

# CIVIL LAW AND THE TRANSFORMATION OF STATE PROPERTY IN POST- SOCIALIST ECONOMIES: ALTERNATIVES TO PRIVATIZATION

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## I. INTRODUCTION

The history of socio-economic progress proves that social relations regarding the production of material goods are primary, and social relations regarding the distribution, exchange, and consumption of material goods are secondary. A society can neither stop producing nor stop consuming. As such, an economy generally consists of two basic zones: production and consumption. Indeed, if everything starts and recommences in the first zone, then it is completed and annihilated in the second one. In between these two zones lies a third one, brisk like a brook, but distinguishable from the first two. This is the zone of exchange, or if you prefer, the market economy.

In order for a commodity market to exist it is necessary for those subjects who initially intend to alienate and appropriate exchangeable goods (i.e. people or business entities) to be in command of the goods as "their own" belongings. In other words, they must be able to possess, use and control goods in accordance with their own interests and by their own free will. Traditionally, the term "ownership" has been used for the definition of such relationships.<sup>1</sup>

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1. Classical Roman jurisprudence, which founded the basis of civil law, considered "ownership" (*dominium*) the absolute, unrestricted and exclusive domination over the material thing; a right which is free from any restrictions in its essence, and absolute by the means of its protection. For instance, in Justinian law this right was designated as "*plena in re potestas*," which means "a plenum of power of the master over his property" or, in modern interpretation, "a full domination by the owner." See, e.g., J. INST. 1, 9, 12; DIG. 2, 1, 13, 1; DIG. 14, 1; see also M. BARTOSHEK, RIMSKOE PRAVO: PONJATIA, TERMINI, OPREDELENIA [THE ROMAN

In socialist countries, which began their post-revolutionary socialist reforms with the country-wide nationalization of private property, the term "ownership" has been assigned a special economic characteristic and a specific legal meaning. In these countries, the ownership of capital assets is legally vested in "the community." As a practical matter, this means that ownership rests in the hands of those who enjoy political power. Property law was replaced by a pervasive system of "entitlement," vested in those who were appointed by the government to make decisions affecting resource use. Unlike legal property rights, entitlements in a command economy are ambiguous in their content, contain numerous restrictions, and are not freely transferable.

The term "property of the whole people" does not provide straight and clear answers to the question of "whose is it." Economic, social and legal "depersonalization" of property leads to a situation where there are no subjects (collective and individual) who possess the combined integral interest and valuable characteristics of a owner-proprietor. Such a "diffusion" of the right of ownership, and its anonymous character are ridiculous; a fact true not only from an economic point of view, but also from the theoretical position of classical civil law. This is why foreign businessmen, as well as practicing lawyers in Russia and other socialist countries, must sometimes face the very practical problem of having to locate the owners of particular pieces of land or real estate in order to resolve property disputes. These issues are discussed in some detail below.

Certainly, the "property of the whole people" is a purely political slogan. It does not make any legal sense, and it does not correspond with any traditional understanding of the theory of ownership under civil law. This article intends to clarify some key legal terms of civil law regarding the ownership and law of real estate in Russia and other formerly socialist countries. Many of these terms are quite confusing even for Russian lawyers. This author will analyze the different legal institutions of real estate law, most of which are unknown to foreign readers despite their crucial significance and importance for business transactions in these countries.

Indeed, the crucial issue relates to the role of entitlement. In a private market economy, individuals can establish property rights that can be freely bought and sold. Rights to productive assets can be transferred through the capital market, which

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LAW: CONCEPTIONS, TERMS, DEFINITIONS] 113 (Juridicheskaja Literatura ed., 1989). Certain restrictions on this right became known to civil law much later, in the era of capitalist development. However, the highest level of such restrictions on the right of ownership was achieved by civil law in socialist countries.

makes it possible to separate ownership from production decisions. One of the basic motivating forces behind communist ideology, on the other hand, was the separation of ownership from the means of production in order to overcome the alienation of the working class. Apparently, this social-political approach has affected the theory of privatization in Russia, as well as in other post-socialist countries, since it is basically incompatible with the essence of Western "pure privatization." The purpose of this article is to help the reader better understand the cause, content, form, and meaning of the distinctive features of post-socialist privatization, as well as the alternatives to such "pure privatization."<sup>2</sup>

## II. DECENTRALIZATION AND ITS ROLE IN THE TRANSFORMATION OF A PLANNED ECONOMY INTO A MARKET-ORIENTED SYSTEM

The economic concept of privatization is not new; it can be found in the writings of Adam Smith as early as 1776.<sup>3</sup> Privatization is the opposite of nationalization: privatization of state enterprises reflects the predominance of capitalist thinking, whereas nationalization is an obvious sign of socialist development.

There is no longer any question that crucial economic reforms are necessary for the transition of a socialist economy from general planning system to a market-oriented system. The heavy, clumsy monolith of state property based enterprises is no longer capable of assuring its self-repayment under market conditions. Applying the communist theory of "the revolutionary situation" to post-socialist countries, we can find major economic preconditions of the revolutionary situation. Fundamental economic reforms are necessary when "the production relations be-

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2. The theme of post-socialist privatization is not virgin territory for American readers. See, e.g., L. GRAY COWAN, *PRIVATIZATION IN THE DEVELOPING WORLD* §§ 2, 6 (Greenwood Press ed. 1990); STANLEY FISCHER, *PRIVATIZATION IN EAST EUROPEAN TRANSFORMATION* (National Bureau of Economic Research Working Paper No. 3703, 1991); EDUARDO BORENSZTEIN AND MANMOHAN S. KUMAR, *PROPOSALS FOR PRIVATIZATION IN EASTERN EUROPE* (June 1991) (on file with *International Monetary Fund*, Vol. 38, No. 2); Janos Kornai, *The Affinity Between Ownership Forms and Coordination Mechanisms: The Common Experience of Reforms in Socialist Countries*, 4 J. ECON. PERSP. 131, 131-47 (1990). However, in this article the author will focus on issues such as: Does privatization have any worthwhile legal alternatives? Is privatization crucial? Is privatization the only way to resolve problems in planned economies? Why does privatization in Russia bear the burden of old socialist commando-administrative methods?

3. ADAM SMITH, *THE WEALTH OF NATIONS* 7-16 (E. Cannan ed., The Modern Library Edition 1937) (1776).

come a brake on the development of productive forces" in the economic development of a country. However, this "revolutionary situation" is now being applied to socialist production relationships instead of the capitalist markets that it was designed for. The decentralization of the command-administrative system is an urgent problem faced by Socialist countries. However, the roots of centralization lie in state ownership of the basic means of production such as state-owned enterprises, factories, small and large stores, real estate, land, material and natural resources. This leads to state monopolies over certain productive activities through the economic and political dictates of the Ministries and the Party, as well as government control over production, distribution, exchange, and consumption of commodities.

The control over *production* was realized through the Gosplan system (State Planning Agency). Gosplan not only developed the Soviet economic five-year plans, but also set up operative plans for each year, which provided the Ministries and Government Departments with certain quotas ("showings") for each branch of industry and consumer service. Ministers and Government Departments were established as governing bodies in different branches of industry, agriculture, consumer services, education, public health, news media, and even in such regulation-resistant areas such as culture, theater, sports and entertainment. The Ministers and Government Departments developed their own quotas and applied them to state-owned enterprises, factories, and collective farmers.

The Government authority over *distribution* was exercised through the Gossnab system (State Supply Agency), which established reciprocal commodity deliveries between enterprises. Gossnab also instituted control over the supply of material and fuel resources, semi-finished products, spare parts, and equipment. As a rule, nobody could go over the head of Gossnab and independently maintain direct commercial connections between the enterprises.

The Government also managed an *exchange* of commodities through the system of state trade (including State wholesale trade centers and State retail trade stores and shops). Special warehouses of foodstuffs and commodities were organized which distributed goods through thousands of state-owned grocery stores and department stores. Everything was run according to the state plan. The vegetable warehouses sometimes allowed a harvest to rot in the depository in order to avoid violating predetermined state quotas for distribution (which were often treated as administrative ordinances). On the other hand, the stores refused to accept all lower-priced essential commodities that did not accord with their interests in achieving high sales

quotas. The warehouses sometimes served local administration as places for storing and accumulating goods for special political events such as election campaigns and holidays, and leading astray inspectors for "the well-being of the people." Commercial business was generally illegal. There were well-known provisions of the Criminal, Administrative and Civil Codes which prohibited buying and reselling goods for the purpose of profit. The Civil Code recognized a whole system of remedies to reimburse the state for the so-called "unearned income" of its citizens. The Criminal Code treated speculation, which was literally defined as "buying and reselling commodities for the purpose of profit," as a very serious crime. This system gave rise to wide-spread corruption and abuse, and the development of the so-called "black market." Having certain executive freedom and being in possession of actual power over commodities, those individuals who were in charge of the distribution of goods on behalf of the government, could, and often did, give special preferences to certain customers even when the commodities were not in short supply. In return for such preferences, recipients were often asked to give preferences in return or they were asked to provide direct material benefits such as bribes, graft, tips, or other forms of extortion. In a certain sense, we see here the existence of a peculiar antipode of the market—the mutual exchange of preferences.

Furthermore, the administrative-command system exercised its control even over the *consumption* of goods by the population. Because of shortages in certain kinds of goods, a system of "coupon distribution" was practiced. Specifically, Russian municipalities issued coupons for sugar, butter, sausage, meat, soup, sweets, vodka, alcoholic beverages, cigarettes, gasoline, and other commodities. According to the Civil Code, passed in 1961, Russian citizens could not possess more than one house or apartment. Civil Code 1961 stated that such a living space could not exceed 60 square meters, with some exceptions made for large families. Special administrative restrictions were also imposed on any individual who purchased more than one car for personal purposes. In 1986 a system of control over personal income was introduced to allow government fiscal organs to demand a declaration of income from anyone making a purchase of more than 10,000 rubles (\$1,667 in 1986).

Thus, the central planning system used in the former Soviet Union clearly failed to provide a standard of living comparable to that of industrial economies in the West. Decentralization became a major task and a determinative factor in later economic reforms. The term "decentralization" includes the following interdependent elements: a) demonopolization, b) deintegration, and c) privatization.

The term "*demonopolization*" means the liquidation of privileges or peculiar advantages vested in one or more state enterprises. This consists of the exclusive right (or power) to carry on a particular business or trade, to manufacture a particular article, or to control the sale of the whole supply of a particular commodity.

One of the five main characteristics of capitalism, according to Vladimir Lenin's work, "Imperialism, the Highest Stage of Capitalism,"<sup>4</sup> is the monopolization of industrial capital. This was almost an academic phrase of communist theory since the 1920's. Ironically, the most significant concentrations and monopolization of industries have been achieved in socialist countries. For instance, in the former Soviet Union there was only one airline company, "Aeroflot," one savings bank, "Sberbank," one insurance company, "Gosstrach," one telephone company, one gas company, one electric company, and so on for hundreds of other monopolized industries. The largest and most powerful monopoly was the state itself. Indeed, the basis for such a monopoly was state ownership. As a result, identical prices for the same goods can be found throughout the entire country. The whole country essentially became a large company with its own subsistence economy. Competition in a market sense did not exist. "Socialist competition" meant nothing more than a contest to achieve established quotas.

The term "*deintegration*" refers to the management reform of the national economy by means of reorganizing Ministries and Government Departments, and abolishing systems of control over the distribution and consumption of commodities.

As we have seen, demonopolization and deintegration are primarily oriented towards reforming the framework and organization of the national economic pattern. However, the third element of decentralization, privatization, can be considered as a way of completely abolishing the basis of the whole socialist command system, the concept of state ownership.

### III. TRANSFORMATION OF THE NATIONAL ECONOMY WITHOUT PRIVATIZATION

Before discussing possible alternatives to privatization, it is necessary to find some common ground for all or most of the opposing theories and approaches. As this common ground I will consider the majority position that the decentralization of the national economy, along with the other major reforms which

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4. VLADIMIR IL'ICH LENIN, IMPERIALISM, THE HIGHEST STAGE OF CAPITALISM (E. Varga & L. Mendelsohn eds., 1938).

took place in the former Soviet Union and other former socialist countries, was necessary.

The alternative to a market and commodity production system is a system of centralized command-administrative control and planned-administrative distribution. To a certain degree this can be compared with a natural economy, but since a return to this system has been rejected by common practice, former socialist countries no longer have any alternatives other than the market and commodity production system.

We can conclude that Russia has made its choice already. Notwithstanding the still considerable influence of conservative communist parties in the former Soviet Union, the necessity for economic reforms are almost beyond question. One striking example of the changed political alignment of forces was seen on April 25, 1992, in the national referendum where the absolute majority of the Russian population supported the economic reforms proposed by President Yeltsin. The significance of the April 25th referendum is not so much in the people's solid support of Yeltsin and his reforms, but rather their rejection of the threat of communist restoration. While this vote is not proof of the endorsement of radical economic reform, it does show that the concept of centralized economy has been rejected.

Nevertheless, there is still a question of whether the goal of efficiency can be achieved by maintaining the status quo of state ownership without establishing a legal mechanism requiring state enterprises to respond to market signals in their operations.

#### A. AMERICAN AND WESTERN APPROACH: "DO AS WE DO."

There was considerable discussion on the question of the efficiency of state-owned enterprises in Western literature during the 1970's in the context of a more rational central planning system.<sup>5</sup> The arguments for possible methods of transformation of state property have continued during the whole period of "perestroika."<sup>6</sup> Although the author of this article is a staunch supporter of privatization, this article must consider the fact that the answer to the above-stated question may not be as simple as it is

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5. See, e.g., WODZIMIERZ BRUS, *THE MARKET IN A SOCIALIST ECONOMY* (Angus Walker, Trans., Routledge & Kegan Paul eds., 1972); WODZIMIERZ BRUS, *THE ECONOMICS AND POLITICS OF SOCIALISM: COLLECTED ESSAYS* (Routledge & Kegan Paul eds., 1973); ALEC NOVE AND D.M. NUTI, *SOCIALIST ECONOMICS: SELECTED READINGS* (1972); PETER WILES, *ECONOMIC INSTITUTIONS COMPARED* (1977).

6. See, e.g., PRAVO SOBSTVENNOSTY V SSSR: PROBLEMI, DISCUSSII, PREDLOZHENIA [THE LAW ON OWNERSHIP IN THE USSR: PROBLEMS, DISCUSSIONS, PROPOSALS], (J.K. Tolstoy & V.F. Yakovlev eds., Juridicheskaya Literatura 1989).

pictured by some American and Western researchers and analysts.

The central argument here is that private sector organizations, where rights to profits are clearly defined, will perform better than public sector organizations, where rights are diffused and uncertain.<sup>7</sup> However, the statement that the socialist countries' practical experiences suggest "that the answer is in the negative" is not totally convincing.<sup>8</sup> As a matter of fact, most socialist leaders today do not dispute the lack of economic success of past epochs of developing socialism in Eastern Europe, China, and the former Soviet Union. Instead, they shift their political emphasis toward eliminating the extremes of centralization in a planned basic economy and they attempt to substantiate their own theories of economic reforms by revising the old state ownership system.

Secondly, the theoretical reasons for "why governments should privatize" that appear in American legal literature fail to consider the uniqueness of ownership in the former Soviet Union and other socialist countries, or the specific Civil Law Regulations prevailing in the countries of continental law. These theories contend that the "panacea" of privatization is on its last legs. On the one hand, they are very generalized and abstract; on the other, they are unreasonably specific. For example, we cannot push into the Procrustean bed all the different historical, legal, and economic forms of privatization; neither can we prescribe the same known economic and legal formula for all different countries and socio-economic systems. Obviously, the French experience of privatization is unsuitable for Russia and Mexican lessons are useless for Eastern European, Cuban, Chinese and Vietnamese enterprises. Mary M. Shirley, a leading expert and the Chief of the Public Sector Management and Private Sector Development Division of the World Bank, appeals to concrete examples of Mexican enterprises in her attempts to elucidate the necessity of global privatization. However it is doubtful that her examples are illustrative of either the Soviet Republic factories, or even of other factories within Mexico itself.<sup>9</sup>

Nevertheless, Shirley makes two interesting points: a) that all types of privatization "have the potential to increase so-called

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7. A. Alchian, *Some Economics of Property Rights*, 30 *IL POLITICO* 816-29 (1965); *THE ECONOMICS OF PROPERTY RIGHTS* (Eirik G. Furubotn & Svetor Pejovich eds., Ballinger 1974); Louis De Alessi, *The Economics Of Property Rights: A Review Of The Evidence*, 2 *RESEARCH IN LAW AND ECONOMICS* 1-47 (Richard O. Zerbe, Jr., ed., 1980).

