
The Formation of Authorized Capital in Economic Organizations

Tatyana A. Skvortsova¹, Yuriy A. Kolesnikov², Tatyana A. Mosienko³,
Nikolay G. Romanenko⁴

Corresponding author: T. A. Skvortsova Assoc. Prof., Ph.D. of Law, Rostov State University of Economics, 69, Bolshaya Sadovaya str., Rostov-on-Don, 344002, Rostov-on-Don, Russian Federation, tel. +78632635708, e-mail: tas242@yandex.ru

Abstract:

The aim of the study is to investigate the sense and order of formation of authorized capital in economic organizations within the context of modern Russia. Throughout the research conducted, authors analyze the legal nature of authorized capital of economic organizations and the order of authorized capital formation amongst the organizations with limited liability, as well as joint-stock companies in Russia.

As a result, authors conclude, that as authorized capital represents a minimal scale of possessions, guaranteeing the interests from agricultural creditors; there is a need for a step-by-step implementation of «hard» authorized capital concept in the Russian legislation, as well as expansion of minimal requirement for authorized capital for Russian limited liability organizations as well as joint-stock companies.

On the basis of the research conducted, authors propose recommendation, regarding the improvements of current Russian legislation regarding the order of authorized capital formation within economic organizations.

Keywords: agricultural community, authorized capital, formation of authorized capital, minimal authorized capital requirements.

¹ Assoc. Prof., Ph.D. of Law, Rostov State University of Economics, Rostov-on-Don, Russian Federation.

² Doctor of Legal Sciences, associate Professor, Department of Law, Southern Federal University; Member of the Expert Council of the Committee of the State Duma of the Russian Federation on financial market, Rostov-on-Don, Russian Federation.

³ Assoc. Prof., Ph.D. of Law, Rostov State University of Economics, Rostov-on-Don, Russian Federation.

⁴ Assoc. Prof., Ph.D. of Law, Rostov State University of Economics, Rostov-on-Don, Russian Federation.

Introduction

The conceptual basis of the legislative system of economic organizations is presented in the form of requirements regarding authorized capital within such organizations, which is assumed to be the minimal property basis for the organization's activity, guaranteeing the interests from creditors.

Moreover, authorized capital, its function in the process of establishment of economic organizations, and its size - are one the problematic areas in the current legal framework. The problems of the legal framework regarding the authorized capital are pointed out by a number of authors, including (Makarova, 2010). Among the main problems - the question regarding the necessity, size and composition of authorized capital in economic organizations. The problems of legal nature and legal regime of shares within the authorized capital are also out for discussion.

Therefore the relevance of the topic under discussion is explained by the following: important role of authorized capital in the process of formation of economic organizations property; discussion nature of theoretical basis within the structure of authorized capital, shares in authorized capital and others; imperfections of legislative basis that constitutes the legal regime of authorized capital of economic organizations.

Real research is emerging from the hypothesis stating the need for improvement of the current authorized capital concept in the Russian Federation and changes in the current Russian legislation in the mentioned sphere. The study aims, to investigate the point of the matter and the order of formation of authorized capital in the context of current Russian legislation. In order to achieve the targets presented above, the following problems need to be resolved: to define the legal nature of authorized capital and shares in authorized capital, to consider the order of formation of authorized capital at the stage of agricultural community formation, and to establish the proposals to improve the acting Russian legislation.

As the subjects of the study, the authors consider communal relationships that occur during the process of authorized capital formation within the economic organizations in modern Russia. The subject of this study is civil-legal norms, forming the legal regime around the authorized capital of economic organizations, as well as its application practices.

Literature review

Economic literature points out the importance of economic organizations in the organizational structure of the economy (Ushakov and Shieh, 2013; Glavina, 2015), considering the investment attractiveness of communities as small business enterprises (Ermakova *et al.*, 2016; Bashamakov *et al.*, 2015; Arslan-Ayaydin *et al.*, 2014). It is pointed out, that the main reasoning behind the purchase of shares of the

authorized capital by investors is profit seeking, which means that a more effective system of asset management is needed (Xudaykulov, 2014; Lukasevicius and Lapinskaite, 2014).

