) of civil legal relations, which are aimed at creating, changing or terminating legal relations".

Also, Article 290 should be supplemented, by adding a new paragraph 4: "4. The action of a participant (participants) performed regarding the participation in organizations or their management is considered to be a transaction, the rules of the present part are applied thereon only if not otherwise prescribed by law, other legal acts, charter or documents of internal regulation concerning the transaction's form, contents and validity." It is also necessary to regulate the relations connected with the consequences of invalidity of certain decisions both in general provisions about legal entities of the Code and in special laws regulating the particularities of this or that organizational-legal form of a legal entity.

The shortcomings of the Code and why not, also the shortcomings of the norms regulating corporate legal relations of the laws regulating the relations concerning different organizational-legal forms of a legal entity can be divided into:

- shortcomings in the phase of legal entity's creation,
- reorganization,
- exercising the rights of corporate legal relations' participants,
- in the phase of liquidation.

Even in Article 50(1) the definition of a legal entity does not actually reflect the factual state of things. By characterizing a legal entity as an organization "which has separate property as ownership…", the legislator contradicts its logic with its further legal regulation. In particular, by eliminating the minimum amount of statutory capital the legislator created such a situation that a legal entity can be created without having something in its ownership at the moment of its creation.

The situation is even more obvious in case of foundations for which the Code does not prescribe any requirements of having property in its ownership at the moment of its creation. So, in fact, in the current legal regulation the feature of having property in ownership is just the fixation of the possibility to have property by the right of ownership and this circumstance must be clearly expressed in the formulation of the legislative concept of legal entity.

Besides, the incomplete regulation of the process of legal entity's creation makes it objectively impossible to have property by the right of ownership at the moment of its creation[12].

Let us examine this issue by the example of a joint-stock company. The legal entity is considered as created from the moment of its state registration (Article 56(3) of the Code). Moreover, the current legislation allows the founders of limited liability companies to pay a certain part of the statutory capital during the period of one year after the state registration (Article 30 of the Law of the Republic Armenia "On limited liability companies"), and in case of joint-stock companies the legislation prescribes a mandatory condition according to which the shares must be entirely paid before the state registration of the company (Article 30(2) of the Law of the Republic Armenia "On joint-stock companies").

The study of corporate legislation allows dividing the process of joint-stock company's creation into two stages: first stage is the establishment of the company, and the second stage is the state registration[13] of the already established company. Article 10(3) and Article 30(3)(3) of the RA Law "On joint-stock companies"

[12] Avetisyan V.D. Features of Corporate legal Relations. "Bulleting of the Yerevan State University" 2011, #134.3, pp. 27-38. [Ավետիսյան Վ.Դ., Կորպորատիվ իրավահարաբերությունների առանձնահատկությունները, «Բանբեր Երևանի Համալսարանի 2011, N 134.3, 27-38].

[13] In case of on limited liability companies this classification does not work, as Article 8(4) of the RA Law "On limited liability companies" just prescribes that the company is considered to be established from the moment of its state registration in accordance to the procedure defined by law. And, depending on the peculiarities of the company's field of activity, in particular, banks, insurance companies, etc., the company is considered to be created from the moment of being registered in the authorized body. For example, see the Article 27(5) of the RA Law "On banks and bank activity".

prescribe[14] that when establishing the company all its shares must be distributed among the founders. Article 111(3) of the Code also has a similar legal regulation, but there is an exception: it uses the term ***distribute*** instead of the term ***allocate.*** Here a question arises: from which moment is the company considered as established and what do we understand by saying distributed and allocated shares?

The analysis of the current legislation allows to state that the company is considered as established from the moment of issuing the decision on the establishment of the company by its founding assembly (Law of the Republic of Armenia "On joint-stock companies", Article 12). So, it turns out that the law recognizes the fact of the joint-stock company's existence without the state registration of the legal entity, while the state registration shall be the recognition by the state of the legal capacity of the given legal entity (Law of the Republic of Armenia "On the state registration of legal entities", Article 3(1)).

The law does not clarify the question how it is possible to allocate the shares of the company which has not been created yet among the founders at the time of the company's establishment. And the term allocation, within the meaning of Article 33 of the Law "On joint- stock companies" means the shares which are sold and factually handed to the shareholders. The point is that we can speak about the allocation of the company's shares only after the creation of the company as only in that case can the company issue securities of documentary or non-documentary form. In our opinion, the use of the term allocation instead of the term distribution in the Civil Code actually makes it impossible to implement the requirements of the mentioned norm of the law.