8. BORENSZTEIN & KUMAR, *supra* note 2; KORNAI, *supra* note 2.

9. Mary Shirley, *The What, Why, and How of Privatization: A World Bank Perspective*, 60 *FORDHAM L. REV.* 23, 24-28 (1992).

*static efficiency*," which means "pushing enterprises to operate cost effectively on their production frontier;" and b) that "only by privatizing property rights . . . can you bring *dynamic efficiency*—in other words, new investment, or innovation. Leases and contracts do not stimulate dynamic efficiency, because they do not create stakeholders with a clear interest in putting their own funds at risk."<sup>10</sup> Generally, her point of view reflects the classical understanding of the significance of privatization.<sup>11</sup> "Efficiency" is the bottom line of this consideration.<sup>12</sup> Nothing can be said against that. However, in this connection, we cannot help but notice some weak points with regards to post-socialist transformation of ownership in the "do as we do" position. To find an appropriate prescription for post-socialist economies which are seriously sick with the disease of centralization we should keep in mind some of these possible objections that may be raised by the opponents of denationalization.

#### B. DISCREPANT FACTA CUM DICTIS.<sup>13</sup>

Accordingly, the general question of whether ownership is an important determinant of economic performance needs to be addressed. First of all, as could be expected, there exists some contrary evidence which leads to the exact opposite conclusions regarding the efficiency benefits of private enterprises. In their widely quoted 1982 survey, Borcharding, Pommerehne and Schneider,<sup>14</sup> reached the conclusion that given sufficient competition between public and private producers (and no discriminating regulations and subsidies), the differences in unit cost between the two systems are insignificant. From this we may conclude that the causes of inefficiency in public producers are not so much the difference in the transferability of ownership but rather the lack of competition. Additionally, in 1983 another widely quoted survey on the topic, written by Millward and

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10. *Id.* at 24.

11. See, e.g., David Heald, *The United Kingdom: Privatization and its Political Context*, 11(4) W. EUR. POL. 31-48 (1988); D. Heald and D.R. Steel, *The Privatization of UK Public Enterprises*, 52 ANN. PUB. AND CO-OPERATIVE ECON. 351-67 (1981); J. A. Kay and D.J. Thompson, *Privatization: A Policy in Search of a Rationale*, 96 ECON. J. 18-32 (1986); MANEUR OLSEN, *On the Priority of Public Problems*, in *THE CORPORATE SOCIETY* 294 (Robin Marris ed., 1974); ANNAMARIE HAUCK WALSH, *THE PUBLIC'S BUSINESS* (1978).

12. See, e.g., *PRIVATIZATION AND ECONOMICAL EFFICIENCY: A COMPARATIVE ANALYSIS OF DEVELOPED AND DEVELOPING COUNTRIES* (Attiat F. Ott & Keith Harley eds., 1991).

13. According to Cicero this phrase means: "The facts are controversial to speeches."

14. T. E. Borcharding et al., *Comparing the Efficiency of Private and Public Production: Evidence from Five Countries*, ZEITSCHRIFT FUR NATIONALOKONOMIE [J. ECON.], Supp. 2, 127-56 (1982).

Parker, independently arrived at the conclusion that there is no systematic evidence proving that public enterprises are less cost effective than private firms.<sup>15</sup> A similar conclusion can be found in another piece of Parker's research from 1985.<sup>16</sup> Finally, C.W. Boyd summarizes the relevant literature in his 1986 survey and arrives at the conclusion that there is no systematic difference between performance under public and private ownership.<sup>17</sup>

Therefore, it is not quite accurate to diagnose the complicated economic situations by using the political method of "good example" alone. Transformation of ownership relations, which is the basis of a socio-economic system, proceeds far more painfully than one might imagine. State industry enterprises face steep drops in output production caused by the demolition of stable and close business links between suppliers. Indeed, new-born private firms, often start the reckless chase of swift and incredible profit by promoting severe speculation over the production of state enterprises. The privatized firms cannot hope to reach the level of industrial development of their predecessors, the state-owned enterprises, in such a short time. This is mostly due to the immense pressure and dictates of the huge state monopolies in energy and transport, the loss of historically established economic and business ties with their former suppliers, the elimination of government orders for production which guaranteed the full distribution of goods, the undeveloped bank and credit system, the severe shortage of currency, the seizure of land from trade turnover and commodity exchange, the absence of basic ethical principles of market coexistence and commerce, the undeveloped commercial and business legislation, the political instability, and the rudimentary remnants of communist thinking and socialist egalitarianism. As we shall see, the sweet dreams of a "panacea" of privatization can easily turn into disappointment, bitterness, and despair.

As an illustration, on March 18, 1993, the Polish Parliament rejected a government plan for the privatization of large firms. Much of Poland's economy, including small businesses, had already been privatized. The program, first announced two years ago, envisioned handing control of up to 600 of the largest state

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15. R. MILLWARD & D.M. PARKER, PUBLIC AND PRIVATE ENTERPRISE: COMPARATIVE BEHAVIOR AND RELATIVE EFFICIENCY (R. Millward et al. eds., Public Sector Economics, Longman 1983).

16. D.M. Parker, *Is the Private Sector More Efficient? A study in the Public v. Private Debate*, PUB. ADMIN. BULL. 2-23 (Aug. 1985).

17. C. W. Boyd, *The Comparative Efficiency of State-Owned Enterprise: A New Challenge in International Business*, in MULTINATIONAL CORPORATIONS AND STATE-OWNED ENTERPRISES: A NEW CHALLENGE IN INTERNATIONAL BUSINESS, RESEARCH IN INTERNATIONAL BUSINESS AND INTERNATIONAL RELATIONS (JAI Press ed., 1986).

enterprises to more than a dozen Western consultants who would manage, restructure and prepare them for sale or flotation on the Warsaw Stock Exchange. But deputies criticized the plan, saying this would take \$10 billion worth of assets out of government hands. Prime Minister Hanna Suchocka told reporters that "this is a serious sign that there is a possibility of turning back from the path of reform."<sup>18</sup> In spite of the fact that the Polish Parliament finally approved the Plan of privatizing the bulk of the largest state owned industries (with some amendments) two months later on May 7, 1993,<sup>19</sup> the initial rejection gives ground for speculation about the results of privatization and the apparent consent towards future economic reforms.

Moreover, Russia, with her huge territory and devastated infrastructure, became most sensitive to economic changes. On April 28, 1993, the Russian Parliament issued the decree "On the Implementation of the State Program of Privatization of State-Owned and Municipal Enterprises." This document deemed the results of privatization unsatisfactory because the introduction of vouchers "created conditions for profiteering and fraud," and, as a result, "state property is being handed over to private investors for a nominal price."<sup>20</sup>

At the end of April, Chelyabinsk Province Authorities in Russia raised a threatening hand against privatization, suspending the holding of check-based auctions. "There is no need for hurry" was one of the arguments used by the Chelyabinsk Deputies.<sup>21</sup> In April 1993, the privatization of municipal enterprises was suspended in the Mordovian capital, Novosibirsk, Ulyanovsk, and other large cities and regions in Russia. In Ulyanovsk, persistent attempts were being made to restore already privatized enterprises to state ownership. The head of the regional administration has issued an order suspending the privatization of a number of enterprises on grounds of their social significance. In another order, about 100 agricultural supply

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18. *Polish Parliament Rejects Plan for Privatization of Large Firms*, L.A. TIMES, Mar. 19, 1993, at A14.

19. See, e.g., *Polish Privatization Plan Awaits Walesa Signature*, N. SHORE FINAL ED., CHI. TRIB., May 8, 1993, at 11, Zone N; (Under the plan, 60% of the shares in 600 state enterprises will be turned over to about 20 funds, which will manage efforts to revive the struggling industries. Workers will get 15% of the remaining shares. The state treasury will keep 25 percent.).

20. Yelena Kotelnikova, *Parlament Obsuzhdal Programmu Privatizazii. Verhovnii Sovet ne dovolen privatizaziei* [Parliament discussed privatization program. Supreme Soviet unhappy with progress of privatization], KOMMERSANT, Moscow, Apr. 1993.

21. Aleksander Bekker, *Zamestitel Prim'er Ministra Anatoly Chubias Vojuet S Uralskimi Reakzionerami* [Deputy Prime Minister Anatoly Chubias Fights With the Ural Reactionaries], SEVODNYA, Apr. 20, 1993, at 3.

firms (more than half of which have applied for privatization and at least nine have actually floated shares) have been amalgamated into a state enterprise called Ulyanovskagrotekhsnab (Ulyanovsk Agricultural and Technical Supply). After a flood of complaints and protests, the regional administration decided to preempt all further complications over privatization by temporarily assigning a majority sharehold in certain enterprises to the regional property fund, or in other words, to the state.<sup>22</sup>

Privatization in the Soviet Republics was the political issue most clearly evidenced in political demonstrations on May 1st and May 9th, 1993, in Moscow, St. Petersburg and other major political and economic centers of Russia. The nation's biggest labor protest of the post-socialist era, involving more than 150,000 miners from at least 200 coal mines, spread on June 11, 1993. According to the *Los Angeles Times*, this strike was "the most serious challenge to the Ukraine's free market reform program, which mirrors that being attempted in Russia and other former Soviet republics."<sup>23</sup> The Russian Parliament Speaker Ruslan Khasbulatov announced that he did not see any direct link between support for reform, voted for by the Russian people in the April 25, 1993 referendum, and support for the development of privatization, which is held by the State Property Committee.<sup>24</sup> These words by the Head of Parliament can be understood to refer to definite alternatives to privatization.

Furthermore, on July 20, 1993, the Russian Supreme Soviet suspended the Russian president's decree "Of State Guarantees For the Right of the Citizens of Russia to Participate in Privatization," which guarantees that people in Russia have the right to a share of state property.<sup>25</sup> The Russian Parliament also adopted a resolution (which passed 173-4) that envisaged the transfer of the powers of the State Committee for the Management of State Property to the Ministries, effectively recreating the socialist planned economy.<sup>26</sup> This amounts to a carefully

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22. *Privatization at Standstill in Ulyanovsk Oblast*, Russia's Radio, Moscow [1000 gmt 30 Apr. 1993], May 7, 1993, available in LEXIS, WORLD Library, ALLWLD File.

23. Robert Seely, *Fueled by Fiscal Hardship, Ukraine Miners Strike Spreads*, L.A. TIMES, June 12, 1993, at A6.

24. KOTELNIKOVA, *supra* note 20.

25. Postanovlenie Verhovnogo Soveta Rossiiskoi Federazii o Napravlenii v Konstituzionnii Sud RF Hodataistva o Proverke Konstituzionnosti Ukaza Prezidenta RF ot 8 Maja 1993 No. 640 "O gosudarstvennih garantijah prava grazhdan Rossii na uchastie v privatizazii." See, e.g., 29 KOMMERSANT, July 19-25, 1993, at 26.

26. Postanovlenie Verhovnogo Soveta Rossiiskoi Federazii O Vnesenii Izmnenii i Dopolnenii V Postanovlenie Verhovnogo Soveta Rossiiskoi Federazii ot 27 dekabria 1991 goda No. 3020-1, 29 KOMMERSANT, July 19-25, 1993, at 26.

planned attempt to destroy privatization, a key element in economic reform.

These decisions do not exhaust the list of measures which have been proposed against privatization. Speaking at a press conference, Russian Deputy Premier Anatoliy Chubays said that the Parliament had drafted a package of documents aimed at blocking the privatization process in Russia, including resolutions repealing the President's decree and transferring the rights of the State Property Committee, headed by himself, to the Ministries. Chubays, according to the ITAR-TASS news agency, told the press conference that the Supreme Soviet was ready to approve two other resolutions which aimed to halt privatization by replacing privatization vouchers with personalized privatization accounts and suspending the 1992 state privatization program. Chubays accused the Parliament of "secret activities," since neither the government nor the State Property Committee had been notified about the agenda. According to Chubays, "the move was taken in the interests of the Parliament's leadership and the irreconcilable opposition backing them, and would sacrifice the interests of tens of millions of people."<sup>27</sup>

Thus, the first conclusion to be drawn from this article is that privatization is not a magic wand but a protracted, gradual, and complicated economic process which should not be urged nor precipitated by the government. Privatization is a constituent part of a whole process of economic transformation and decentralization of a command-administrative system, therefore it should not be isolated from accompanying economic and socio-political changes. Otherwise, it will create economic chaos and political instability, such as that now faced by Russia and the other former Soviet republics repeating Russian mistakes. At the same time, privatization is a well-known method of transforming political power in a society, and as such, it cannot be left on its own without the support of a democratic government. Finally, privatization reforms in post-socialist countries, if they are intended to be successfully undertaken by the government, should not fail to take into account the economic interests of different social groups and major political parties and civil movements. Such reforms should also include various political compromises and economic concessions. Civil law is called upon to play a major role in such a process.

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27. *Chubays warns Supreme Soviet not to block privatization programme.* (British Broadcasting Corp., World Service in English 1603 gmt, July 22, 1993).

#### IV. THE ECONOMIC AND LEGAL DEFINITION OF PRIVATIZATION IN LIGHT OF THE POST-SOCIALIST METAMORPHOSIS

The process of raising questions regarding the meaning of any term observing the process of the transformation of state ownership is a new one for Soviet jurisprudence and economic science.

To begin with, economists have a different approach towards privatization from that of lawyers. For instance, the American economist L. Gray Cowan defined privatization as "the transfer of function, activity, or organization from the public to the private sector."<sup>28</sup> As a result, privatization has been given an unreasonably broad definition which includes other economic-legal forms of decentralization, such as demonopolization and deintegration of united economic complexes. This position is held by other Western economists, such as Keith Hartley and David Parker, who state that "privatization embraces denationalization or selling-off state-owned assets, de-regulation (liberalization), competitive tendering, together with the introduction of private ownership and market arrangements in socialist states (for example, Eastern Europe and the USSR)."<sup>29</sup>

To a certain extent, this approach reflects the mixture of well-known ideas concerning the concept of economic reforms and the post-socialist decentralization of plan-based economies. However, it also hinders the understanding of the essence of privatization itself and its expediency for the transformation of plan-based economies.

In an attempt to find the most comprehensive definition of the economic phenomenon of privatization faced by socialist countries, some Western scholars have digressed from a substantive understanding of the nature of privatization. Instead, they concentrate their efforts and attention on secondary appearances of privatization. For example, Dieter Bös, in *Privatization: A Theoretical Treatment*, concludes that the word "privatization" has many different meanings. According to Bos, the term privatization includes the sale of public assets, as well as contracting out, de-bureaucratization, promotion of competition by market

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28. COWAN, *supra* note 2, at 6.

29. Keith Hartley and David Parker, *Privatization: A Conceptual Framework, in PRIVATIZATION AND ECONOMICAL EFFICIENCY. A COMPARATIVE ANALYSIS OF DEVELOPED AND DEVELOPING COUNTRIES* 11 (Attiat F. Ott & Keith Hartley eds., 1991).

processes, and "cold privatization."<sup>30</sup> Thiemeyer similarly enumerates fifteen definitions for "privatization."<sup>31</sup>

Certainly, the concept of a mixture of interacting yet independent definitions is, at the very least, inaccurate. All of these definitions are derived from the process of the democratization of a society and the decentralization of an economy. They are siblings but not identical twins. Some of these economic transformations are primary and fundamental, others are derivative and secondary.

Incidentally, a number of political discussions have been initiated in an attempt to distinguish these different definitions. The slogan of "reform without privatization" is quite well-known in Russian political struggles. By not taking this slogan into account, one would essentially be ignoring the problems of economic reforms in former socialist countries, thereby blinding oneself to particular features of the privatization process in the former Soviet Union that have distinguished the process from those undertaken in the past by other developing industrial countries.