Problems of legal regime regarding the authorized capital of economic organizations have been numerously brought up in civil literature. Authorized capital of a community - is a money equivalent of property value, which should have a legal party in the process of its establishment (not related to the objects included in its composition); the value of pure assets of the legal party should never be on a level lower than the authorized capital (Shapkina, 2001). Authorized capital represents the value (or money valuation) of property, invested by all the shareholders as a payment for the right to be part of the community. Hence the sum of authorized capital, stated in the communities' documentation - is a nominal, narrative number that only specifies the cumulative value of inputs made by the shareholders at the moment of joining (Shitkina, 2011; Nejad, 2014).

Authorized capital represents conditional measure that consists of value (money valuation) of shareholder inputs. At the moment of communities' establishment, all property consists of authorized capital, which formed from shareholder inputs. However, what happens in the future, is a sort of «separation» away from authorized capital, and its existence is only stated in the legal balance sheets, in the passive of which, the nominal values of authorized capital is reflected (Gutnikov, 2015; Macijauskas and Maditinos, 2014).

As a result of literature review, it can be concluded that the level of understanding of the problem is relatively high. Given this, there is a unified approach to deal with the legal nature of authorized capital. Furthermore, the majority of research considered a narrow set of objects (relationships) that related to authorized capital: legal nature of authorized capital and the shares in authorized capital, problems of formation of authorized capital and etc. Such approach doesn't allow to sufficiently investigating the given matter, which is a precondition for additional research of the given problems in this article.

Research methods

The methodology used authors is presented as all-round scientific methods of research - dialectical, systematic, sociological, as well as scientific methods - legal-comparative, historical, structural, functional, normative, logical, technical and linguistic.

Results

1. Characteristics of the legal nature of authorized capital in economic organizations

All economic communities (limited liability companies and joint-stock companies) are inter-connected by the presence of authorized capital that is divided proportionally to the stock. Modern Russian legislation doesn't contain the definition for «authorized capital», resulting in its legal nature not being properly defined. We suppose that the definition of authorized capital should be considered through defining its functions.

According to the commonly accepted expert opinion in the field of corporate right, authorized capital fulfills three main functions:

First function is basis (starting, funding provision), which is the fact, that the property inputs that happen at the establishment stage of any corporation. In case of authorized capital expansion, the funds can be used to accomplish the firm projects. Overall it is the idea of provision of funds/property to fulfill a risky venture, without responsibility before creditors, is the underlying basis of any joint-stock entrepreneurial activity. At the moment, the governments that lean toward the outsider model of conducting business, the possibility of funds attraction, via the process of issuing new equity stock is the basis for development of some companies and the country's economy as a whole. In the process of implementation of this function, the process of defining the minimal funding necessary for the start is solely defined private sector - government should be indifferent towards how much funding/property does an economic organization possess, what the organization wants to purchase using these resources and whether the resources are sufficient for successfully conducting business.

It is important to point out, that the starting function is fulfilled by assets, which have been transferred by the shareholders as a payment for the share of the authorized capital, and not the authorized capital itself (which is conditional). In this case scenario, there is place for the mix up of functions of authorized capital and the functions of assets of the organization. As a result, it is agreed that this function is not carried out by the authorized capital and physically cannot be carried out by authorized capital.

The second function, which is traditionally highlighted by the legal literature is the distributive function. Shares of stockholders are determined through authorized capital, which means that the size of equity stock is proportional to the volume of rights of a single participant. Furthermore, the size of authorized capital doesn't affect its distributive function - it is equally carried out, even if the size of authorized capital is 1 ruble (it defines proportions). The fact that authorized capital is needed to define the level of participation (as only authorized capital defines the shares of participants) cannot be argued with. Therefore it obviously possess the distributive function, however the function stated is not the main function allowing to define the legal nature of authorized capital in our opinion.