Hence, we suggest using the term *distributed* instead of the term *allocated* in Article 10(3) of the RA Law "On joint-stock companies", and repeal the Article 30(3)(3) since it unnecessarily

[14] We find it necessary to mention that in the Law "On joint-stock companies" there are cases when a norm regulating the same legal relation is unnecessarily repeated, for example Article 10(3) and Article 30(3)(3) of the RA Law "On joint-stock companies".

repeats the contents of the above-mentioned norm. Some other amendments conditioned by the mentioned amendment should be done also in other articles, for example in Article 12(3)(g), etc.

It is also necessary to amend the Article 42(2) to read as follows: "2. At the time of company's establishment, after the state registration of the company, in compliance with the founding contract the value of shares which are to be handed to the shareholders must be fully paid until the state registration of the company."

It is also necessary to add a new paragraph 5 in Article 51 with the following contents: during 10 working days after handing the conducting and maintenance of the Registry to the professional organization, the Company must hand to the founders the shares which belong to them by the founding contract".

The study of the corporations' creation experience has shown that giving any property to the entity which has not been created or to empower it with property rights is quite problematic, and if we talk about real estate, then it is absolutely impossible.

In order to get out of such situation, some authors suggest envisaging in the law the possibility of creating a "preliminary company" which is applied in German law, according to which from the moment of signing the contract about creating the company by the founders (this is called the company's establishment) up to its registration we have a preliminary company which is not a legal entity but is empowered by some jurisdiction[15] characteristic only to the subjects of law. A similar procedure is envisaged by the Finnish law[16] about organizations. While, for example in England the law,

---

[15] Yem V.S., Kozlova N.V., Selyakow N.Yu Eternal Lamp // article in a book; Suvorov N.S. On Legal Entities from the point of view of Roman Law. Moscow 2000, P. 13. [Ем В. С., Козлова Н. В., Селяков Н. Ю., Неугасимая лампада //Вст. статья к книге: Суворов Н. С., Об юридических лицах по римскому праву. М., 2000г. С. 13].

[16] Kozlova N. V. Legal status of joint stock companies and limited liability companies in Finland // Legislation, 2001, #10, pp. 68-73. [Козлова Н. В., Правовое положение акционерных обществ и обществ с ограниченной ответственностью в Финляндии // Законодательство. 2001г. N 10. С. 68-73].

which dates back to 1844, envisages the organization's re-registration process preliminary, which must be done until the final establishment of the organization, consequently until receiving the governmental concession and final approval. Until the final approval (registration) no transaction can be made[17] related to the shares of the organization.

We believe that if we implement the mechanism of "preliminary company" (which exists in German law) in our legislation or if we remove the requirement of paying the statutory capital at the moment of the corporation's creation will help to a great extent to solve the above mentioned problems.

At first sight it seems that the relations linked to the reorganization of the legal entity are the sectors the most thoroughly regulated by the Code and by the RA Law "On joint-stock companies". But the study of the mentioned institute allowed us to reveal some issues which appear in this field and have their negative influence not only on the normal course of corporate legal relations but also they break the stability of civil legal relations in general.

The reorganization of a corporation is an legal phenomenon which is characterized by the processes of legal entity's creation and termination of its activity. The RA Civil Code as well as the RA Law "On limited liability companies" and the RA Law "On joint-stock companies" do not formulate the concept[18] of reorganization but simply define the forms of reorganization: merger, acquisition, separation, reformation.

A lot of formulations have been given in the theoretical literature in particular; some authors find that reorganization is a transaction, the others find that reorganization is a set of legal facts a

[17] Kaminka A.I. Stock companies. Part 1, Saint Petersbourg, 1902, P. 225. [Каминка А. И., Акционерные компании. Т. 1. СПб., 1902, С.225].

[18] We agree with the point of view expressed in literature according to which the word "reorganisation" is not rightly used in the Civil Code of RA. In essence, reorganisation is one of the types of reconstruction. See about this in more details in Barseghyan T. K. Civil Law of the Republic of Armenia. Part 1. Yerevan 2009, P. 126. [Բարսեղյան Տ. Կ., Հայաստանի Հանրապետության քաղաքացիական իրավունք, առաջին մաս, Երևան, 2009, էջ 126].

part of which consists of transactions, etc.[19]. But, in our opinion, the reorganization of a joint-stock company can be characterized as creation of a new subject or subjects of law on the material basis of an already existing legal entity through the termination of the existence of the subject of law which existed or by the expansion or reduction of the material basis.