#### A. DISTINGUISHING FEATURES OF POST-SOCIALIST PRIVATIZATION

First of all, a country's entire economy, with thousands of enterprises, must be involved in the process of privatization; a process that needs to be completed in a very short period of time. The share of the state sector in Czechoslovakia (1986) amounts to approximately 97%, in East Germany (1982) - 96.5%, in the U.S.S.R. (1985) - 96%, in Poland (1985) - 81.7%, and in Hungary (1984) - 65.2%.<sup>32</sup> In comparison, the largest completed privatization program so far is the post-Allende Chile, which succeeded in moving approximately 25% of the enterprises into the private sector. Even this high percentage is not accurately comparable since most of the Chilean firms have only recently been nationalized.<sup>33</sup> This is an example of de-nationalization rather than privatization. The well-known United Kingdom program of privatization shifted only about 4.5% of the GNP and employment out of the state sector.<sup>34</sup>

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30. DIETER BÖS, *PRIVATIZATION: A THEORETICAL TREATMENT 2* (Oxford ed. 1991).

31. T. Thiemeyer, *Privatization: On the Many Senses in which this Word is Used in an International Discussion on Economic Theory*, in *THE PRIVATIZATION OF PUBLIC ENTERPRISES: A EUROPEAN DEBATE 7-10* (T. Thiemeyer & G. Quaden eds., 1986).

32. STANLEY FISCHER, *supra* note 2, at 4.

33. *Id.*

34. *Id.*

Secondly, the privatization of state-owned property in Eastern-block countries is only one part of the entire process of decentralizing the economy and democratizing socio-economic and political conditions of developing businesses. Privatization in post-socialist countries takes place together with processes of demonopolization, deintegration, conversion of the military complex, denationalization, land reform, formation of new legal foundations for the functioning of state and public life, and social and ideological changes.

The proposals for privatization in post-socialist countries have to contend with some specific constraints present in the economies in which this process has to take place: namely, the existence of highly distorted product markets, where prices do not generally reflect relative scarcities; the embryonic competitive environment; the virtual absence of entrepreneurial culture; the lack of capital markets and broad-based investor publics; the absence of a developed banking system; the weak and undeveloped legal institutions such as mortgages, credit, and suretyship; the absence of a legal concept of bankruptcy; the shortage of free domestic capital available for investing; the lack of private sector savings to purchase the firms being privatized; and the nonconvertible national currency, which obstructs the participation of foreign capital and makes it virtually impossible to adequately estimate firms' market values.

There is no system of capital credit available for individuals to participate in privatization and raising enough money from savings to purchase companies can be very difficult. In fact, there is a critical shortage of cash in all of the former Soviet Republics. It is no surprise anymore when employees are not paid for two to three months. Some enterprises have started the practice of making payments with their own products. For instance, according to *Moscow News*, the Riga Stocking-Maker Factory "Aurora" reimbursed employees with stockings instead of a salary, the workers of the textile factory "Saula" received plaids, the workers of the flax-mill factory "Larelini" were paid in textiles, and the employees of "Stilo" received shoes and leather jackets.<sup>35</sup>

Apparently, we are witnessing the phenomena of a so-called barter economy. The system of "exchange of privileges" has distorted the valuable equivalent of money. The same amount of cash may hold different material value, depending mostly on who possesses this money. In essence, individuals with different access to privileges have different economic capacities with the

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35. Agris Peterson, *Zarplatu Vidali Kalgotkami* [The Salary Was Paid by Stockings], *MOSKOVSKIE NOVOSTI*, Jan. 10, 1993, at 3B.

same amount of cash. For instance, foreigners have to pay twenty-five times more for airline tickets on the Russian airline "Aeroflot" than Russian citizens do. Cash has two to three percent more value than money in savings accounts. Nobody is surprised anymore when some financial companies openly offer to exchange non-cash savings to cash money or back for a three percent commission. There is widespread barter of entitlements which cannot be directly transferred. For example, there is the well-known barter of apartments of dwelling houses. In fact, there is a whole branch in dwelling legislation devoted to the exchange of apartments.

Furthermore, most ex-Soviet republics, faced with triple-digit inflation and low treasury reserves, fled the "ruble zone" and introduced their own national currencies.<sup>36</sup> As a result, Russia, with a trade surplus in the ruble zone, was the big loser in that game. Money has also lost its valuable equivalent because of intensified inflation, the annual rate of which has reached about 2,500%, and because of recurring currency reforms.<sup>37</sup>

Third, economic reforms in the former Soviet Union bear a heavy social burden. As a matter of fact, the state was not considered to be the owner of the enterprises, but only an administrator, while the community as a whole is deemed the ultimate owner. One of the founders of the legal theory of socialist state property, academician A.B. Venedictov, stated as the basis of his doctrine that the united and sole subject of the right of state so-

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36. Specifically, Estonia introduced "kroon," Latvia -"lat," Lithuania -"lita," Ukraine -"karbovanetz," Kyrgyzstan -"som," Belarus -"zaichik," Moldova -"leu," Turkmenistan -"manat," Azerbaijan -"manat," Georgia -"lari." As of October 1993, the following countries were still in the ruble zone: Russia, Armenia, Tajikistan, Uzbekistan, Kazakhstan. In November 1993, Kazakhstan, Uzbekistan, and Armenia issued their own currencies. However, the ruble is easily convertible in almost all ex-Soviet republics.

37. For instance, on Saturday, July 24, 1993, Russia's Central Bank abruptly announced that all ruble bills issued before 1993 would not be honored as of the following Monday. Russian citizens had two weeks to exchange up to 35,000 of their old rubles (about \$35) for 1993 ruble bills. Anything over that amount could be deposited in a state savings bank — but the funds could not be withdrawn for six months, by which time inflation may have reduced their value to roughly zero. *See, e.g., Telegramma ZB Rossijskoj Federazii ob obmene kupur*, 29 KOMMERSANT, July 19-25, 1993, at 23. In effect this abrupt measure, which created turmoil in banks and marketplaces throughout most of the Soviet Republics, introduced national currencies in fact and aggravated the inflation inside Russia by flooding the ruble zone with rubles which were useless on their own territory, gives Russia its own exclusive currency. However, in spite of the fact that the reform concerned only the cash money which was in the hands of the population rather than money in savings and checking accounts of state and commercial banks, this unpredictable behavior on the part of the Central Bank shook public faith in the ruble and undermined government authority. It was the second money reform in Russia in the last three years and the third in the last thirty-two years. *See, e.g., Sonni Efron, Russia Won't Honor Pre-1993 Rubles Bills*. L.A. TIMES, July 25, 1993, at A1, A9.

cialist ownership is the whole public community, organized as the state.<sup>38</sup> Venedictov elaborated the legal theory of the "right of operative management" as a legal form of assignment of state assets to state enterprises and associations. This theory will be discussed in detail below. The legal form of "all-people property" was adopted by the constitutions and civil legislation of the former Soviet Union and other socialist countries. In the Constitution of the USSR, 1977, (Article 11), it was stated that all-people ownership of the means of production is the basic form of socialist (community) property. Moreover, some Soviet theoreticians drew a line of difference between the subject of the legal right of state ownership and the subject of the economic relationship of property.<sup>39</sup> It was held that the subject of the legal right of state ownership is the state, but the subject of the economic relationship of property is the public community.

However, since the community is considered the owner, there are just arguments in favor of free distribution on an equitable basis on the grounds that the property has already been paid for by the population. This issue apparently was not faced by other countries during their privatization programs in the past. It is this issue which added specific meaning to the process of privatization in Eastern Europe and the Soviet republics.

Finally, the process of privatization in Eastern Europe and particularly in the former Soviet Union is taking place in face of severe political opposition. In essence, this is a process of property transformation, which ties in to the evolution of the entire society and the transformation of the whole socio-political system. We cannot help but take this into account. These circumstances explain the concessions and the compromises which have been made by Russian President Boris Yeltzin, Polish President Walensa, and other leaders of Eastern European countries and former Soviet Republics, and they can be considered the rudiments of the centralized administrative system.

Thus, a privatization policy encounters different problems in different market economies, depending on the present level of economic development. The "planned economies" differ markedly from one another in current standards of living and material endowments, technical and educational attainment, level of privatization, socio-cultural impediments to economic growth, entrepreneurial culture, degree of industrial development, as well as history and culture. But what binds them together, and

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38. V.A. VENEDICTOV, GOSSUDARSTVENNAJA SOBSTVENNOST [STATE SOCIALIST PROPERTY] (Academija Nauk ed., 1948).

39. PRAVO SOBSTVENNOSTI V SSSR: PROBLEMI, DISCUSSII, PREDLOZHENIA, *supra* note 6, at 83.

makes the privatization policy a special problem, is the common experiences of almost half a century of command-administrative style economic planning. It is this shared characteristic which makes it worthwhile to study privatization in developing socialist countries as a special problem, which needs its own approach and treatment.

#### B. DEFINITION OF PRIVATIZATION: ECONOMIC AND LEGAL APPROACHES

More recently, the question of privatization has become an independent issue in Eastern-block countries. This key element of socio-economic transformation has acquired its own legal and economic understanding, in a manner which is quite different from the concept of social metamorphosis. Special privatization legislation was created which became a constituent part of civil legislation, even though the means of decentralization included a whole complex of problems involving constitutional law, administrative law, labor law, finance law, business law, land law, dwelling law, antitrust and antimonopolistic law, bankruptcy law, civil law, and criminal law. Indeed, this is a transformation of the entire society or, if you wish, a social revolution. The highlight of the reforms was privatization. Accordingly, it was the privatization theory which engendered most of the questions and arguments regarding the new economic changes. To address these issues we must first agree on the meaning of this term.

In light of the above-mentioned theory of the post-socialist economic reforms, privatization can be initially defined, using an economic point of view, as: a process of socio-economic transformation of the foundation of socialist centralized economies by means of transferring state assets and state enterprises to the private sector and thereby resulting in fundamental changes in ownership relationships in the spheres of production and distribution of material welfare. The implication of this seems to be that the purpose of privatization lies in the transfer of assets owned by "the people" to individuals in their capacity as citizens as a means of translating the notional and unenforceable collective "rights" into identifiably specific and transferrable claims on assets.

From a legal point of view, privatization is the single act of transferring (by the means of buying and selling) the legal title of state property, which was in the possession of state enterprises for restricted purposes of producing certain goods under owner-state control, to individual or associated owners. Therefore, these individual or associated owners are acquiring, through their own initiative and by contract of sale with the State, certain legal

*absolute*<sup>40</sup> rights of possession: to use and command said property in accordance with their free will, their own interests, and by their own power over the property.

It is interesting to note how legal and economic perspectives differ with respect to the same act; lawyers principally see a legal effect, which is brought about as a result of concerted wills, while economists probably see a movement of values. This means that, for the same act, lawyers generally analyze the basics, while economists evaluate the results. In their definition of privatization, lawyers must first express: a) sufficient equilibrium of parity and priorities of parties, including option, free will, and absence of dictates on the stage of negotiation of a contract (unfortunately "justice," and "fairness" are not legal terms in civil law), b) equality of opportunities for everybody to participate in such negotiations, c) mutual benefit of the parties, d) contract relations, e) the legal nature of transferred rights, specifically their absolute character, and f) guaranties of realization of transferred rights.

Applying the above theory to real life, it is my conclusion that pure privatization, as we understand it, is the sale of privatization objects by tender. The privatization of state and municipal enterprises by tender would mean acquisition by citizens and legal persons, recognized as purchases, of privatization objects, including shares (or blocks of shares), where purchasers would be required to make certain investments in the enterprise in conformity with an investment program drawn up by the vendor.<sup>41</sup> First of all, this would include open tenders, where the bidding would be conducted by an auctioneer in the presence of bidders at a public auction; and, second, closed tenders, where bids would be submitted by bidders in sealed form. Title to privatized objects would pass from vendor to buyer upon registration of the contract of sale. Accordingly, all other methods of the transformation of assets of state enterprises into the private sector should be deemed to be alternatives to privatization.

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40. There are two major characteristics — "absolute right" and "liability right" — which are used to describe two different legal institutions of civil law: estate law (including the right of ownership) and liability law (including contracts liabilities and torts). In contrast to liability law, bearers of which have subjective rights toward certain obliged persons, estate law is an absolute right, which provides to its bearer legal conditions where his rights correspond to obligations of others to refrain from any violation of said rights, which therefore surround the owner with stable legal boundaries.

41. Model Statute of Investment Tenders For Sale Of Privatization Objects, Russian Federation State Committee For Management Of State Proprieties Order No. 770-r. (Nov. 13, 1992), available in LEXIS, World Library, ALLAW File.

## V. ALTERNATIVES TO PRIVATIZATION: LEGAL ISSUES

In giving consideration to the process of privatization, we are able to outline some of the possible alternatives which are raised as political and economic issues in post-socialist countries. Obviously, as an alternative to the process of privatization there is the absence of combined privatization and nationalization systems. What social benefits and economic advantages does private ownership assume? Indeed, the right of private ownership is not a question of political economic only; it is a question of political strategy and economic tactics. Unfortunately, it is not always possible to find a simple answer for the question of political economy conformity under variable circumstances. Apparently, the answer cannot be an absolute. Otherwise, how could the Soviet Union arrange its existence and industrialization when the country was basically agricultural? How could its industries have survived the two destructive wars on its territory and the great human sacrifices caused by Stalin's repressions? How could the Soviet Union successfully compete in economic, scientific and military areas with the whole world for 74 years? What about the Chinese phenomena? Was it only the "Soviet influence" that established and kept together a whole camp of socialist countries in Eastern Europe? What was the enticing reason for the nationalization in France in the first half of 1980's? What is the positive economic effect of state ownership? This is a topic for separate research by political scientists. However, we can conclude that the model of economic socialization exercised in the Soviet Union and Eastern Europe led to unfortunate results. Was this a fault of state ownership or the erroneous methods and forms of its realization?

For the purpose of this article I shall concentrate my analysis on the legal issues that have arisen from the question of whether there are alternatives to the privatization process.

### A. THE VARIETY OF LEGAL FORMS OF OWNERSHIP

Turning to the subject of ownership relations, it is clear that such ownership relations must be multi-structural and multiform since a commodity-money exchange cannot exist without them. A commodity-market economy is a self-regulated business mechanism and requires a diversity in the form and type of property. This diversity of forms engenders diversity of economic interests.

The Law of the Russian Federation "On Ownership in Russia" (adopted on December 24, 1990) states that the "establishment by the State of any kinds of restrictions or preferences in realizing the right of ownership, depending on the possession of

property in private, state, municipal ownership and ownership of public unions (organizations), are not allowed.”<sup>42</sup> The preamble to the “Enterprises and Entrepreneurial Activity Act” (as amended on June 24, 1992),<sup>43</sup> a major Russian corporate and business law Act, reads as follows: “This Act defines general legal, economic and social foundations for the establishment of enterprises in conditions of variety of forms of ownership. . . .” Furthermore,

The provisions of the present Act apply in the entire territory of the Russian Federation in respect to all subjects of entrepreneurial activity and enterprises, irrespective of the form of ownership and sphere of activity, including juridical persons and citizens of other Union Republics and foreign states. . . .

For the first time in the legislative history of Russia, the guarantees of the Russia Federation were laid out with specificity. Article 20 states, as one of the guarantees of entrepreneurial activity, guaranteed in the Russia Federation are: “[E]qual rights of access for all entrepreneurial activity, subject to the material, financial, labor, information and natural resources, equal conditions for activity of the enterprises, regardless of their kind of ownership and organizational-legal form.”

Thus, the existence of past dogma about the fundamental principle of state ownership and the necessity of a high level socialization of property becomes just a communist theory, no longer a legal practice in Russia or other post-socialist countries. Recognition by the Russian Legislation of the various forms of ownership and the equal rights of subjects of these ownerships also means that there are legal alternatives to private property in Russia and the other post-socialist countries.

