ISSUES OF LEGAL REGULATION OF ENERGY COMPANIES IN CORPORATE CONTROL OF PROCUREMENT

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As of today, effective Russian laws contains a range of measures for controlling activities of major energy companies. These may include optional rules allowing major companies to decide on control forms and methods, as well as obligatory ones violation of which can cause negative consequences for the company.

It often makes transactions too long, sometimes even impossible. The article describes issues related to procurement by energy companies in accordance with Federal Law No. 223-ФЗ on Procurement of Goods, Works, Services by Specific Types of Legal Entities dated July 18, 2011, discovers excessive provisions in current laws, inconsistencies in rules in this field of legal regulation. The author proposes ways to improve legal regulation of internal procurement control.

Keywords: *energy law; legal status of energy companies; contractual regulation in the energy sector; procurement provisions.*

Several laws were adopted to promote competition, including: Federal Law No. 135-ФЗ on Competition Protection dated 2006 (hereinafter referred to as Federal Law No. 135-ФЗ), Federal Law No. 223-ФЗ on Procurement of Goods, Works, Services by Specific Types of Legal Entities dated July 18, 2011 (hereinafter referred to as Federal Law No. 223-ФЗ), and Federal Law No. 44-ФЗ on the Contract System for Procurement of Goods, Works, and Services for State and Municipal Needs dated April 5, 2013 (hereinafter referred to as Federal Law No. 44-ФЗ).

The Expert Board for the Procurement Law (223-ФЗ) will be created within the Federal Anti-Trust Service responsible for improvement of the procurement legislation, discussion of the law enforcement practice and preparation of anti-trust compliance during procurement under 223-ФЗ. [1] The Federal Anti-Trust Service expects companies to develop an industry-specific document on procurement in cooperation with the regulator, thereby creating standards of operation, their activities are to be checked against by the companies themselves and the Federal Anti-Trust Service, implement anti-trust compliance during procurement under 223-ФЗ, which will reduce the number of violations during procurement by state companies, considering that, in 2019, the Anti-Trust Service received over 13.6 thousand complaints under the Procurement Law, 91% more than in 2018. [2]

Overall, almost 13.7 thousand complaints were received under 223-ФЗ in 2019, which is 91.3% more than in 2018, about 4.4 thousand of them were considered reasonable. [3]

Legal studies are rightly focused on various aspects of legal regulation of procurement. Thesis research by A.V. Molchanov addresses anti-trust requirements for bidding; M.S. Solovyev studies administrative and legal grounds of public procurement; A.Yu. Misak explores legal problems of corporate procurement regulation with state participation. [4]

The state-owned energy companies listed in Article 1 of Federal Law No. 223-ФЗ shall perform procurements in accordance with the Procurement Regulation approved by the company. According to Article 2 of Federal Law No. 223-ФЗ, it is the Customers' responsibility to develop and approve a document on procurement procedures (Procurement Regulation).

Generally, state-owned energy companies are large holdings comprised of a number of subsidiaries located in Russia's further-flung regions and abroad. [5]

Therefore, there is always a problem with parent company's controlling compliance of subsidiaries with procurement laws, as well as internal regulations reflecting the entire holding's interests.

This problem can be solved by implementing a number of measures. For instance, it may be made by developing a standard procurement regulation for the entire corporation that will be recommended for approval by all subsidiaries of the holding.

In addition, each company should have a structural unit responsible for correct arrangement of procurements, while the parent company should have a procurement management center (hereinafter referred to as the PMC) which, apart from conducting procurements for the company itself, will be responsible for guidance, development and improvement of local company regulations, control and prevent violations by subsidiaries.

Depending on the tasks to be performed by each energy company, main procurement issues can be approved by the PMC only or partially delegated to structural units to be dealt with locally.

The most important procurement issues include procurement planning by the Group of Companies for which the PMC shall:

- Develop and approve an annual procurement plan of the Group, quarterly amendments or addenda thereto;
- Establish procurement methods under the effective Procurement Regulation;
- Determine Organizers of specific procurements, as well as single-source procurements by marketing research;
- Issue recommendations or instructions to the procurement initiator on forming of lots for planned Procurements, form the lots itself, if necessary;
- Decide on joint procurements by the Group Companies.

The PMC should be responsible for methodological support of the Group Companies' procurement activities, including the following functions:

- Development of standard forms, templates and sample documents used by the Group Companies during Procurements and included in Procurement documents, notices of invitation to tender;
- Compilation of a set of standard draft contracts/agreements (standard terms and conditions) used for Procurement;
- Development of standard evaluation methods to be used by the Group Companies during procurements, included in procurement documents, notices of invitation to tender;
- Development of draft orders, instructions, recommendations and regulations on specific procurement arrangement issues;
- Interaction with state authorities and organizations, state corporations and other stakeholders on methodological issues of the Group's procurement activities;
- Clarification of the procedure of application of the Procurement Regulation and other issues governing seminars holding.