Both the interests of the company's **creditors** and the shareholders constituting a **minority** can be often violated as a result of joint-stock company's reorganization. That is the reason why the Code and the RA Law "On joint-stock companies" prescribed some guarantees for protecting the rights of the mentioned persons. In particular, within 30 days after deciding to reorganize the company, the company shall provide a written notice thereon to all of its creditors. The notice shall contain information on the date of rendering the decision on reorganization, the type of reorganization, the parties involved, and the legal succession of the company's obligations.

In this case the creditors of the reorganizing company become entitled to demand from the company to provide additional guarantees that the obligations will be met, termination of obligations or early fulfillment, as well as compensation of losses. In case of receiving the notice about reorganization in form of merger, acquisition, separation or reformation, they must present these demands within 30 days from the moment of receiving the notice in case of merger, acquisition, or reformation, and within 60 days from the moment of receiving the notice in case of division or separation.

We think that giving quite broad rights to the creditors of the reorganizing company, the legislator did not take into account the interests of the reorganizing company. For example, two companies are reorganized in form of merger and the creditor's right to demand is ensured by pledge of property. A question arises here: why in such

[19] Naumov O.A. On the Protection of credits in the case of reorganization of debtors// Artbitral Practice. 2001, #3; Gabov A., Fedorchuk D. Reorganization of Stock Companies // Journal for shareholders. 2003, #4, pp. 33,34. [Наумов О.А., О защите прав кредиторов при реорганизации должников // Арбитражная практика. 2001. N 3; Габов А., Федорчук Д., Реорганизация акционерных обществ // Журнал для акционеров. 2003. N 3, С. 33, 34].

a situation do we give right to the creditor to demand from the company to provide additional guarantees that the obligations will be met, termination of obligations or early fulfillment, as well as compensation of losses?

We find that the creditor should use these rights only in case of such obligations, the fulfilment of which came up at the moment of giving the notice about the reorganization or the fulfilment is conditioned by the demand. In other cases, if the creditor offers an equivalent fulfilment of obligation, he must be deprived of the right to present the above mentioned demands.

The study of the reorganization process of joint-stock companies allowed discovering some issues characteristic to all the forms of reorganization which arise or may arise as a result of the reorganization of joint-stock companies.

The issues which arise during the reorganization are mainly related to the registry holding correlations of the reorganizing company and the company's share owners, as well as the problems which arise in case of recognizing the decision about reorganization invalid.

The point is that the companies, as a rule, provide the information about the reorganization processes which occurred or were occurring both before starting the reorganization process and after it to the registry holder of the share owners only after a certain period of time following the termination of the reorganization process.

In such conditions some practically insoluble problems appear during the times when the owners of the shares hold the registry which directly influence the persons who obtain the shares of the company which is undergoing reorganization or is already reorganized, as well as the protection of the rights of other participants of civil turnover[20].

[20] Avetisyan V.D. Some issues of reorganization of joint stock companies in Armenia. "Legality", Yerevan 2011, # 68, pp. 17-25. [Ավետիսյան Վ.Դ., Բաժնետիրական ընկերությունների վերակազմակերպման իրավական կարգավորման որոշ հիմնահարցեր Հայաստանի Հանրապետությունում, «Օրինականություն», Եր., 2011, թիվ 68, էջ 17-25].

In order to raise the effectiveness of the reorganization process of legal entities, we suggest as a mandatory condition to envisage an obligation for the reorganizing company to inform, within two working days after rendering the decision on reorganization, about it the body which carries out the state registration of legal entities and the registry holder, and to establish an obligation of publishing that information or providing the interested persons with this information. This will help minimizing the above mentioned problems arising in connection with the third persons who are related to the securities of the reorganizing company.

The problem becomes even more complicated when the decision on reorganization, as it was shown in the example of "X" company, is recognized as invalid and there is necessity to ensure the stability of civil legal regulation, to form trust towards the notes made in the registry of legal entities.