#### B. THE LEGAL TERM “PRIVATE OWNERSHIP” AND ITS RECOGNITION BY LAW

Before the Russian Federation passed the law “On Ownership in Russia” in 1990, the legal terms “private ownership” and “private property” were unknown to the Russian and Soviet Legislation. Traditionally, the Soviet Legislature used the term “personal property.” The difference is substantial. Without going into the details of present regulation, the legal watershed between these two terms lies in the realm of practical use and exploitation of the objects governed by the right of ownership. From the economic point of view the major distinguishing factor

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42. Law of the Russian Federation, “On Ownership in Russia” (adopted on December 24, 1990), article 2(2). VSE O PRIVATIZAZII (Yekaterinburg, Uizi ed. 1991).

43. Law of the Russian Federation, the “Enterprises and Entrepreneurial Activity Act” (as amended on June 24, 1992) available in LEXIS, World Library, ALLAW file.

is in the nature of these material objects. According to the Foundations of Civil Legislation of the Union of Soviet Socialist Republics, the Civil Code Of RSFSR (1961), and the civil codes of other Soviet republics, citizens could have articles for personal consumption as their "*personal property*."<sup>44</sup> Generally speaking, these objects included articles of domestic utility and everyday use. Until recently it was generally illegal in socialist countries to have in one's personal possession and ownership any means of production, such as land, factories, office buildings, industrial facilities, means of commercial transportation, newspapers, retail stores, and all forms of enterprise or company. In other words, anything that could be used for the production of any kind of good or service was considered "private property" and possession of such property was a violation of civil law. The State could confiscate each and every one of these objects, as well as all gross profits derived from these objects. On some occasions the violator could be subjected to an administrative penalty. There were some exceptions, of course, at different periods of time and in different countries, but the general picture remains unchanged<sup>45</sup>.

The first changes toward the liberalizing economic life and legislation were made in the beginning of the 1980's. New economic trends were bound up with developing "individual labor activity" and "personal subsidiary small-holdings." The term "*individual property*" was introduced. The common trait of these individual industrial and agricultural activities was the recognition of these activities as subsidiary sources of generating personal property; a kind of moonlighting. But from the moment that the citizens realized their rights to industrial and agricultural

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44. Grazhdanskii Kodeks RSFSR [GK RSFSR] art. 105 (Russia).

45. During the so-called New Economic Policy (NEP) in Russia in 1922-1928, the state's policy was to encourage the development of widespread private business while all the "commanding heights" of heavy industry, transportation and communication were still state's property and under the government's control. The purpose of NEP was more political than economic. The Head of the Russian Sovnarcum, Vladimir Lenin, initiated this new reversal of economic politics of the young revolutionary state to win the support of the middle class peasants, who were the majority in agricultural Russia, by establishing the commodity-money interchange between city and province. As is well-known, before 1922 there was a period of "war communism" in Russia, when special military provision platoons expropriated goods of the peasants without any significant economic compensation. Indeed, these measures were not popular among the population which therefore demanded some economic changes, which were expressed in the New Economic Policy. However, the New Economic Policy was terminated by Stalin in 1928 as "inappropriate to the principles of socialist development."

Moreover, some Eastern European countries, as for example, Poland, historically permitted the existence of private property including ownership of land. But that was more the exception than the rule. Certainly, private property everywhere, daily and on a large scale, was subjected to severe restrictions. M.K. OZIEWANOWSKI, A HISTORY OF SOVIET RUSSIA 127, 179 (4th ed. 1993).

activity as their exclusive means of subsistence, their activity was considered the source of another kind of property—"private property." There prevailed in Russian civil legislation and political economy a theory that the major difference between "individual property" and "private property" was that using an individual's property was not considered the primary form of a citizen's participation in social production, and as such, the net profit received from the use of individual property cannot be considered the only source of subsistence.<sup>46</sup> The same provisions have been reflected in the Constitution of the Soviet Union of 1977, the Fundamentals of Civil Legislation of the USSR, and many other civil legislation.<sup>47</sup> However, there was a consistent differentiation in the application of the above-discussed theoretical bases of private property in the Civil Codes of the various socialist countries.<sup>48</sup> Thus, the legislation of socialist countries recognized and distinguished three terms: personal property, individual property, and private property.

However, one of the major characteristics of the laws regulating ownership of private property during the history of socialist ideological development was the concern with wage labor exploitation. Some socialist countries even permitted, with certain restrictions, the hiring laborers. For instance, legislation in the German Democratic Republic and Hungary allowed the enlistment of six to ten hired laborers, while Poland and China permitted the hiring of substantially more workers. As for the Soviet Republics, they banned any exploitation of wage labor as "dangerous in its social-political meanings."<sup>49</sup> The attempts by some Hungarian lawyers and economists to substitute these forms of personal, individual and private property with the united term "property of citizens" did not find support in legislation until the "new economic thinking" of the period of Perestroika.<sup>50</sup> This liberalized goal was reached by the Legislative

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46. See, e.g., PRAVO SOBSTVENNOSTI V SSSR: PROBLEMI, DISCUSSII, PREDLOZHENIA, *supra* note 6, at 162 (the round table discussion of lawyers, economists, scholars on the current problems of the right of ownership in Soviet Union).

47. See, e.g., Konstitutsiia SSSR [Constitution of the Soviet Union] [KONST. SSSR (1987)] art. 13 (U.S.S.R.); Osnovi Grazhdanskogo Zakonodatelstva SSSR [The Fundamentals of Civil Legislation of the USSR], art. 25; Zakon SSSR Ob Individualnoi Trudovoi De'etelnosti [The Act of USSR "On Individual Labor Activity"]; Grazhdanskii Kodeks RSFSR [Civil Code Of RSFSR] [GK RSFSR] art. 105, 115; see also civil codes of other Soviet Republics.

48. See, e.g., Civil Code of Poland, arts. 130, 132; Polgarl Törvénykönyv [PTK] [Civil Code of Hungary] §§ 92-3; Civil Code of Czechoslovakia §§ 125, 126, 489; The Act on Ownership of Bulgaria, arts. 28, 29.

49. See, e.g., PRAVO SOBSTVENNOSTI V SSSR: PROBLEMI, DISCUSSII, PREDLOZHENIA, *supra* note 6, at 163.

50. See, e.g., L. Vekas, *Über die grundsätzliche Frage der staatsbürgerlichen Eigentums*, 26 (F.1-2) ACTA JURIDICA, 1984, at 130-38.

Act of the USSR "On Ownership in The USSR," adopted by Gorbachev's Soviet Parliament on March 6, 1990. Section 2 of this Act is dedicated to the rights of private ownership. However, because of political considerations, the terms "private ownership" and "private property" were not applied. The Act introduced to Soviet jurisprudence the new legal term "ownership of citizens," which included ownership of the means of production, "production and received profit, as well as other chattels destined for consumers and productive purposes." Furthermore, the Act "On Ownership in the USSR" can be construed as granting Soviet citizens the legal right to use hired laborers and to be hired laborers. Certainly, this was the next step toward liberalizing Soviet legislation through guarantees of the economic rights of citizens and the establishment of the basic principles of a law-binding state. Finally, on the long thorny path to developing a legal theory of "private ownership" in Soviet civil legislation, the terms "private ownership" and "private property" were generally recognized by the Law of the Russian Federation "On Property in the RSFSR," announced on December 24, 1990. This was the beginning of severe economic reforms in Russia.

## VI. THE LEGAL CHARACTER OF REAL ESTATE RIGHTS OF STATE ENTERPRISES ON ASSETS ASSIGNED TO THEM

The technical legal problems of classifying the legal right of state enterprises to state assets apportioned to them have been discussed in literature for many years.<sup>51</sup> Since this article intends to inquire into possible alternatives to privatization, I cannot ignore this "major question of civil law."

### A. THE RIGHT OF "OPERATIVE MANAGEMENT"

The legal term "*the right of operative management*" originated among Soviet scholars of civil law and was adopted by the Soviet Legislature. The right of operative management has been considered an alternative to the legal right of ownership. During the Soviet era "the right of operative management" was the "principal form of realization of state ownership," or, in other words, the principal means by which state ownership was exercised.

The "right of operative management" is unique among ownership relationships in both common law and civil law legal sys-

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51. See, e.g., SOVETSKOE I INOSTRANNOE GRAGDANSKOE PRAVO: PROBLEMI VZAIMODEISTVIJA I RAZVITIA [SOVIET AND FOREIGN CIVIL LAW: PROBLEMS OF RECIPROCITY AND DEVELOPMENT], (B. Mozolin ed., Nauka 1989), at 212-13 (a survey of foreign literature on this topic).

tems. With certain reservations, "the right of operative management" is most closely related to the theory of a "splintered" or "compound-structural" model of ownership (known in the Anglo-Saxon legal system as "fiduciary ownership" or "trust"), despite the fact that the latter has very little in common with the civil law institutions of estate law and ownership in Russia. These theories belong to different legal systems: the continental system, derived from Roman civil law, and the Anglo-Saxon common law system. As a matter of fact, fiduciary ownership or trusts have no direct analogies in Soviet civil law legislation. As is well known, the "fiduciary" model of ownership is trilateral and historically became the traditional ground for dividing the Anglo-Saxon system of law into two branches: equity (ownership, in this case, was designated as "equitable ownership") and law (accordingly, for the designation of ownership it used the term "legal ownership").

Russian literature has clearly expressed the view that using the theoretical model of fiduciary ownership as per the continental legal system would inevitably cause "incalculable impediments, both of a legislative and practical nature" and demand "repudiation of a great many proven legal constructions, which have existed from the times of Roman Law."<sup>52</sup> However, despite its unique place in the nature of civil law, the so-called "right of operative management" has become recognized as universal and was used as the legal characterization of competent enterprises that operated on self-supporting bases.

The phenomenon of the "right of operative management" also found its normative incarnation in Article 5(3) of the recent Law Of Russian Federation On Ownership In RSFSR, which stated that

assets, assigned<sup>53</sup> by the owner to State institutions or other establishments, which are financed by the owner, are in

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52. D.A. Medvedev, *K Voprosy o Prirode Prava Gosudarstvennogo Predpriyatiya na Imushchestvo* [Questions Regarding the Nature of the Right of State Enterprises to Their Assets], in *PRAVO SOBSTVENNOSTI V USLOVIYACH SOVERSHESTVOVANIA SOCIALIZMA* (IGPAN ed., 1989), at 50-51.

53. It is interesting to note that the English language, as far as I know, does not have a word which literally expresses the meaning of the Russian term "zakrepliat," which generally is used to describe the rights of enterprises to assets which were "given to them by the government to exercise their right of operative management." The term "zakrepliat" applies to object-substantial, registration-statistic and technical-legal isolation of assets, which are in the possession of the enterprise. The word "assigned" is not quite right in the context of understanding the nature of the above-said right since it is not a factual transferring of tangible nor an assignment of the legal rights to the assets. The legal rights of state enterprises to their assets were not transferred but rather assumed. Furthermore, these rights of operative management, which will be discussed later, are not completely "assigned" because the government can always restrict, take away, cancel or otherwise affect any given right. The right

the operative management of this institution, which exercises within the limits established by Law and according to the *purposes of its activity, the tasks of the owner and the predestination of the assets*, the rights of possession, use and command of these assets.<sup>54</sup>

It is very important to mention that this recent determination has revised the former meaning of the term "the right of operative management." As we can see, the legislation deals only with institutions that are financed or subsidized by the owner (such institutions generally include government agencies, public organizations, state universities, colleges and high schools, scientific institutes and laboratories, libraries and other non-commercial organizations), but not with industrial enterprises. The right of operative management had originally been applied to all state enterprises. Now enterprises are covered by the new academic-legal term "the right of full proprietary authority," which will be discussed further. Secondly, the Article refers to all owners, not exclusively to the government, as had been the case in former Soviet and Russian legislation. Thus, we witness an attempt to apply old socialist legal forms, derived from a necessity to substantiate the uniqueness of the economic and legal title of state enterprises to their assets, to new economic situations.

Simple analysis shows that "the right of operative management" can undoubtedly be considered as an alternative to the right of ownership. It is very important to realize that assets which were in possession of state enterprises were given to them, and the enterprises' rights of possession of these assets did not depend on their own choice. That means that state enterprises had no voice regarding whether or not to possess assets given them, and as such, the exercise of these rights also does not depend on the interests of the enterprises.

According to generally accepted civil theory, the legal term "the right of ownership" includes a well-known triad of ownership powers: the rights of *possession, use, and command* of one's belongings. The economic and legal possibility for an owner to exercise the above-said rights by acting in his *own interest* is no less important an absolute right of ownership. The owner's "own interest" became a key element in distinguishing between the absolute right of ownership and the "right of operative management." The Law of the Russian Federation On Ownership in the

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of operative management is not an absolute right by its legal nature. In a sense, we can translate the referenced word and compare its meaning with the English term "entrust." But for the reasons stated above, I am not inclined to mix two different legal terms and systems.

54. Zakon RSFSR o Sobstvennosti v RSFSR [The Law Of Russian Federation On Ownership In RSFSR], art. 5(3), Vse o privatizazii (Ekaterinburg UIZI ed., 1991), at 57-68.

RSFSR (Article 2 (2)) stated that "an owner in his own discretion possesses, uses and commands property belonging to him." In contrast, the holder of the right of operative management exercises its right according to the purposes of its activity, the tasks given by the owner, and the purpose of the assets use. To put this in practical language, state enterprises could not change their industrial specialization and the specific character of their production without consulting a government ministry, which was virtually impossible; producers were banned from using their land, real estate, equipment, machines, and other chattels for purposes other than those stated in their charters and local regulations; state enterprises had to follow government tasks and instructions regarding the use and command of their assets; state enterprises could not rent or lease their assets without permission from the above-stated ministry; and apparently state enterprises did not have an absolute right to dispose of assets by selling, giving away, or eliminating them. This was quite an established bureaucratic system for writing off obsolete equipment: the government could always terminate state enterprises' rights to possess assets by liquidating the enterprises through the abolition, separation, or amalgamation of several different enterprises. Obviously all of these restrictions are far from our understanding of the owner's "own interest."

A.V. Venedictov, the founder of the theory of "the right of operative management," insisted on asserting that "the socialist state organ, as special subject of the legal right, is a holder of "its own special interest," and that "this special interest first and foremost consists in the fulfillment and overfulfillment of a plan, with which it was entrusted by the government."<sup>55</sup> This dictum is in full conformity not only with what was recognized at that time as the conception of a planned economy and legal establishment, but also with the practice of management.

The concept of Venedictov's operative management strictly, logically, and most adequately expressed a political-economic paradigm of the political requirements and existing organization of state ownership. His concept was based on the axiom of a complete coincidence of interests between society, state, government and labor collective enterprises. The main instrument of ensuring such a coincidence was a comprehensive system of directive planning that was supplemented with mechanisms of compulsion and incentives. Consistent with the above-stated structure of management, and within the bounds of a corresponding economic paradigm, an enterprise first and foremost

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55. V.A. VENEDICTOV, GOSSUDARSTVENNAJA SOBSTVENNOST 350 [STATE SOCIALIST PROPERTY] (Academija Nauk ed., 1948).

was considered an object of management and an executor of numerous plans, instructions, administrative targets, and work quotas.

A critical analysis of publications regarding the problems of socialist property and the right of operative management was put forth in a detailed article by the famous Russian civil law professor, Yuri K. Tolstoy.<sup>56</sup> He not only affirmatively denies the proposals to decrease the use of operative management, he also attempts to modify this term in light of new interpretations (other than Venedictov's theory) such as the modern point of view recognizing this theory as a civil law phenomenon. According to Tolstoy, the theory of operative management is very "successful" and it "adequately reflects the existing conditions of management."<sup>57</sup> While I can probably agree with his conclusion, this article was not intended to address the question of whether the theory of operative management reflected existing reality, but rather if the said reality has to be changed. As a matter of fact, the theory of operative management strictly corresponded to the hierarchical mechanism of a planned economy and administrative-command methods of management. In this connection I can agree that the use of the right of operative management was quite successful.

However, the creation of a new economic mechanism of management and the transformation of the national economy to the market demand system takes away one of the major elements preserving the existing socialist system — the right of operative management, the main tool of the hierarchical organization of state ownership. The socialist concept of a complete coincidence of the interests of government, labor collectives, and enterprises loses its meaning under these new market economy conditions. The owners of a private firm are interested in profit. As such, the manager of the private firm knows the goal of the owner and there should be no uncertainty about the weight that he should give to various other objectives.