The following authorities of the PMC are also important and rather effective:

- Monitoring of procurement activities of the Group Companies;
- Controlling procurement activities of the Group Companies;
- Having single-source (contractor/executor) procurements approved by the PMC under some more significant contracts, for example, in case of a failed procurement. This will help prevent/remedy potential mistakes of subsidiaries within the holding during procurement procedures, correct procurement

documents, including in case of typing errors or other inaccuracies.

However, each holding will have companies beyond the scope of Federal Law No. 223-ФЗ, in which case imposing strict procurement rules can unnecessarily limit their activities, leading to financial losses and overcomplication of the already tedious procedure of approval of each procurement step.

For such organizations, each company should decide how to approach these issues itself, for example:

1. By applying rules different from the standard procurement regulation allowing the subsidiary to apply them partially.

2. By waiving of the Procurement Regulation. However, it seems too risky since consistency of rules and regulations creates a more transparent procurement mechanism for holding management.

3. By developing a separate Procurement Regulation. This option is appropriate when internal regulations cannot be applied (for example, if the subsidiary is not a Russian resident), but control is still necessary.

However, if such procurement control measures inside an energy company are optional, and subsidiaries can operate independently of the parent company, then the laws stipulate mandatory forms of corporate governance to protect interests of the company owners. At the same time, inconsistencies arising out of application of the effective corporate legislation provisions and procurement laws should not be overlooked.

Thus, according to Federal Law No. 208-ФЗ on Joint-Stock Companies dated December 26, 1995 (hereinafter referred to as Federal Law No. 208-ФЗ) and Federal Law No. 14-ФЗ on Limited Liability Companies dated February 8, 1998 (hereinafter referred to as Federal Law No. 14-ФЗ), more significant transactions of the company (major transactions, interested party transactions) should be preliminarily approved by resolutions of the general meeting of members/general meeting of shareholders/board of directors (supervisory board) (hereinafter referred to as Company management bodies), which is necessary to control current business of the company and protect interests of its owners.

Failure to comply with these regulations entails a risk of these transactions invalidation. However, Federal Law No. 223-ФЗ along with Federal Law No. 135-ФЗ also oblige businesses to conduct bidding procedures for selection of suppliers before entering into a contract without limiting competition or creating advantages for specific suppliers. Failure to comply with these procurement regulations will not only invalidate the transaction, but risk administrative sanctions for the Company and/or its officials.

It raises the question of when to approve the transaction? Also, can the management body reject a contract to be entered into following the bidding? In fact, a situation can occur in a company when finalization of one contract can take six months or more, and the works (services) will be no longer needed or the Company will incur major financial losses due to long-term approval.

For instance, when consummating interested party transactions under Article 83 Clause 4 of Federal Law No. 208-ФЗ, the following algorithm applies:

The company establishes its needs in a procurement plan, then (if necessary) has them approved by the Federal Corporation for Small and Medium Business Development as part of the procurement plan, published the procurement plan, then conducts all bidding procedures and, if the successful bidder meets the criteria of an interested party, convenes a meeting of the company management bodies to approve an interested party transaction.

It is possible that officials within the management bodies are not members of procurement committees, and they can decide to reject this transaction. Thus, this decision can be deemed a market restriction, when a bidder is prevented from participation in the procurement. While, under Article 3.2 Clause15 of Federal Law No. 223-ФЗ, the Company is to finalize a contract in 10 days after publication of the final protocol drawn up following a specific procurement process in the unified information system (hereinafter referred to as the UIS). The contract should be entered into within 20 after the protocol is published or in 5 days from the date of transaction approval, if such approval is necessary.

However, in my view, this results in a situation when the Company has to enter into a contract not approved by the management bodies. Otherwise, the successful bidder will be entitled to file a claim to enforce a contract. It should be noted that the federal anti-trust authority and courts adopt a stance on mandatory execution of a contract following the procurement. [6]

Today, Federal Laws Nos. 14-ФЗ and 208-ФЗ state that absence of approval of such a transaction does not constitute sufficient grounds for its invalidation. Besides, I believe that Federal Law No. 223-ФЗ contains special regulations that should prevail in this case, while the decision to select the successful bidder is made collectively and its bid is deemed the best one based on objective circumstances and evaluation methods. However, we should consider the possibility to amend laws stating that transactions to be consummated under Federal Law No. 223-ФЗ in similar situations should not be approved by management bodies, or the information on transaction consummation should only serve as a notification.

A similar algorithm applies for major transactions (the transaction value is 25% of the balance sheet assets or more): A company establishes its needs in a procurement plan, publishes the procurement plan and conducts the necessary bidding procedures.

Then when is the expected transaction to be approved?

For approval of a major transaction according to the requirements of federal laws (e.g., Article 46 of Federal Law No. 14-ФЗ), the following details should be provided:

— Party to the transaction;

— Subject matter and material terms of the transaction;

— Contract price.