From this perspective we propose to prescribe a special three-month period for the demand of recognizing the decision on reorganization as invalid, and, at the same time prohibit by the Code the reorganized company to reorganize again or get liquidated until the termination of the mentioned period. Then, it would be expedient to define the consequences of invalidity which are applied in case of recognizing the decision on reorganization as invalid during the mentioned period; in particular, allow restoring the state which existed before making the decision on reorganization and envisage mechanisms for protection of the interests of creditors of the companies which were created as a result of reorganization. Afterwards, during the period of limitation of actions, it is necessary to exclude the possibility of invalidating the decision on reorganization and to establish joint liability for compensating the damages to the interested persons which were caused as a result of actions which were made by the persons who carried out an illegal reorganization.

We are deeply convinced that the shortcomings that exist in the phase of exercising the rights of corporation's participants are conditioned by the principle of legal regulation, according to which the interests of the corporation are often assimilated with the interests

of a major participant.

As a result, the major shareholders often abuse their right [21] by presenting their wishes as if these are the activities deriving from the corporation's interests, as a result of which not only the interests of the minority participants, but also the interests of the corporation are violated. We find it necessary to mention that such approach is not justified from the perspective of forming an atmosphere of development of corporate relations and the protection of the investments, especially when we talk about the joint-stock companies created as a result of privatization and their shareholders which are more than 150000 and constitute a minority. In this regard, the Law "On joint-stock companies" needs to be reviewed, in particular, the financial-economic crisis showed that while regulating corporate legal relations the preference should exclusively be given to the interests of the corporation and the remaining legal regulation must be built on that basis.

And, at the moment, we have plenty of norms which give the major shareholder the possibility to abuse his right. We can meet this kind of situations in case of consolidation, when upon the discretion of the major shareholder the minority shareholders can be thrown out of the company at the time of distributing the dividends, or in case of distributing the property remaining after the liquidation among the participants and in other cases.

Taking into account the necessity of balancing the interests of a joint-stock company, the company and the shareholder, individual shareholder and shareholder groups, as a solution[22] of problems

[21] Avetisyan V.D. Features of abuse of righ in corporate legal relations// Judicial Power, Yerevan 2013, #2/163. Pp.45-51. [Ավետիսյան Վ.Դ., Իրավունքի չարաշահման առանձնահատկությունները կորպորատիվ իրավահարաբերություններում, Դատական իշխանություն, Եր., 2013, թիվ 2/163, էջ 45-51].

[22] See about this in more details in Avetisyan V.D. Features of Consolidation of shares and problems of legal regulation in the Republic of Armenia: "Violation and legal responsibility", Materials of international academic-practical Conference, Tolyatti, 2012, pp. 1-13. [Аветисян В. Д., Особенности консолидации акций и проблемы правового регулирования в Республике Армения: "Правонарушение и юридическая ответственность", Материалы международной научно-практической конференции, Тольятти, 2012, С. 1-13].

which have arisen due to the consolidation of shares, we suggest making relevant amendments to the RA Law "On joint-stock companies" and condition the possibility of carrying out consolidation of shares by the following circumstances:

- the consolidation of shares must be carried out exclusively in favor of the company's corporate interests but not in favor of the interests of individual shareholders or a group of shareholders;
- the decision on consolidation must be made not by simple, but by quantitative majority of the votes;
- do not allow applying such a formulation of consolidation as a result of which the company will be obliged to change the size of the statutory capital;
- shareholders possessing fractional shares must be given the possibility to combine the fractional shares belonging to them in a certain period after making a decision on the consolidation and in this way form complete shares';
- in case of not using the right to combine the fractional shares in the period prescribed by the fractional shares' owners, an obligation has to be envisaged for the company to buy them back at a fair price.

The right of the corporation participant (shareholder) to take part in the distribution of profit is one of the key rights of the participant[23]. As a rule, by making an investment in the corporation the person has the objective of receiving a certain share from the profit.

The shareholder exercises his right to participate in the distribution of the profit by[24] receiving dividends corresponding to the shares belonging to him and among the share owners according to the sizes of shares they have in their statutory capital.

We find it necessary to mention that the RA Law "On limited

[23] In this work, the pecularities of the exercise of this right is mostly discussed in the example of a shareholder, within the framework of the law on joint-stock companies as the legislation about limited liability companies does not regulate this matter in details.