Indeed, the government has several other objectives which may not coincide with the profit maximization goals of the enterprises. Such a conflict would arise, for instance, with objectives such as price stability, preservation of historically established economic ties, artificial support of the national currency, maintenance of high employment, social security, and regional development. All the above-mentioned objectives influence the

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56. Yuri K. Tolstoy, *Socialisticheskaya sobstvennost i operativnoe upravlenie* [Socialist Property and Operative Management], in *PROBLEMI GRAZHDANSKOGO PRAVA* 68 (Leningradskii Gossudarstvennii Universitet ed., 1987).

57. *Id.* at 69.

maximization of votes. Therefore, it can be assumed that the higher the consumer welfare, the lower the prices—a situation analogous to a policy of capturing votes.<sup>58</sup>

Second, even if enterprises enjoy full autonomy and markets are liberalized, how well could the state supervise the behavior of management? It is known that the most objective method to judge management performance is by the valuation of enterprises on a stock market. The private capital market imposes pressure on the firm to be efficient (for example, via threats of take-over and bankruptcy). However, the operation of an efficient stock market requires that the ownership of enterprises be transferable. In other words, the enterprises themselves have to be privately owned. Generally, a worker's claim on the firm's profits or assets is not transferable—that is, it is contingent on being an employee. In the case where ownership is not transferable (non-traded stocks), capital market pressure is much weaker than would be if the stocks were traded. As for state enterprises, their minimal risk of bankruptcy would distort financial markets and savings allocation. This is why socialist legislation is not familiar with the term bankruptcy.

Third, due in part to an integral economic complex based on common property as the means of production, it is unlikely that sufficient competition could take place in the industries operated by public enterprises. The proposal that “in order to provide extensive competition and to prevent the springing up of monopolies, it should be established that important work quotas have to be set, not just to one but parallel to several organizations so as to have a possibility of comparing the results of fulfilling the task” is more than nonsense.<sup>59</sup> It is obvious that even if several producers combined, they still could not fully satisfy the achievement of high-quality products if these requirements are determined by the government as an administrative order. The government is not omnipotent and cannot know every need of society. Only a market, with its hundreds of thousands of enterprises, could appraise the concrete productive results. The needs of customers, not a “government quota,” must determine productive development; and everyone must have access to the market, not just a few selected organizations. Also, it is obvious that the government's tasks and the enterprises' goals are different with regard to profits and as such, it would be possible for certain enterprises to obtain a privileged position by infringing upon

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58. See, e.g., B. Caillaud et al., *Government Intervention in Production and Incentives Theory: A Review of Recent Contributions*, 19 RAND J. ECON. 1-26 (1988).

59. Sobranie Postanovlenii Pravitel'stva SSSR [SP SSSR], Issue No. 18, at 122 (1968).

others. This system cannot help but affect small business negatively and support, rather than liquidate, the monopolies.

Furthermore, under the condition of socialist public property, the term "competition" has been understood as comparing last year's results for the enterprise with the current year's results for the same enterprise. Exceeding last year's results has been taken as the basis for comparing it against other enterprises. The labor collective of the winner received some bonuses and the director might receive an award. It is quite surprising that this approach is still under consideration by Russian legal literature.<sup>60</sup>

Fourth, if shares were not transferable, worker mobility would be seriously impaired, since they would lose their preexisting right to receive shares by any change in jobs. This would affect the whole society.

Based on all of the above, I conclude that the right of operative management is not a reasonable alternative to ownership. Accordingly, it is quite unjustified for the Russian legislation to place the legal norms of the right of operative management in an ownership section that is dedicated to the rights of estate. The nature of this right is more obligatory than the proprietary essence of estate rights.<sup>61</sup>

## B. THE RIGHT OF "FULL PROPRIETARY AUTHORITY"

The legal "*right of full proprietary authority*" is quite new for Russian legislation. For the first time this term was technically legalized by the Soviet legislature in The Law On Ownership in the U.S.S.R. (March, 1990), Article 24. This right is currently presented in The Law Of the Russian Federation On Ownership In RSFSR (December 24, 1990) and in The Law Of the Russian Federation On Enterprises and Entrepreneurial Activity (December 25, 1990). According to Article 24(1) of The Russian Law On Ownership In RSFSR "assets considered to be state and municipal property, and which were assigned to state and municipal enterprises, belong to the enterprise by right of full proprietary authority." The Law On Enterprises and Entrepreneurial Activity (Article 6(2)) also states that "the assets can be given to a working collective of an enterprise for proprietary authority."

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60. See, e.g., V. Mamutov, *Pravovoe obespechenie uslovii dlia razvitiia sorevnovaniia v ekonomike* [The Legal Security of Conditions for Developing Competition in the Economy], 6 CHOZIAJSTVO I PRAVO 64 (1992).

61. See, e.g., DINUS N. SAFIULLIN, *TEORIYA I PRACTICA PRAVOVOGO REGULIROVANIA HOZIAJSTVENNIH SVIAZEI V SSSR* [THEORY AND PRACTICE OF LEGAL REGULATION OF ECONOMICAL CONNECTIONS IN USSR] § 2 (Izdatelstvo Uralskogo Uneversiteta ed., 1990).

There are some appropriate questions which could arise in this context. What does "full proprietary authority" mean? What is the nature of the right of full proprietary authority? What is the substance of the right? What authorities does it include? What is the difference between the right of ownership and the right of full proprietary authority? Can this right be considered as an alternative to private property?

The answers to these questions are intriguing because few attorneys practicing law in Russia and the former Soviet Union can give reasonable explanations of these problems. Unfortunately, the plain language of the law regarding "proprietary authority" is ambiguous even though the term is very important for both an understanding of the current authority of state enterprises as well as for the practical application of legal rules in everyday business in Russia and in the former Soviet Republics.

The literal translation of the term "proprietary authority"<sup>62</sup> means "authority," "power," "being in charge," "management," "superintendence" of the "master" or "proprietor." Adding the word "full" to the phrase "proprietary authority" at first does not have any legal sense, but only makes it more complicated. Logically, if there is "full authority," it has to mean more than simply "authority." This rule does not work here. There is only one "proprietary authority" in Russian legislation — "full proprietary authority." The word "full" is only a semantic load—to emphasize the completeness of the legal authority of the holder of this right. This authority is the following: not partial as the right of operative management; an expression of the whole triad of ownership powers; sufficient for efficient management of self-running state enterprises; ample to exercise economic freedom; complete legal and economic power. However, the key word of the phrase is "*master*" or "*proprietor*."

Beginning in the 1980's, legislation in socialist countries introduced the term "master." It was even recognized in the whole legal construction—*state-owner, enterprise-master*—that has been elaborated in theoretical literature.<sup>63</sup> Then, for the first time, the

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62. The phrase "*proprietary authority*" represents the author's translation of the Russian legal term "*hoziajstvennoe vedenie*." Apparently, different economic systems are reflected in the different linguistic and business vocabulary of the two languages. There are no equivalents to some common Russian economic phenomena in the American language, and on the other hand it is still almost impossible to find in Russian an appropriate translation for widely-used American terms, such as "mortgage," "trust," "land security," "endorsement," and "bill." For these terms Russian business people and lawyers use either old pre-Revolutionary language, or Western-American words. The change of the economic system inevitably caused a change of vocabulary.

63. See, e.g., CH. GOLEMINOV, *PRAVOVIE ASPECTI NOVOGO ECONOMICHESKOGO MECHANIZMA v NRB*, at 81-83 (Moskva ed., 1984).

term was used in legislation in Bulgaria in 1984.<sup>64</sup> This legal construction also found its reflection in legislation in Poland, Romania, Hungary, the German Democratic Republic, China, and the former Soviet Union.<sup>65</sup> For instance, according to the Soviet Law On State Enterprise (Association) a work collective is "a competent master of the enterprise" (Article 2(3)) and a collective of an enterprise "uses public property as a master" (Article 1(2)). In Bulgaria, on April 29, 1987, the Decree of State Soviet (the highest organ of legislature power in Bulgaria) "On Granting Socialist Property To Work Collectives For Management" was promulgated. Consistent with the statute, the state, "as an owner upon authorization of the people," grants "guaranteed rights of the master" of common socialist property to "its real masters:" self-managed work collectives.<sup>66</sup> The People's Republic of China's Act On Industrial Enterprise of Public Ownership was approved and went into force on August 1, 1988. This act applied the theoretical principle of separating the right of ownership and the right of operative management by transferring the rights of possession, use, and command of the property from the state to the enterprises.

However, the legislation intentionally chose not to provide a clear and concise answer to the question of what is meant by the terms "to use property as a master," "guaranteed rights of master," "real masters," and "master management." Moreover, the language of this new "management legislation" was not originally phrased in true legal terms. This is not surprising, because all of these innovations were partially prepared for political considerations and proclaimed by congresses of communist parties in the socialist countries as a rule. Notwithstanding its political orientation and unconcealed political content, the term "master" came to be legally recognized in all socialist countries and, more importantly, it caused the development of a new branch of legislation: the so-called "master legislation."

This new legislation is distinguished from traditional civil legislation by its subject and method of regulation. Civil law regulation focuses on equality between the rights of parties and

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64. Derzhaven Vestnik, 1984, at 12.

65. See, e.g., 24 Dziennik Ustaw PLR, 122 (1981) (Poland); 54 Buletinul oficial al RSR, (1983) (Romania); The Law Act IV, On State Enterprise of Hungary Peoples Republic [with amendments made by Decree of Presidium of Hungary Peoples Republic No. 22, 1984] § 22 (1977) (Hungary); Zakon SSSR o gosudarstvennom predpriyatii (objedinenii) v SSSR [The Law Act On State Enterprize (Association) in USSR], Articles 1(2), 2(3) (1990); see also CHOZIAJSTVENOE ZAKONODATELSTVO STRAN CHLENOV SEV (Progress ed., Moskva 1989); E.A. Suchanov, *Opit zarubeznich socialisticheskikh stran v oblasti soverchenstvovaniia otnochenii sobstvennosti*, in PRAVO SOBSTVENNOSTI V SSSR, *supra* note 6, at 204-13.

66. Derzhaven Vestnik, Issue No. 34 (1987).

those of the "optional conduct"<sup>67</sup> in realizing the parties' subjective rights. It cannot adequately reflect the practical tasks involved in developing a legal base for business relations between government and state enterprises or between individual business entities. The subject of "management legislation" is social relationships within the sphere of entity relationship organization and the possible partial subordination between them to the administration and management. Civil law, on the other hand, regulates commodity-money relations and disregards the nature of the participants or the character of the business relationship between them. Civil law is interested in economic equality, mutual benefit and civil justice. The "master legislation" seeks economic expediency in the interests of society and involves the legal norms of the different branches of legislation including financial, banking, labor, and civil law.

Indeed, the more sophisticated character of state property relations in a new economic situation, and the political goal of maintaining the socialist content of such relations, demand a more clearly organized legal expression and consolidation of a variety of interrelations between the owners and producers of material values. The socialist society was faced with the necessity "to surmount the alienation of working producers from the means of production." The constitutional term "property of the people" does not have any real practical consequence. The distance between the terms "my" and "our" is considerable. The category "our," regarding public property, is quite abstract and without concrete legal content. Hence, it appears to follow that people think of such property as "bureaucratic," "formal," and "no one's belongings."<sup>68</sup> The economic reforms bore a new theoretical approach by lawyers and economists to the problem of the state enterprises' legal rights to their assigned state assets. The simple universal triad of "possession, use and command," recognized by civil law for centuries, cannot encompass the diversity among estate law institutions use in allotting public property to the different state organs and associations. One such institution given to enterprises by the government is the "right of full proprietary authority," which influenced the assignment to state enterprises of the rights of a "master" or a "proprietor" over state property. In socialist countries this institution became known by different names: "the right of management" in Bulgaria, "the right of possession of fund" in the Germany Democratic

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67. See, e.g., VENIAMIN F. YAKOVLEV, *GRAZDANSKOPRAVOVOI METOD REGULIROVANIA OBSHESTVENNICH OTNOSHENII* [THE METHOD OF CIVIL LAW REGULATION OF SOCIAL RELATIONS] (URGU ed., Sverdlovsk 1972).

68. L.I. Abalkin, *Polnii choziajstvennii raschet* [The Self-Supporting Running], PRAVDA, December 12, 1986.

Republic, and "the right of proprietary entrepreneur of state" in Hungary.<sup>69</sup>

The right of a master, which was given to working collectives of state enterprises, has its own economic and legal content. From an *economic* position, this right includes the following aspects of the state enterprises' working collectives: a) self-supporting operation, b) self-financing, and c) self-repayment. The labor collectives of enterprises were given the right to independently decide questions over how to deal with their gross manufacturing profits (with some restrictions as to deductions for expenses of production, credits and tax payments, assignment of social and medical security funds, fixed payments to the government as its share of the profit, and the expenses of labor). The collectives became more independent in allotting net profit and organizing different financial funds. The annual state plans became less detailed and some even provided incentives by establishing general annual quotas or fixed indices of government payments. The activity of administration and management became less regulated and the knowledge of government deduction indices stimulated further industrial development which resulted in larger profits.

Furthermore, legislation in some countries instituted special "contracts-obligations" between the State, as the general administrator of the people's property, and the labor collectives of state enterprises.<sup>70</sup> Planning relations slowly moved toward contractual business ties. Indeed, self-operating enterprises were still being provided with requirements for raw materials and energy by the government and, as a result, contractual relations between the "master" and "owner" can be seen as a definite step towards the democratization of economies. Additionally, in Hungary, Bulgaria, Poland, Czechoslovakia, and the Soviet Republics, working collectives were given the right to elect the executives and directors of their enterprises.

Thus, enterprises (directors, administration, and working collectives) finally became responsible for the results of their "proprietary activity" as well as the success of their management. However, these reforms were only a re-decoration of the old socio-economic relations that were based on public property. The political slogan "property of the whole people" remains primarily a socialist principle and it still does not contain any signifi-

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69. E.A. SUHANOV, GRAZHDANSKOE I CHOZIAJSTVENNOE PRAVO EVROPEISKICH GOSUDARSTV—CHLENOV SEV 98-104 [THE CIVIL LAW AND THE COMMERCIAL LAW OF EUROPEAN COUNTRIES—MEMBERS OF COMECON] (Juridicheskaja Literatura ed., Moskva 1984).

70. See, e.g., The Law Act of Romania No. 3, July 9, 1983; 54 Buletinul oficial al RSR (1983); THE DECREE OF STATE SOVIET OF BULGARIA, April 29, 1987; 34 Derzaven Vestnik, Issue No. 34, (1987).

cant meaning. The term "our," with regard to public property, became less widely used and it too remains ambiguous and vague. The individual workers of state enterprises and their families did not have any rights to dividends. Their share in common property was invisible, imperceptible, and unapparent. Their rights remain personal and non-transferable. The workers did not hold any stock in their enterprises or other property certificates and they were left with nothing upon termination of their employment. As for social fairness, many citizens (including seniors, pensioners, students, the handicapped, housewives, teachers, doctors, government employees, and other workers in non-productive spheres of the economy) were prevented from exercising their "rights of a master" and sharing in the financial benefits of such rights because they had little or nothing in common with most other enterprises. Obviously, different enterprises, with different management and dissimilar production, have different levels of profitability of production. Therefore, "the rights of a master" of a large machinery or military factory would be considerably different from the "rights of a master" of a bakery or hair salon. This unreasonable situation caused nonsensical differences in the salaries of doctors, scientists, and teachers, on the one hand, and those of state enterprise workers, on the other. As a matter of fact, doctors in the former Soviet Republics have incomes seven times less than those of qualified workers. Scientists have to leave their jobs and work as taxi drivers; medical doctors work at several hospitals just to make ends meet; and government employees, to compensate for their low living standard often accept bribes and demand other types of satisfaction. Material stratification of the population required the government to locate more money for social needs. This caused the deficit in the state budget, increased inflation, and rising unemployment. Political instability stands in the way of new liberal movements supporting the economic freedom of new enterprises and causes great difficulties in the supply, production, and sales for these enterprises. This is essentially a self-destroying system.