It makes sense for a major transaction to be approved when competitive bidding is competed and all contract terms and conditions are known. However, a major transaction can be preliminarily approved without specifying the contracting party, in which case the maximum rather than actual contract price will be stated. This helps expedite the contracting procedure and prevent situations when no contract is approved following the procurement procedures.

It should also be noted that Decree of the Government of the Russian Federation No. 2258-p dated November 6, 2015, on approval of the list of specific customers whose draft plans of procurement of goods, works, services, draft amendments to these plans are subject to evaluation for compliance with the Russian laws that require participation of small and medium business in procurement (hereinafter referred to as Decree 2258-p) by Joint-Stock Company Federal Corporation for Small and Medium Business Development prior to their approval. [7]

According to this Decree, the organizations listed in it are to have their procurement plans approved by the Federal Corporation for Small and Medium Business Development before publishing them. Today, this helps energy companies ensure execution of the number of contracts with small and medium businesses required by the Decree of the Government of the Russian Federation No. 1352 dated December 11, 2014, on approval of the Regulation Aspects of Participation of Small and Medium Businesses in Procurement of Goods, Works, Services by Specific Types of Legal Entities, Annual Procurement Volume and Volume Calculation Procedure (hereinafter referred to as Decree of the Government of the Russian Federation No. 1352 dated December 11, 2014).

Additionally, for the purpose of procurement control, Article 4 of Federal Law No. 223-ФЗ obliges energy companies to post the procurement regulation, plan and information in the unified information system (hereinafter referred to as the UIS). Furthermore, based on the said law, the customer shall publish information on the contracts entered into, amendments and contract implementation in the UIS register of contracts along with the notice of procurement.

The law stipulates certain exceptions for minor procurement and procurements containing state secrets. Article 4 Clause 15 of Federal Law No. 223-ФЗ states that the customer may not post information on procurements exceeding 100 thousand Russian rubles (for companies with the annual revenue under 5 billion Russian rubles) or 500 thousand Russian rubles (for companies with the annual revenue over 5 billion Russian rubles); financial transactions for raising deposits, etc.; as well as procurements that involve transferring the right to own and/or use real estate. Article 4 Clause 5 of Federal Law No. 223-ФЗ contains another exception negating the need to publish a notice of procurement from a single supplier (executor, contractor).

It should be noted that any failure to post the information to be posted in the UIS is a violation under Clause 7.32.3 of the Code of Administrative Offenses and entails imposition of a fine on the organization and/or officials.

This form of control over activities of energy companies is highly controversial. Currently, there is much concern about the need to make this information public. As contracts to be entered into by companies are in fact information about its business,

branches, facilities under construction/repair, services rendered, etc., which can be associated with not only financial risks, but also issues of security of an unlimited number of parties. We must remember that major energy companies often serve hazardous or important social facilities.

As mentioned above, Article 4 Clause 5 of Federal Law No. 223-ФЗ says that the notice of single-source procurement is unnecessary; however, this regulation is somewhat contrary to Decree of the Government of the Russian Federation No. 1352 dated December 11, 2014.

For instance, as per Clause 20 of Decree of the Government of the Russian Federation No. 1352 dated December 11, 2014, procurements from small and medium businesses can be considered when calculating 18% of the total annual volume of procurements from small and medium businesses to be performed under the draft procurement plan as long as the procurement notice and documents state that only small and medium businesses can take part in the procurement. This is without exceptions to the general rule.

In fact, when the customer specifies procurement amounting to 18% of the total annual volume of procurements from small and medium businesses, it has to publish a notice of procurement, including single-source procurement. This requirement is in fact superfluous.

Of course, elimination of the obligation to publish a notice of single-source procurement from small and medium businesses will not solve the information disclosure issue, but can potentially reduce the burden of energy companies in terms of additional operations.

Summarizing the above, control is a very important part of corporate governance allowing company owners and management bodies to take timely measures to prevent risks and minimize losses. State control ensures protection of public interests, as well as those of all stakeholders involved in activities of energy companies.

However, one has to remember that too many agreement and approval procedures deprives the company of "mobility" when making decisions and responding to ever-changing market conditions. This, in its turn, decreases companies' competitive performance on both internal and external markets.

While adopting new control regulations, the existing regulations are to be reviewed promptly. Thus, if a collegiate body makes decisions on transactions, it seems more reasonable to require approval of such transactions by the company management bodies and disclose information on a notification basis.

The approach to information transparency should also be changed towards milder regulation. Evidently, state bodies should have access to information needed to control compliance with the current laws on procurement. However, the issue of third party access to this information remains controversial. If a procurement party believes its rights to be violated, it may file a complaint with a state authority requesting it to verify lawfulness of certain procedures. It should be noted that this right is currently extensively exercised by all parties to the procurement activities. Therefore, interests of procurement stakeholders can be protected while maintaining activities of energy companies confidential. ■

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