[24] Mogilevskyi S.D. Joint-stock Companies. Mosocow, 1998, P. 83. [Могилевский С.Д. "Акционерные общества", изд-во "Дело",М., 1998, С. 83].

liability companies" does not define the concept of "profit" and the RA Law "On joint-stock companies" just uses the concepts profit and accumulated profit. In general, we call dividends just the part of the profit (that is to say, the profit which remained after paying all kinds of taxes and mandatory payments) which is subject to be distributed among the shareholders according to their participation in the shares and is counted per share[25]. Besides, in case of joint-stock companies, it is allowed to include in profit also the profit that was accumulated during the previous years but has not been paid (Article 49(2) of the RA Law "On joint-stock companies).

The subjective right of the corporation participant to receive a dividend arises after the authorized body of the corporation renders the decision about distributing the profit among the corporation participants, because only the declared profit is subject to be paid. The decision of the general assembly or the council of directors about paying dividends is the only legal fact and the obligation of the corporation to make a payment in the terms and procedure defined by the decision.

V. V. Laptev finds that before the corporation makes the relevant decision, the shareholder (the participant) does not have any subjective right to receive dividends which allow him to talk about[26] the conditional nature of this right. Indeed, until making the relevant decision the participant of the corporation does not have the right to receive dividends: a right which can be exercised within the framework of regulated legal relations, a right which can be protected by court, and the corporation does not bear the obligation to pay dividends. But the size of the dividends in the joint-stock companies, depending on the type and category, can be different.

Some authors find that in case of preferential shares for which the size of dividends subject to be paid is predetermined by the

[25] Commentaries to the Federal Law on Joint Stock Companies. Moscow 2002, P. 240. [Комментарий к федеральному закону об акционерных обществах. изд-во "Юринформцентр". М., 2002, С. 240].

[26] Laptev V.V. Joint-Stock Companies. Moscow, 1999. P. 67. [Лаптев В. В. Акционерное право. М., 1999. С. 67].

charter of the company and no decision is required for it, the company is obliged to pay the dividends to their owners. The company, which refuses to pay the annual dividends by such shares, will be considered as a lawbreaker, and the shareholder will have the right to present a demand of confiscating the non-declared dividends except for the case if the profit was paid partially or a decision was made about[27] not paying dividends at all.

Until adopting the Russian Federation Law "On joint-stock companies", in Russia there was a Regulation on the procedure for paying interests for the dividends and bonds which was adopted by the Ministry of Finance and Economy on January 10, 1992. The Regulation also prescribed that the payment of dividends with equity shares is not considered to be the obligation of the company and if the income of the company is sufficient for paying fixed dividends with preferential shares, the company does not have any right to refuse to pay it to the owners of the shares.

Upon the Decision of the RA Government No 1194 of December 5, 2001, in order to regulate the process of paying the dividends which are received from the state shares in companies with state participation, the government defined when it is mandatory for the general assembly to make a decision on paying the annual dividends, for example in case of companies with more than 50 percent state participation, the general assembly of the shareholders has to vote and approve the issue of paying 20 percent of the profit received for the state participation as an annual dividend to the state budget of the Republic of Armenia.

We think that in the conditions of legal regulation existing in RA, in case of not making a decision about paying dividends, the shareholder is deprived of the right to demand shares from the

[27] Legal Regulation of the Joint-Stock Companies (Corporate Law). Gubina E.P. (ed.) Moscow, 1998, P. 152; Management and Corporate Control in Joint-stock Companies (E.P. Gubina, ed.)- Moscow, 1999, pp. 70-74 (Chapter written by D.V. Lomakin). [Правовое регулирование деятельности акционерных обществ (Акционерное право) Под ред. Е. П. Губина. М., 1998, С. 152; Управнление и корпоративный контроль к акционерном обществе/ Под ред. Е. П. Губина.- 1999, С. 70-74 (автор главы Д. В. Ломакин)].

company by judicial procedure. Moreover, in such conditions the law allows the owner of equity shares to participate in the management of the company on equal basis with the owners, and if during the succeeding three years the dividends which belong to the preferential shares are not paid, the shareholder can apply to the court demanding the liquidation of the company through a judicial procedure (Article 38(7) of the RA Law "On joint-stock companies").

Regarding this problem, the RA Court of Cassation expressed the following position in its decision rendered with respect to the case No 3-789(TD): deciding the size of the limited liability company's profit subject to be distributed is the exclusive authorization[28] of the general assembly which is the highest management body of the company. And in the given case, the first instance court sustained the claimant's request to determine the profit subject to distribution (in essence, made a decision about paying dividends instead of the assembly) and oblige the company to pay it, while the right to make a decision concerning the mentioned matters is the exclusive authorization of the general assembly. In this case, the RA Court of Cassation, in essence, responded to the issue when the participant of the company obtains the right to receive dividends, conditioning it with the circumstance of making the relevant decision by the authorized body.