From a *legal point* of view "the right of full proprietary authority" is not quite the same as absolute ownership. In The Law Of the Russian Federation on Ownership in the RSFSR, the so-called "right of full proprietary authority" was attributed to the category of estate rights, but not included in the section on "the right of ownership." Notwithstanding this fact, according to The Law on Ownership in the RSFSR (Article 5(2)(part 2)) "the rules on the right of ownership are applied to the right of full proprietary authority, only if the statutes or contracts between enterprises and an owner do not provide otherwise." Furthermore, according to Article 5(1) (part 2) of said Act, the holders

of the legal right of full proprietary authority have their rights secured by having "the same guarantees of legal protection of their rights and interests that an owner has, if the statutes of RSFSR do not provide otherwise." What is the difference between the "right of ownership" and the "right of full proprietary authority?"

As stated above, the theory of civil law recognizes the legal term "the right of ownership" as a triad of an owner's powers, including the subjective rights of: a) possession, b) use, and c) command. This triad is not only an academic template from any law school course on civil law, but also a legal term affecting the practical approach of lawyers in analyzing different relationships between people regarding the property in their possession or ownership. As also mentioned above, another equally important trait of the absolute right of ownership is the economic and legal capacity of an owner to realize his subjective rights by acting in his own best interest. As we recall, the "own interest" factor became a key element in distinguishing between the "absolute right of ownership" and the "right of operative management." However, there is a great deal of discussion in legal literature that says the triad of an owner's subjective rights does not completely exhaust the legal contents of the term "right of ownership."<sup>71</sup> One striking example of such imperfection in defining and understanding the right of ownership in civil law legislation is the so-called "right of full proprietary authority" and its equivalents in the legislation of former socialist countries.

An analysis of the legal regime of state enterprise belongings established by the government shows the essence and substance of an owner's or a master-enterprise's legal title to be qualitatively different from each other.

First, the "right of full proprietary authority" was attributed by legislation to the category of "estate rights" by placing the norms of said institution in the section which corresponds to "estate rights" but not in the section on "the rights of ownership." Thus, a legislator may assume that these rights are distinguishable from each other and, therefore, have to be governed by different legal norms having dissimilar legal regimes.

Second, the fact that a state-owner transfers to an enterprise its rights of possession, use, and command of assets does not, in itself, mean that the right of ownership was transferred. In his fundamental work, "State Socialist Property," A.V. Venedictov

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71. See, e.g., Maria Y. Kirillova, *Osobnosti pravootnoshenii sobstvennosti*, [Peculiarities of the Legal Relationships of Ownership], in XXVII SJEZD KPSS I MECHANIZM GRAZHDANSKO-PRAVOVOGO REGULIROVANIA OBSHESTVENNICH OTNOSHENII 73 (Sverdlovskii Juridicheskii Institut ed., 1988).

noted that the power of possession, use and command are realized by state enterprises "beyond their power and beyond their interest, but in the power of the state and on behalf of the state."<sup>72</sup> Obviously, state enterprises have different *interests* than the state itself. The contracts between the enterprises and the state do not resolve irreconcilable administrative conflicts between them. The parties to such agreements are contractors, who are in administrative subordination to each other regarding the subject of the agreement. The ministers and state agencies represent the interest of the state in communications with the enterprises. Apparently ministers have their own bureaucratic interests which are, in fact, contrary to the interests of the working collectives. These contradictions become antagonistic during the negotiation of plans, showings, and deductions. The administration of enterprises and working collectives is often subjected to heavy pressure from their ministers. The current legislation returned to this position by allowing the directors of state enterprises to be appointed by the owner. This gave the government additional means to affect "the master's activity." Thus, state enterprises do not have an absolute right to exercise the rights assigned to them by the state.

Furthermore, the process of transferring assets to state enterprises took place without the working collectives' participation, consent, option, or showing of will or desire. The fact is that, as a practical matter, transfer did not take place because the assets that had already been transferred and were legally in the possession of the working collectives from the moment the enterprises were established. Transfer was only declared by statute. The working collectives did not *initiate* such a transformation. No legal papers were ever signed. Furthermore, the working collectives had no *option* over whether to accept certain property. Most of the assets that were transferred were old and obsolete. Many enterprises were not initially profitable. In addition to "masters rights," working collectives took over the enterprises' duties and obligations. Working collectives also had to take "an advantageous gift" as to objects of socio-cultural purpose; these were often unprofitable. Most socialist countries had systems which tied workers' housing to specific enterprises, and this became a damper on the economic development of such enterprises. Enterprises were forced to pay for such housing, with a significant negative impact on their profitability since it put a tremendous financial burden on such enterprises and their working collectives when they were forced to compete in a market economy. Thus, "masters," in contrast with "owners," did not initiate

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72. VENEDICTOV, *supra* note 38, at 590-91.

a change in their status; they became "masters" without their consent, did not have the right to negotiate such a transfer, and could not help but accept the assets assigned to them.

Finally, the powers of a "master" to possess, use, and command property are restricted by law and are subordinate to the owner of this property. The superiority of the rights of an owner are evident in Russian legislation. According to The Law On Enterprises and Entrepreneurial Activity in Russia, "The owner of the assets exercises his rights to *manage* the enterprise either directly or through bodies authorized by him" (Article 30(2)). Another Russian Act On Ownership (Article 5(2)) states that "the owner, or persons who are authorized by the owner to manage his property, according to the law and charter of the enterprise, decides questions of establishing the enterprise and determining the purposes of its activity, reorganization and liquidation, and exercises *control* over the efficiency of using the entrusted property and its safety." Russian legislation does not contain a direct prohibition on withdrawal and confiscation of the assets assigned to state enterprises; an activity which has therefore been allowed.

Thus, to be an owner means not only to have a right to possess, use, and command property with your own interest, but also, to manage and control the property in your own power. To be able to exercise all these subjective rights the owner has to have an option of whether, and to what extent, he will use his power by initiating a change in his legal status. The above-stated "right of full proprietary authority" can only doubtfully be considered as a "right of ownership." However, under existing conditions, when enterprises undoubtedly are interested in the stability of their property relationships and the resolution of all possible questions regarding the violation of their rights of possession, it has been prudent and logical to assign them reliable rights of protection. In this connection, the legal norm of Article 5(1) (part 2) of the Act on Ownership of the Russian Federation, assigned the holders of the legal right of full proprietary authority "the same guaranties of legal protection of their rights and interests that an owner has" — a norm of pure judicial procedure. This norm obviously does not have any substantive ground. The author of this article personally shares the position of Dinus N. Safiullin that "the right of proprietary authority" can be considered neither the "legal right of estate," nor an "absolute" right, nor a "subjective" right.<sup>73</sup>

Enterprises will become neither masters, nor commodity-producers, if they do not possess constant rights of an inalienable and absolute character. Historically such character was inherent

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73. SAFIULLIN, *supra* note 61, at 45.

in the subjective rights and rights of estate.<sup>74</sup> As such, we can conclude that "the right of full proprietary authority" cannot reasonably be considered a serious alternative to the absolute right of ownership. Between the legal position of an owner and a "master" there is a considerable distance. Ignoring this difference or, guided by political considerations, intentionally disguising it is not going to help national economies. An enterprise is an important part of economics, and economic progress is dependent upon its success.

## VII. THE DUAL CHARACTER OF LEASE RELATIONSHIPS

Lease relations in the process of reproduction are nothing more than a form of the realization of ownership interests on the basis of economic exchange. There is no doubt that the idea of rent appears where and when the owner is not himself rationally able to possess, use and command his property in his present economic situation. Therefore, the necessity of rent is demanded by the hypothetical owner, either for subjective reasons (the owner's interests, inadequate physical conditions of the owner, or irrational methods of exploitation of the property) or because of objective circumstances (lack of due correspondence between production potentialities of rented property and the meeting of certain technical requirements and expectations of it). The subjective and objective factors are interdependent, interactive and mutually supplement one another.

The economic essence of the model of a leasehold estate consists of a clear differentiation of the powers of the owner and the lessee over the process of reproduction. Lease relations assume a distinction between the powers of the owner and the lessee over the leasehold in such way that a function of reproduction is borne by the owner-lessor and a function of production of material values by using the leasehold property becomes the main task of the lessee (commodity producer). Thus, the lessee, as a possessor of the means of production, which are let to him on hire by the owner, becomes himself a proprietor of such useful characteristics of the substantial rented factors of production, in which their owner was not interested. These "useful" factors are the abilities to create indispensable concrete social products. As to the lessor, he views the value of his property, which is let

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74. See, e.g., G. DERNBURG, PANDENTI, V.111, OBJAZATELSTVENNOE PRAVO 360-61 (2d ed., Moskovskii Universitet 1904); A.O. Kunizin, *O sile dogovora naima imushchestva*, in 9 GHURNAL MINISTERSTVA USTIZII 494 (1861); N.A. POLETAJEV, POLZOVANIE I NAEM IMUSHESTVA V IH VZAIMNIH OTNOSHENIJAH 22 (St. Petersburg, 1903).

on hire, in its ability to bring in a regular revenue under the guise of lease payments.

Under these circumstances, from the position of modern civil law, lease relations assume a special dual character: on the one hand, the lease is considered as an obligatory (contractual) relationship between the parties regarding the lease-held property; on the other hand, the lease is a type of real estate right, which in certain conditions can even provide the transference of legal title on lease-hold property.<sup>75</sup>

#### A. THE TRADITIONAL CIVIL-LAW APPROACH TO LEASE CONTRACTS

In spite of the fact that leases do not result in the transference of the right of ownership for leasehold property, the lessor, according to a lease contract, has to transfer certain rights of estate to the lessee: "the output and income, which are received by the lessee as a result of the exploitation of the leasehold property, are the owner's property."<sup>76</sup> Furthermore, "during the lease of an enterprise and other integral property complexes (entities), the lessee has a right to be reimbursed for the value of inseparable improvements on the leasehold property which have been made at the lessee's expense, irrespective of the permission of the owner for such improvement."<sup>77</sup> Thus, it is significant that the lessee becomes an independent participant in the commodity exchange with a property interest of his own. As we see, the legislators intentionally tore the cause-effect connection — "the owner of means of production - the owner of output" — as discussed above. Due to this rupture, a transfer of the rights of estate to the lessee can be achieved.

One manifestation of the absolute character of the right of estate is the so-called "right of following." This means that the right follows after the thing. For instance, if somebody has the right of estate with respect to a certain thing, then this right remains his in full capacity, in spite of the fact that the title for the thing could be transferred to another owner. The Basics of Leg-

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75. See, e.g., Andrei A. Baev, *Dvoistvenii Haracter arendniish otnoshenii* [The Dual Character Of Lease Relations], in ACTUALNII PROBLEMI PRAVOVOGO REGULIROVANIIA OBSHESTVENNICH OTNOSHENII V USLOVIACH PERECHODA K RINOCHNOJ ECONOMICE 106 [ACTUAL PROBLEMS OF LEGAL REGULATION OF SOCIAL RELATIONS UNDER CONDITIONS OF TRANSFORMATION TO THE MARKET ECONOMY] (Altaj Gosudarstvenii Universitet ed., 1991).

76. Osnovi Zakonodatelstva SSSR i Sojuzniich Respublic ob Arende [The Foundations of Legislation of USSR and Soviet Republic On Lease], SOCIALISTICHESKAYA INDUSTRIYA, December 1, 1989, art. 9. (The Statute is still in effect in the territory of Russia and some former Soviet Republics, including but not limited to Kazachstan.)

77. *Id.*

islation of the USSR and Soviet Republics on Lease state that, "the reorganization of an entity-lessor, as well as changing the title of ownership of leasehold property, is not a basis for changing the terms or for the dissolution of the contract" (Article 13, Part 2). Furthermore, the lessee's rights are also guaranteed by Article 33 of the Basics of Legislation, which states that "withdrawing the leasehold property, which was given to labor collectives for lease, is banned." The lessee also has the right to demand restitution of the lease hold property from an illegal possession by anyone, including the owner. The lessee is entitled to relief for any damages which were caused by the violation of his rights of possession or rights of use, even when such damages are the result of the owner's conduct. Finally, in spite of the fact that the lessor retains the legal title of ownership, Article 9, part 1, "imposing a penalty upon the lease hold property which is in possession of a lessee for the debt of a lessor is banned" (Article 15, part 2).

Thus, taking into account the factors set forth above, we can consider the legal capacity of the lessee from the position of "estate law" in contrast to the legal powers of the "master" and "operative manager." The legal powers of the lessee place him closer to the owner (in the vertical estate law capacities scale) than the bearers of the rights of "operative management" and "the right of full proprietary authority." The estate rights of the lessee are more stable than the rights of "the master" and "the manager;" they do not depend upon the "discretion" of the owner. Even shifting the title of ownership would not effect these rights. Under some circumstances the lessee even has priority over the owner; a fact which further consolidates his position as the user and the entrepreneur. Therefore, we can define three characteristics which analogize the rights of the lessee to the rights of the owner: a) the breadth of legal powers to use the lease hold property, b) the absolute character of possession, and c) the level of legal defense and the system of legal guarantees. In a certain sense, the legal title of a lessee to lease hold property can be perceived as a kind of quasi-ownership.

This is why it is not surprising that in the history of commodity-money relations, there were situations in which the lease became a practical alternative to the right of ownership. For instance, during the time Saint Petersburg was built, there was a goal to absorb capital. The Edict of July 8, 1733, was issued, thus builders were banned from selling their new buildings and real estate. However, in spite of this prohibition, the sale of real estate continued through the use of legal contracts for long-term

leases and cash payments in an amount mutually agreed upon.<sup>78</sup> Obviously, these conditions could satisfy the "buyers" of real estate only when there was confidence in the fact that they had acquired the absolute estate right for the property, not merely certain benefits of using the lease hold estate which depended on the unpredictable will and "discretion" of the owner. The existence of such transactions is evidence that historically, lawyers and society as a whole have considered the lease contract not only as a liability contract but also as an estate right. For example: the Soviet state farm in the Ukrainian resort town of Yevpatorija City granted a ten year fur farm lease, as an entity with a large area of arable land, to the cooperative "Runo" from Yekaterinburg (Russia) in 1990. Under the Law of the Ukraine Republic "On Property," which passed into law the next year on March 26, 1991, all lands in the Ukraine were pronounced the "national wealth" of the Ukraine, and the exclusive property of all Ukranian people (Article 9). Furthermore, the Ukrainian people exercised their right of ownership over the land through the Supreme Soviet of the Peoples Deputies and local bodies of state power. Obviously, Soviet state farms were no longer considered the owners of the land and they therefore became the improper lessors of the land. In other words, this was a legal act of transferring the title of ownership of the land. However, the lease contract with regard to Ukrainian land, entered into by a Russian cooperative and a Soviet state farm one year prior to issuing The Act "On Ownership" by the newly independent Ukraine, remains in legal effect, according to all former conditions of said contract and for the rest of its contractual term. The fact that the cooperative probably has to pay rent to the new owner of the land does not have any practical effect on the interests of the lessee.

As we have seen, in certain circumstances the lease can be considered an alternative to the right of ownership. However, in spite of the fact that the lease shows pronounced estate law traits, lease relations bear a dual civil law character. The liability side of lease relations can be seen in the legal norm of Article 9 of The Basics Of Legislation "On Lease," which clearly states that "granting property on lease does not involve transferring the ownership of the property." This primary liability norm finds its development in various restrictions of the lessee's rights. For example, the fixed term of the contract between the lessee and the lessor inevitably imposes some restraints on the entrepreneurial

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78. See, e.g., A. Pesterzeskei, *O veshnom haractere najma nedvizimich imushestv* [About Real Estate Character of The Lease of Non-Movable Property], in 7 ZURNAL MINISTERSTVA JUSTIZII 31-42 (1861).

interest of the lessee.<sup>79</sup> In view of the fact that the lessee's options of entrepreneurial activities in the sphere of production are restricted by the limits of "guaranteed success" during a given period of time, the heuristic effect of his entrepreneurial interests reduce the results in a general degradation in the heuristic entrepreneurship.

Accordingly, the legal model of the lease discussed above fails to provide "socio-economic transformation of the foundation of a socialist centralized economic system" because it does not transfer the legal title of the ownership of state property.<sup>80</sup> If we return to the above-explained theory of the right of ownership in civil law, we notice that the theoretical owner-lessor retains the so-called "nudum jus domini" — the right of ownership without factual possession of the property. The owner indirectly uses the lease hold property by means of receiving rent payments for the exploitation of his property by the lessee. Furthermore, the owner manages his property by exercising the right of control over the lessee's exploitation of the property. The owner also keeps his right to the return of the lease hold property after the expiration of the contract term ("fee simple in reversion").

#### B. LEASES WITH AN OPTION TO BUY AS A METHOD OF TRANSFORMATION OF OWNERSHIP RELATIONS

In spite of the partially contractual nature of lease relations, it is interesting to note that the process of privatization of state enterprises in Russia and the former Soviet republics was initiated by the Fundamentals of Legislation Of the USSR "On Lease." This legislation allowed labor collectives to organize so-called "lease collectives" or "organizations of lessees" with the power of legal entities to take an enterprise on lease, and with the right to buy the enterprise after the expiration of the term of the contract between the lease collective and the higher State's Ministry (Article 10). This is why so much economic literature has focused on the lease as a method of transferring state property to the private sector.<sup>81</sup>

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79. A. Honore, *Ownership*, in OXFORD ESSAYS IN JURISPRUDENCE 107-47 (1961) (The author shares the position of A. Honore who considered "open-ended" as one of one of the characteristics of the right of ownership.).

80. Here, under the term "transformation" of ownership the author understands cessation of the assignor's absolute rights at the same time the assignee's comparable rights on the same subject arise.

81. See, e.g., Pavel G. Bunich, *Pora sobirati arendatorov rati*, PRAVITELSTVENNII VESTNIK, Dec. 1989, Issue No. 25; see also Andrei A. Baev, *The Lease and the Right of Ownership: Issues Of Their Reciprocity* 203 (1992) (unpublished dissertation, Sverdlovsk Law Institute (Yekaterinburg, Russia)).

According to the Fundamentals of legislation, the lessee has the right to buy the enterprise by reimbursing the owner (the state), not for the market value of the enterprise (real estate, buildings, equipment, machinery, and all tangible and intangible assets), but by paying an amount equal to the value of the enterprise at the moment the lease was granted, minus the total of lease payments which had already been paid by the lessee (the labor collective) during the period of the lease contract. To illustrate, assume that the value of an enterprise at the moment of the parties' entry into five year lease relation was 1 million rubles. According to the lease contract, the lessee had to pay an annual rent in the amount of 160,000 rubles. Thus, after a five year period the lessee would have the option to buy the enterprise from the state for only 200,000 rubles. Accordingly, if the annual rent in this example had been 200,000 rubles, the lessee could acquire the enterprise for nothing.<sup>82</sup> Therefore, lease payment can be considered a payment for acquisition, rather than a payment of rent.

To begin analyzing this legal model of leases, I have to consider the fact that this type of a contract may not be a lease contract at all. There are two possible alternatives in this context. The lease-purchase can be a system of two independent transactions: a) the lease contract according to civil law's traditional understanding of lease relations, plus a contract of purchase; or b) a contract of purchase on an installment plan. A brilliant example is offered by Gaius, in which he illustrates a possible comparison between a lease-purchase and a sale:

If a band of gladiators are delivered on the following terms, that is to say, that for the performance of every one who leaves the arena safe and sound there shall be paid twenty denarii, and for every one who is killed or disabled there shall be paid one thousand denarii, it is disputed whether the contract is one of purchase and sale or of letting and hiring; but the better opinion is that the unharmed were let and hired, the killed or disabled were bought and sold, the contracts depending on contingent events, and each gladiator being the subject of a conditional hiring and a conditional sale, for it is now certain that both hiring and sale may be conditional.<sup>83</sup>

There is no doubt that this conditional type of contract or system of contracts has its own reasons for existence. An exam-

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82. This is true if the lessee does not retain the amortization deductions for depreciation of the property, that are allowed by law, but regularly makes these payments to the owner of the property. As a rule, the amount of deductions is fixed and quite reasonable. Indeed, this "redemption" model was also complicated by economic appraisal of the enterprise, inflation and other social-economic peripeteia.

83. GAIUS, *INSTITUTES OF ROMAN LAW*, bk.III, § 146 (E. Poste, Trans. & C. Whittuck ed., 1904) (1st ed. London 1865).

ple from more civilized times may be found in the contract of *Wiederkauf* or *Rentenkauf*, which had widespread application in the Western provinces of Russia, as well as in many German Laws.<sup>84</sup> This contract concerns the sale of an estate by an ecclesiastic to a private person with a special condition that the buyer make accept a perpetual obligation to pay seven percent annual interest on the amount of money which he paid to the seller. In exchange, the seller waives his right to demand the surrendered amount of money, and if the buyer breaks the terms of the agreement, he has to reimburse the seller with the full amount of the selling price or the property itself. This type of contract can be considered for buying-selling relations because the buyer did not acquire the absolute rights of the owner yet he still had to bear the burden of forever paying an annual percentage.

Therefore, it can be concluded that the history of legal regulation on the relations of possession recognizes different types of legal titles, external to the traditional civil law approach to both ownership and lease relations. Some of these titles bear the absolute character of estate rights. Accordingly these can be considered possible alternatives to ownership relations. As a rule, these alternatives arise from the rights of "jura in re aliena" (the rights on alien's property), which are mostly outside of the current research because of their general unsuitability to the proposals for privatization. The rights of *superficies*, *emphyteusis*, *hypotheca et servitutes*, and *usufruct* express the conditions of restraining the ownership for the certain thing or, to be precise — the law under which such a condition is maintained.<sup>85</sup> Servitudes are mainly someone's rights to another's chattel. The owner of the chattel must tolerate something or endure a shortage of something for the convenience of the other. While we are basically looking for a method which could harmonize the interest of the owner with the entrepreneurial plans of the labor collective, we can see how the servitude lays a heavy burden on the owner of the property.<sup>86</sup>

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84. V. Bartenev, *Dogovor Wiederkaufa in zapadnich guberniach*, 4 ZURNAL MINISTERSTVA JUSTIZII, at 38-39 (1865).

85. Soviet Civil Law did not recognize the institution of servitudes, and therefore my research relies on theoretical propositions of pre-revolutionary Russian Civil Law. See, e.g., A. Gusakov, *K voprosu o teorii servitutnogo prava*, 4 ZURNAL GRAZDANSKOGO I TORGOVOGO PRAVA, at 724-741 (1871); N. Mullov, *Voprosi Mr. Meyera o servitutach*, 7 ZURNAL MINISTERSTVA JUSTIZII, at 3-13 (1862); I.Sh., *Voprosi dlia nashich juristov: Ob ogranichenii prava sobstvennosti*, 17 ODESSKI VESTNIK (1863); I. Gornovich, *Issledovanie o servitutach*, 8 ZURNAL GRAZDANSKOGO I UGOLOVNOGO PRAVA (1883); I.B. NOVIZKIJ, RIMSKOE CHASTNOE PRAVO, at 90-96 (VJuZI ed., 1948). However, The Russian Law "On Ownership" (approved on December 24, 1990) assumes a possibility of such relations in current Russian Civil Law (art. II, part 8).

86. See, e.g., Baev, *supra* note 81, at 186-92.

Returning to the lease-purchase contract; in my opinion, these relations cannot be considered as acts of privatization as defined previously. Basically, a lease with an option to buy the leased property does not necessarily presuppose that the title of property would be transferred. Not only could the lessee exercise his option to purchase the property, he can also refuse the right to make such a purchase. Indeed, the lessee's intent to purchase depends on a whole complex of objective and subjective reasons and is therefore not predictable. Obviously, during the term of the lease the lessee does not have any absolute guarantees of developing his "entrepreneurial interest." Consequently, the indispensable stability of his property relations is absent. Furthermore, the act of transforming the title of ownership of the lease hold property from the owner to the lessee is reflected in the contract of purchase (if a lessee decides to exercise his right to purchase after the expiration the contract's term) as well as a "transmission list" that is usually attached to the contract of purchase although not on the lease contract itself. The act of purchase, on the other hand, stands far distant from the time of signing the initial lease contract. Obviously, the purpose of privatization is not achieved. Society must also be careful about the fact that the lessee in such relations has a definite preference over each and every other member of society with regards to the unreasonably low price of the purchase of the enterprise and the possibility that no one else will participate in the bargaining. The lessee becomes the only candidate for such an artificial "privatization." Is this a way around the law? Is this a round-about way which labor collectives can use to avoid the public privatization of their enterprises? For instance, why should industrial workers obtain larger claims on state assets than workers in less capital intensive industries, such as teaching, medical assistance, or legal practice? Why should workers in successful firms become wealthier than workers in less successful firms? Indeed, the lease privatization would leave a major part of the country's population untouched: those who are not working in profitable enterprises or who are not working at all. This is why the Russian Law "On Privatization of State and Municipal Enterprises in Russia" in Article 19, part 2 changed the basic approach to lease relations, denying the possibility of crediting lease payments towards payment of the purchase price. The law began to look at the enterprises as a usual commodity, which had to be sold according to the economic laws of the market. Exceptions were made only for enterprises which were working under the existing lease contracts at the moment when the law went into force.

Thus, it is my opinion that this statute essentially excludes the lease from consideration as an alternative in the process of privatization. The lease of enterprises without the option to buy the leased property loses all incentive and interest for labor collectives.

### VIII. THE SEARCH FOR ALTERNATIVES AND CURRENT PROBLEMS OF A COMPREHENSIVE PRIVATIZATION PROGRAM

As stated above, one obvious reason for the serious economic, social, and political problems encountered by comprehensive privatization is the fact that private enterprise systems can rarely prosper within a centrally planned economy. The Russian economy was pushed into large-scale privatization prematurely. It is becoming clear that privatization cannot be attempted unless other fundamental economic reforms are also being undertaken. Instead of realizing the initial demonopolization<sup>87</sup> and decentralization of the national economy by taking steps such as eliminating the means of government control, demolishing ministries and agencies, building up a banking system before privatization,<sup>88</sup> reforming trade to encourage competition and export, establishing legal incentives for foreign investors,<sup>89</sup> liberalizing prices and foreign trade,<sup>90</sup> reforming prices and liberalizing the market, proclaiming private ownership of the rights to land, enacting legal reforms to assure proper disclosure, developing bankruptcy, tax and antitrust legislation,<sup>91</sup> or enforcing contracts and due process, the Russian President and Parliament, already accustomed to administrative remedies, went ahead and proclaimed yet another government plan - the Program of Privatization.<sup>92</sup> In a cer-

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87. Some authors believe that successful privatization in the U.K. required the privatized firm to operate in a competitive environment. See, e.g., JOHN VICKERS AND GEORGE YARROW, *PRIVATIZATION: AN ECONOMIC ANALYSIS* (1988); Stanley Fischer clearly stated that "demonopolization should precede privatization." FISCHER, *supra* note 2, at 3.

88. See, e.g., LAWRENCE J. BRAINARD, *STRATEGIC FOR ECONOMICAL TRANSFORMATION IN EASTERN EUROPE: THE ROLE OF FINANCIAL REFORM* (1990) (on file with the Bankers Trust Company).

89. See, e.g., *Foreign Participation in Russian Privatization Must Deal With Various Obstacles*, 3 *RUSSIA AND COMMONWEALTH BUS. L. REP.*, No. 21, March 9, 1993, available in LEXIS, World Library, ALLWLD file.

90. See, e.g., BORENSZTEIN & KUMAR, *supra* note 2, at 319.

91. See, e.g., V.K. Mamutov, *Pravovoe obespechenie uslovii dlia razvitiia sorevnovania v ekonomike* [Legal Guarantees of Conditions for Developing Competition in Economics], 6 *GOSUDARSTVO I PRAVO*, at 56-64 (1992) (About the developing Russian anti-monopoly legislation).

92. Generally speaking, there are annual State Programs of Privatization, which have to be discussed and approved by the Government of the Russian Federation

tain sense, this program reflects the entire range of opinions about privatization and, accordingly, it includes different approaches to the process of transferring state property to the private sector.

#### A. EMPLOYEE OWNERSHIP

First of all, the purpose of privatization in Russia and other socialist countries is not private ownership, but rather employee ownership. Employees are the key in this process. As a matter of fact, the Russian interest in employee ownership is a direct result of what they learned from the experiences of employee ownership in the United States. For instance, through employee stock ownership plans (known as ESOPs for short), broadly distributed stock option plans, and other arrangements, more than 15,000 American companies are partly or wholly employee-owned. About 15 million American workers collectively own over \$150 billion in stock.<sup>93</sup>

The Russian Government created a privatization system that permitted employees of large enterprises to choose one of three options for privatization. One of these options provides for 25 percent employee ownership of the preferred stock at no charge and the right to buy 10 percent of the common stock on preferential terms. Additionally, the managers of the enterprise and the administrative officers have the right to buy 5 percent of the common stock, also on favorable terms such as a reduced price (Variant I). A second option allows the employees to buy 51 percent of the ownership (a controlling interest in a corporation) at a price which is 70 percent higher than the nominal value of the said interest (Variant II). Lastly, a third option offers the employees 20 percent ownership in bankrupt firms, restructured to face value, and an additional 20 percent ownership on preferential terms (Variant III).<sup>94</sup> All three variants provide the employees with significant rights to convert their preferred stock into common stock with the right to vote. A labor collective also has

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and passed by the Russian Parliament—the Supreme Soviet of the Russian Federation. The Programs establish methods and scale of privatization including units and enterprises which are subject to compulsory transformation of ownership rights. For example, according to the State Program of Privatization for 1993 more than 5,000 of the largest state enterprises are subject to privatization through corporatization.

93. Rosen Cory, *Employee Ownership May be Next Russian Revolution*, 8 THE FIRST INDEPENDENT RUSSIAN-AMERICAN NEWSPAPER "WE," April 19 - May 2, 1993, at 7.

94. According to Kommersant, labor collectives, as a rule, are expected to prefer to acquire a controlling interest in a corporation: 77.4% of enterprises using the second variant of employment privatization; 21.2% - the first variant; and only 1.4%, or 78 enterprises, were privatized according to the third variant. *Krugooborot vauchera v prirode*, 27 KOMMERSANT, July 5, 1993, at 16.

the right to establish a special Joint Stock Fund of Employees of The Enterprise (FARP), with a volume of five to ten percent ownership, which has to be reorganized after a public auction. Stocks of this Fund have to be given away to employees at no charge or at a cut price.

Obviously the employee privatization schemes reflect the social politics in the country. They serve as the logical conclusion of long term efforts by the legislature to find a method of allotment of public property by placing state assets at the disposal of labor collectives (the right of "operative management" and the right of "full proprietary authority"). There are three major problems with this forms of employee privatization.

First, this model of privatization would sharply limit new public initiative and investment. Not everybody with money can participate and not every asset can be purchased. It aggravates the investment climate and binds free capital. This scheme also imposes various obstacles to foreign participation in Russian privatization.<sup>95</sup>

The second problem is a question of equity and fairness, since this type of transference of assets would benefit only a limited segment of the population (which is already privileged by holding jobs in the largest firms). Indeed, the "employee ownership scheme" also raises an issue of "employee monopolization." For instance, the privatization of local dairies and meat factories has now been suspended in the Sverdlovsk Region. According to the Regional Administrator, this was prompted by the fact that privatization was not being conducted in the interests of the state and collective farms.<sup>96</sup> Under the existing system of privatization, the controlling block of shares (51percent) is in the hands of a collective of processors, which automatically has a monopoly and can dictate its own conditions. This move has been supported by state and collective farmers, but the directors of processing works consider the decision illegal and they intend to take it to court.

The third problem concerns the efficiency of self-managed enterprises. Economic theory suggests that such enterprises will "underinvest and have shorter planning horizons."<sup>97</sup> Indeed, it would be difficult to attract private investors into acquiring minority stakes in a worker-controlled enterprise since the workers could curtail dividend payments by granting themselves salary in-

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95. See, e.g., *Foreign Participation in Russian Privatization Must Deal With Various Obstacles*, *supra* note 89.

96. *Sverdlovsk Oblast Suspends Privatization of Processing Enterprises*, [Moscow radio broadcast 1600 gmt 21 April 1993], April 30, 1993, available in LEXIS, World Library, ALLWLD File.