There are some countries the legislation of which has another approach for this matter; for example, in England and in the USA the shareholder has the right to demand through a judicial procedure to be paid the dividends that belong to him even in case the company did not declare any dividends, but there is profit accumulated as a result of the corporation's activity.

In the cases of the mentioned category, the claimants must prove that the corporation has the funds necessary for paying dividends and the effectiveness of using those funds, as well as the fact that the directors or the owner of the control package have

[28] Decision of the Court of Cassation of the Republic of Armenia of May 18, 2007 with respect to the civil case No 3-789 (TD).

abused[29] their rights.

We find that the reason behind such problems is the incompleteness of the RA legislation regarding the payment of dividends. In particular, the management bodies of the company should not have the possibility, for example, to not make decision about paying dividends for 10 consecutive years and use the accumulated profit for this or that program's realization, because in such a situation the rights of shareholders who constitute a minority can be violated. Let us imagine a situation when a major shareholder is at the same time the director of the company, the president of the council and is not keen on making a decision about dispensing the profit, because without that decision he receives premiums, buys an expensive car, a service apartment for him, etc., and according to the current legislation, the shareholders who constitute a minority are deprived from the possibility to object his actions.

We suggest making relevant amendments in the RA Law "On joint-stock companies" and in the RA Law "On limited liability companies" and limiting the term of not making a decision about paying dividends by two years. After that, the shareholders who are keen on the company's development can receive their dividends, issue supplementary shares and again do their investment in the development of the company. We think that in this way it will be possible to balance the interests of the corporation, the interests of the major shareholders and the interest of the shareholders comprising a minority.

The joint-stock has the right to make a decision (announce) about the payment of quarterly, semi-annual, or annual dividends for distributed shares (Article 49(1)(10) of the RA "Law on joint-stock companies"). And the limited liability company can make a decision about dispensing the profit only once a year (Article 24(1) of the RA "Law on limited liability companies").

The company has to pay dividends announced for each type (category) of shares. As a rule, dividends are paid in monetary terms;

[29] Mozolin V.P. Corporations: monopolies and law in the United States. Moscow, 1996, P. 349. [Мозолин В. П. Корпорации; монополии и право в США. М., 1996, С. 349].

however, in cases prescribed by the charter, they can be paid also by other property, including the company's shares. If the company's charter envisages the possibility of paying the dividends by other property, then it is necessary to clearly define in the charter the cases and the procedure for paying the dividends by other property.

We think that by saying to pay to the shareholder another property instead of dividend, we should understand any property which is not removed from the turnover or does not have limited turnover. In our opinion, giving the right to do payments by other property can become a reason for various violations; for example, in that way the property in the ownership of the company can become the ownership of the shareholder or shareholders, or while making the decision about paying dividends by property it may be decided to pay dividends to a group of shareholders in one type of property and to the other group in another type. For example, to hand the finished product to the major shareholder, and the semi-finished one to the shareholders comprising a minority.

In order to exclude such situations, we suggest excluding the possibility of paying dividends through property.

Dividends are paid from the net profits or accumulated profits of the company. And for a certain category of preferential shares, dividends can be paid from the account of funds of the company which are created especially for that purpose.

According to the types and categories of the shares, the council makes the decision about interim (quarterly and semi-annual) dividends payment, the size and payment form of dividends, and the general assembly, upon the council's suggestion, makes the decision about the annual dividends payment, the size and payment form of the dividends.

The interim dividend size cannot exceed the 50 percent of the dividend which was distributed by the results of the previous financial year. And the size of annual dividends cannot be more than the one offered by the council and less than the size of the interim dividends which are already paid. If the annual dividends' size, per individual types and categories of shares, is defined by the council's decision as equal to the interim dividends which are already paid, then annual dividends are not paid for that types and categories of

shares. And if the annual dividends' size, per individual types and categories of shares is defined by the assembly's decision as more than the sizes of the already paid interim dividends, then the annual dividends for those types and categories of shares are paid by the difference of money of the defined annual dividends and the interim dividends which were already paid during the given year.

The RA Law "On joint-stock companies" does not give an answer to the question about how we should act in case when while summarizing the annual results it turns out that after paying the dividends for the quarter, with the financial year's results, the company has no profit or worked with losses. In current legal regulation, no claim can be presented to the shareholders who received the dividends, except for the case when it turns out that the decision was made as a result of doing mandatory indications by the shareholder, and the company is close to bankruptcy. In this case the rights of the corporation's creditors, and why not, also the interests of the corporation are violated.

In order to exclude the possibility of the above-mentioned situations, we suggest limiting the jurisdiction of the council in making a decision about the payment of interim dividends and give the joint-stock company the possibility to make a decision about the payment of dividends only after summarizing the results of the financial year.

The deadline for paying the annual dividends is prescribed by the charter or by the council's decision about paying dividends. The deadline for paying the interim dividends is defined by the council's decision on paying the interim dividends, but not later than 30 days after the moment of rendering the decision.

For each payment of dividends, the Council shall compile the list of shareholders who are entitled to receive dividends, which includes: in the case of interim dividends, the shareholders of the company that were listed in the company's shareholder registry at least 10 days before the adoption of the Council decision on payment of interim dividends; and in the case of annual dividends, the shareholders of the company that were listed in the company's shareholder registry at the date when the list of shareholders who are entitled to participate in the company's annual meeting of

shareholders was compiled (Article 49(4) of the RA "Law on joint-stock companies").

In our opinion, giving jurisdiction to the council to compile the list of the persons who are entitled to receive dividends 10 days before making the decision on the payment of interim dividends may give the council members the possibility for making different abuses.

For example, the president of the Council, or his friend, his relative sold his shares or a part of them 7 days before making the decision on the payment of interim dividends and suggests compiling the list of the persons who are entitled to receive dividends 9 days before making the decision. As a result, the dividend is received not by the new owner of the share, but by the former owner which, in our opinion, is inadmissible. That is the reason why we suggest compiling the list of the persons who are entitled to receive interim dividends after the date when the council makes the relevant decision.

In case of a company undergoing liquidation, the right to receive a certain part of the property is one of the most important rights of the shareholder. The liquidation commission, in compliance with the procedure (Article 27(2)(2) of the RA Law "On joint-stock companies") approved by the assembly for distribution of the property remaining after the satisfaction of the creditors' claims, distributes it among the shareholders in the following sequence: firstly, the payment for shares that must be bought back by the claim of the shareholders; secondly, the payment for the dividends accrued for the preferential shares but not paid; thirdly, the payment of liquidation value of preferential shares; fourthly, the distribution of the remaining property of the Company amongst the holders of equity (ordinary) shares and all types of preferential shares.

Taking into consideration the comparative best practice and foreign legislation, we find that the above-mentioned sequence prescribed by RA Law "On joint-stock companies" is not fair and should be changed. In particular, the logic of the legislator is not clear regarding the fact of giving a priority right to the claims of equity share owners who presented a buying-back claim towards the owners of preferential shares. In such conditions, 25 percent of share owners, taking advantage of the right given to them by law, may

demand the buying-back of the shares and as a result make it impossible to fulfill the claims of the preferential share owners. That is why we suggest moving the people of the first priority who have the right of the claim into the third priority, and the claims of second and third priorities respectively to the first and second priorities.

Besides, it is also unclear that the owners of preferential shares who ***received the liquidation value*** of preferential shares have the right to participate in the distribution of the remaining property along with the equity share owners of the fourth turn. Moreover, how can an owner of preferential share having 1000 Armenian drams nominal value participate in the distribution of the remaining property along with an owner of equity shares having 10000 drams nominal value? We find that such a legal regulation is illogical, and the owners of preferential shares should be deprived from the fourth turn's right to demand.

Giving by law the possibility to the general assembly to confirm the procedure for the distribution of the remaining property after the fulfillment of creditors' claims, can lead to the violation of the rights of the shareholders who constitute minority. In particular, according to that procedure, the shareholder who has 76 percent participation in the company can set that, for instance, the real estate passes to the major shareholder, and the remaining removable stuff (equipment which is out of order, materials used in the production cycle, etc.) passes to the shareholders constituting minority.

We suggest setting the procedure for distributing the property remaining after the fulfillment of creditors' claims by law. In particular, prescribe that the mentioned procedure must be confirmed by the unanimous votes of the assembly participants. In case there is no unanimous agreement, the property must be sold by public auctions, and the other accumulated financial means must be distributed among the shareholders in the proportion mentioned in law.