97. BORENSZTEIN & KUMAR, *supra* note 2, at 315.

creases. Furthermore, in order to frighten off outside investors from the enterprise and buy it out themselves, the administration of such an enterprise often publicly misrepresents facts regarding the profitability and industrial potential of the enterprise through the mass media. This is a significant problem since there is no independent auditorial service to verify the advertised information.

Thus, employee ownership alone can not cure Russia's problems. Even so, it is still a much better method for solving those problems than the other alternatives.

### B. THE VOUCHER SCHEME

Another key element of the privatization process so far is that most of the shares currently being auctioned to the public are only sold for privatization vouchers, not cash. Employees are able to purchase shares for cash, but shares offered at privatization auctions are being sold to everyone else only for vouchers. By the end of July 1993, a total of 2,700 Russian enterprises have been sold through voucher auctions in Russia.

Under this program, the bulk of state property in Russia will be privatized by auction in 1993. The largest part of state assets, or 80percent of federal property and 45percent of municipal property, will be sold to private owners only for privatization vouchers.<sup>98</sup> The proportion of municipal businesses whose shares will be available for vouchers may be increased up to 90percent by a decision of the local legislatures (local Soviets).

The concept of privatization through vouchers reflects a distribution scheme in which at least some shares of the ownership in state industrial enterprises could be transferred to private citizens for free.<sup>99</sup> According to the recent Edict, "every Russian Federation citizen shall have the right to receive one privatization voucher of equal nominal value of each issue."<sup>100</sup> The nominal value of the 1992 privatization voucher was fixed at 10,000 rubles.<sup>101</sup> It was established that the 1992 privatization vouchers

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98. S. Viktorov, *Pravitelstvo postavilo na vaucher [The Government Staked on Voucher]*, KOMMERSANT, January 27, 1993, at 9.

99. The idea of a voucher system appears to have originated in proposals for privatization in Czechoslovakia. This scheme was also approved in Romania and emulated to some degree in Poland. For purposes of this article we will concentrate our attention on the Russian model of voucher privatization.

100. Edict Enacting Russian Federation System Of Privatization Vouchers, Statute Of Privatization Vouchers, The Russian Federation President's Edict No. 914, art. 2, August 14, 1992.

101. See, e.g., BORENSZTEIN & KUMAR, *supra* note 2, at 308-09. According to different voucher schemes, the vouchers may or may not have a monetary value or be tradeable between individuals. In the Czechoslovak initiative, the vouchers were to be denominated in "points" and could only be used to bid for shares in state-

should remain in effect from December 1, 1992 to December 31, 1993. Organizations and enterprises are prohibited from accepting privatization vouchers as instruments of payment for goods, services or work. However, privatization vouchers are otherwise negotiable instruments and they may be bought and sold on the market without restriction.

Free voucher distribution benefits every citizen within the country—partly because the state, according to the Constitution, is not considered to be the actual owner of the enterprises, but only “the exponent of all peoples’ will” and the main administrator.

However, in my opinion, the voucher scheme faces several serious problems of implementation. First of all, the scheme narrows the chances for investing in privatized enterprises and retards their economic development. This is due to the President’s Decree which set 29percent as the minimum number of shares of privatized enterprises that can be sold for vouchers. Again, money would not play a crucial role in the process of buying out enterprises since money can not buy everything in Russia. Obviously, this will also exacerbate the investment climate and tie up free capital.

Indeed, the voucher scheme will first affect foreign investors. In spite of the fact that the provisions in the law generally permit foreign individuals or entities to participate in privatization transactions and use vouchers for this purpose on an equal basis with Russian persons or entities, there are certain provisions in the law which may present practical obstacles to the acquisition of privatization vouchers by foreign investors. For instance, vouchers can be legally purchased only with rubles, a non-convertible currency. This process is complicated by the lack of adequate currency regulation over the transfer of large amounts of hard currency in and out of the country and its conversion into rubles. The privatization program also requires foreign investors to open special bank accounts to “keep” the rubles used in the privatization process. The unpredictable activity of the Russian Central Bank, galloping inflation, different government and market rates of the ruble, and currency reforms combine to create considerable risk for such investments. Foreign investors may also be required to obtain permission from the Russian Ministry of Finance to acquire privatization vouchers and licenses from the Central Bank in order to acquire any ruble-denominated securities such as the privatization vouchers.

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supervised auctions of individual state enterprises. However, the Romanian example evinces that the liquidity value of vouchers would be considerably diminished if they were nontransferable.

Secondly, the current system of privatization check cancellation provokes the repeated circulation of vouchers after their primary utilization through check auctions. Privatization vouchers used as the instrument of payment in purchasing privatization objects are supposed to be redeemed and withdrawn from circulation. This task, though it offers no technical difficulties in Western countries, is quite serious in Russia. The critical shortage in telecommunication networks and computerized systems, the federal structure of the country, the complicated administrative divisions, the absence of practical experience, the involvement of the entire country's population, and the huge number of vouchers all combine to make the process of accounting exceedingly complicated. There are already some cases in which the police have discovered forged vouchers.<sup>102</sup> The officers of branches of the State Savings Bank, who are responsible for allotting the vouchers among the citizens, have easy access to unregistered vouchers and can easily abuse their power. The officers of the State Savings Bank (which has 200,000 employees and 42,000 branches) have the right to register homeless people—who apparently can be registered more than once. Students, serviceman, and other people who do not have a permanent residence can receive vouchers more than once as well, by visiting different branches of the Bank. Other people in these categories may not receive their legal vouchers from a place where they are registered. Such unclaimed vouchers can then be resold by Bank officers.<sup>103</sup>

It is also quite possible for entrepreneurs to liquidate the vouchers by exchanging them for cash at the exchange-value rate, which is different from the market value of the voucher, using a "cash scheme." Because of the fact that cash does not play the most significant role in market circulation in a barter economy, speculative companies can buy up a great number of vouchers for cash and then make an offer to the labor collectives of state enterprises to exchange these vouchers for the state enterprise's quoted production such as metals, gasoline, machinery, or automobiles. Such transactions distort the market and affect ordinary voucher holders. Additionally, this "cash scheme" lets state enterprises liquidate their stated capital (which includes basic production assets and floating capital of the enterprise) by exchanging it for vouchers with a certain cash value. Consequently, state enterprises can legally utilize not only their own

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102. Anastasia Nariskina, *Igra s vaucherami: Vozmozni varianti* [Playing with Vouchers: There Are Variants], 2 MOSCOVSKIE NOVOSTI, Jan. 10, 1993, at 3B.

103. *Id.*

assets, but the property of the state as well. This is obviously a haven for abuse and bribery.

To summarize, the voucher scheme involves additional expense, does not give the people a significant share of state ownership, equalizes all citizens with their shares without respect to their age, job position and labor contribution to the divided state property, and, in my opinion, bears more of a political than an economic content.

### C. GOVERNMENT CONTROL

In 1993, Russian's sub-surface and forest resources, gem grading, highway and railroad maintenance, public utilities and gasoline distributors will be excluded from privatization.

Assets of the Russian Republic's monopoly producers, which account for more than 35percent of certain goods and services produced in the Russia, may be privatized only under the strict control of the government and the State Property Management Committee. This rule will also apply to the privatization of businesses with more than 20,000 employees or over a billion rubles' worth of fixed assets. In addition, privatization of the tobacco, medical-equipment, mining industries, and distilleries will be restricted.

Controlling blocks of shares in privatized enterprises may be held in federal ownership for a period of up to three years with respect to the following enterprises (by lines of activity<sup>104</sup>): communications; generation and supply of electrical power; extraction, refining, and sale of oil and natural gas; extraction and processing of precious metals, precious stones, radioactive, and rare earth elements; development and production of weapons systems and ammunition; alcohol, vodka, and liquor production (this production is an exclusive state monopoly); air, rail, and water transportation; specialized enterprises designed for the building and the operation of facilities necessary to ensure national security; wholesale enterprises engaged in procurement for state requirements; export and import operations to meet interstate agreements; and many others.<sup>105</sup> When controlling blocks

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104. In my opinion, the differentiation of enterprises regarding "the line of their activity" is rather reasonable. The fact is that before this Edict the law differentiated the categories of enterprises according to their branch of industry. Thus, the enterprises were artificially divided into several categories with regard to their Ministry subordination, but not to "the line of activity." But, for instance, in the system of the Ministry of railroad transportation there are construction, machinery, trade and other service enterprises. The same can be said about practically all branches of industry.

105. Industrial Policy on the Privatization of State Enterprises, The Russian President's Edict No. 1392, Nov. 16, 1992.

of shares in privatized enterprises are placed into federal ownership for a period of up to three years, all the shares within these blocks shall be common shares (voting shares) to be at the disposal of the respective properties' management committees, pending expiration of the aforesaid period or decision on sale thereof.

Furthermore, upon conversion of enterprises into joint-stock companies (whose privatization is permitted only after a decision by the Russian Federation government), the State Committee for Management of State Properties shall be entitled to make decisions on the flotation of their shares and their right to issue so-called "golden shares"—these golden shares give the holder, for a period of up to three years, the right to veto decisions made at shareholders meetings regarding the reorganization or liquidation of the enterprise. The State Committee for Management of State Properties shall also be entitled to decide on amendments and addenda to the Rules and Regulations of the joint-stock company; participation in other enterprises and associations of enterprises; and mortgages, leases, sales, or other alienation of assets determined by the enterprise privatization plan.

The reason for government concern over the power to veto is obvious: the current economic recession may induce enterprises to shift their profile and to relieve themselves of superfluous assets. According to the government of the Russian Federation, "it is impossible to allow, for the sake of momentary benefits, industrial capacities of special purpose to be lost, which were created at the expense of the State and in the interests of the State."<sup>106</sup> As we can see, this proposition is similar to the phenomenon of "the right of operative management," defined by the law as: "Assets, assigned *by the owner* to State institutions or other establishments, which are *financed from means of the owner*, are in the operative management of this institution, which exercises within the *limits established by Law* and *according to the purposes of its activity*, tasks of the owner and *purposes of the assets*, and the rights of possession, use and command of these assets."<sup>107</sup>

The golden share shall be held in state ownership. It may not be mortgaged or put in trust. Sale or alienation of golden shares in other ways, prior to the expiration of the term thereof, shall be allowed only upon a decision by the issuing body at the foundation of the joint-stock company. Any other sale or aliena-

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106. *Preobrazovat giganti* [Press-conference at the Goskomimuchestvo], THE TRUD, Dec. 31, 1992.

107. ZAKON RSFSR O SOBSTVENNOSTI V RSFSR, *supra* note 54, art. 5(3); *see also* text accompanying notes 52-53.

tion shall convert the golden shares into common shares, terminating the special powers vested in the owner.

The institution of the "golden share," however, is not a phenomenon of Russian privatization only. For example, the "golden share," a very effective defense mechanism against foreign investors, was introduced in the French privatization program recently rolled out by the new right-wing French government.<sup>108</sup> The French government uses the "golden share" to obtain certain rights over privatized companies that could effectively protect such companies against foreign takeovers forever. According to the program, a "golden share" will limit voting rights over a set threshold, place one or two non-voting government appointees on the company's board, and grant the government a veto over the sale of any assets it deems "essential to the national interest." Indeed, there can be no economy without government regulations.

#### D. THE LEASE VARIANT

As of July 1, 1993, 19,438 state enterprises in Russia (10 percent of all enterprises) were still on lease.<sup>109</sup> Most of them entered into their lease contracts with the Branch Ministries prior to the enactment of the July 3, 1991, Privatization of State and Municipal Enterprises Act, which practically prohibited the leasehold enterprise buy-outs originally allowed under the former Fundamentals of Civil Legislation of the USSR and the Republics. As to these enterprises, the civil law doctrine that the law does not have retroactive (*ex post facto*) power applies.

According to the Russian President's Edict No. 1230, "On Regulation of Leasehold Relations and Privatization of Leased Property" (enacted on October 14, 1992), the buy-out of lease contract properties concluded prior to the enactment of the Privatization of State and Municipal Enterprises Act. Furthermore, the Edict stated that specifying the time period, amount, procedure, and conditions of a buy-out is allowed and shall be done on the lessee's application, under the lease contract with the right of a buy-out. If the lease contract failed to set out the specific time period, amount, procedure, or conditions of buy-out, then the transaction shall be conducted in one of two ways: a) where the contract value of state (municipal) property at the

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108. The program, which could raise at least 300 billion francs (\$54.72 billion), includes 21 companies ranging from thriving giants such as oil concerned Society National Elf Aquitaine and car maker Renault SA to money-losing headaches like Air France. Charles Fleming, *France Unveils Privatization Plan To Raise at Least \$54.72 Billion*, WALL ST. J., May 27, 1993.

109. 27 KOMMERSANT, July 5, 1993, at 17.

time of its lease amounts to one million rubles or less, it would fall under an additional agreement on buy-out of leased property and an assessment of the buy-out amount upon the lessee's application; or b) where the contractual value of state (or municipal) property at the time of its lease exceeds one million rubles, the leased enterprise would be transformed into a publicly held joint-stock company (Article 7). Thus, as we can see, the labor collectives, in order to exercise their contractual option to buy-out state properties, must enter into so-called additional agreements at the time of buy-out and such agreements are then considered to be an integral part of the earlier lease contract. However, any dispute over the terms of the additional agreements of the buy-out of state (municipal) property under lease contract would come under the jurisdiction of a court of arbitration. Obviously, the lessees cannot be sure about the success of resolving such disputes. The additional agreements clearly call into question the lessees' contractual rights to buy-out leasehold state and municipal properties. Thus lessee's right loses its absolute character, as discussed above, through the government's interference with contractual relations.

Indeed, God gives and God takes away. There are other examples such as when the government grants special rights to certain enterprises. For instance, by a special Edict of The President of the Russian Federation (August 14, 1992, No. 631), a piece of land, a square of 2.2 hectare (5.44 acres), was given on lease to the Moscow Factory "Mikma" with the right to purchase after the expiration of the term of the contract.<sup>110</sup> Government interference in lease relations often cause the leases to lose their civil-law contractual character. As such, such interference can not be considered to be a significant alternative to the process of privatization.

## IX. CONCLUSION

As was expressively stated in January 1988 at the International Conference on Problems of Collective Property in Oxford, a man during the process of the evolution of society passes through several stages in his social development: slave, serf, wage worker, and owner.<sup>111</sup> Indeed, the owner is the highest level and the main goal of man's socio-economic development as the primary economic cell of society. Only economic freedom can provide choice of interests, political liberty, stability, independence of thought, intellectual development, and moral perfection. In

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110. Dmitrii Tushunov, *Malenkie mashini s bolshimi perspektivami*, 27 KOMMERSANT, July 5, 1993, at 23.

111. See, e.g., ARENDA: SUSHNOST I PRACTICA, UCHEBNOE POSOBIE, at 22 (1989).

other words, ownership relations are primary, everything else is secondary. The Program of Transferring Toward The Market of Russian economy stated that “[p]roperty in the hands of everybody is a guarantee of stability of society, one of the most important conditions for the prevention of social and national shocks.”<sup>112</sup> Privatization provides equity of opportunities, establishes conditions for growth of entrepreneurship, and permits competition between different forms of ownership.

At the same time, privatization intensifies social tension. What is happening in former socialist countries is essentially a transfer of power. Seventy-six years ago Vladimir Lenin began the harmful process of nationalization under the revolutionary slogan that “the question of ownership is the question of power.” This policy was realized during the so-called “cavalry attack on the capital” after the Socialist Revolution in October 1917 and has continued throughout Stalins’s bloody collectivization. In essence, privatization is also the transformation of power. The loss of entitlement through a privatization policy is one manifestation of this transformation. This is why the legislators do their best in trying to establish rules and regulations for privatization in accordance with their political leanings. There is no ruling party in Russia now and Russian legislation therefore expresses the will of different political minds. This introduces into privatization legislation a set of characteristics which are inherent to the various alternatives to “clean privatization.” Some of these statutes, as we understand them, are, more often than not, incompatible with the essence of Western “pure privatization.”

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112. PERECHOD K RINKU: KONZEPZIJA I PROGRAMMA, at 5 [Transferring Toward Market: The Conception and The Program] (Aug. 1990).