The third and the main function of authorized capital is the guarantee function - the only that is defined in the norms of Russian legislation, in part 1, p. 25 of the Federal Law of the Russian Federation «About Joint-Stock Companies», part 1 p. 14 of the Federal Law of the Russian Federation «About Limited Liability Organizations». Guarantee function, as commonly agreed, is the function, via which authorized capital defines the minimum assets value, necessary to keep the creditors interested. It is importance of the interest from creditors that dictates the proposal to increase the size of authorized capital (Skvortsova, 2013).

At the moment, the minimum authorized capital defined in the Russian legislation is not able to secure the interest of creditors of economic organizations. If we refer to experience of some of the European governments, that belong to the Roman-Germanic legal family, it is easy to observe a relatively high level of minimum authorized capital, which is significantly greater when compared to the minimum authorized capital in the Russian Federation. The table of comparison of authorized capital in Russia and Germany is presented in Figure 1.

Figure 1. Minimal size of authorized capital in Russian and European organizations

Type of Organization	Minimal authorized capital size		
	Russia	Germany	Switzerland
Limited Liability Company	10,000 RUB	25,000 EUR	20,000 CHF
Joint-Stock Company	10,000 RUB – Joint-Stock Company; 100,000 RUB – Public Joint-Stock Company	50,000 EUR	100,000 CHF

However the given stance is only supported by a few researchers. Thus, Fillipova (2012) relies on the fact, that the analysis of foreign corporate right doesn't provide evidence, necessary to make conclusions regarding the size of authorized capital. On the contrary, a reverse tendency is more likely, where a continuous decrease in the minimal level of authorized capital is observed, in order to provide for easier market entrance, as well as competition between legislation in different European governments (Dubrovitskaya, 2008).

In fact, France recently has abolished the requirements towards the minimal joint-stock capital in the SAS Corporation, and even Germany, the initiator of capital protection doctrine, has changed the law regarding private organizations with limited liability, softening the capital requirements for GmbH. It also introduced new type of private corporation *Unternehmersgesellschaft*, which is free of legal

requirements regarding the establishment of minimal joint-stock capital, related to GmbH (Goncharovm, 2011). Both French and German reforms, integrate the form of corporation that is totally free of minimal joint-stock capital requirements, which de facto constitutes: protection given to creditors via the basic joint-stock capital is an illusion. We suppose that in order to provide for real third party protection, authorized capital should be significant and adequate, in proportion to the financial responsibilities of the corporation. It is the guarantee function of the authorized capital, present in the legislation that can be supported through the real value of authorized capital of the organization.

Furthermore, the characteristic of authorized capital as a minimal asset size, that guarantees the interests of creditors, is in our opinion is the closest to the traditional continental model of economic organization, which the Russian legal framework is leaning towards. Therefore, we believe that the authorized capital of economic organization is a money measure that reflects the minimal asset size of the organization guaranteeing the interests of creditors, defined by the cumulative value of nominal shares of participants of the organization.

2. Analysis of the order of formation of the authorized capital in modern Russia

The order of formation of authorized capital is defined by the norms of the Civil Code of the Russian Federation, applicable to all society types and is detailed by the norms of special legislation. All the requirements that apply to the formation of authorized capital can be divided into three groups: quantitative, qualitative and processual. Detailed description of the following requirements is presented in the Figure 2.

Figure 2. Authorized Capital Requirements

Quantitative requirements	relate to the need to comply with the minimal authorized capital size
Qualitative requirements	establish that authorized capital must be formed only using defined assets
Procedure requirements	establish deadlines and the order of investing funds into the authorized capital, and the necessity to comply with anti-monopolistic regulations and etc.

While characterizing the quantitative requirements it should be pointed out, that the current issue of the Civil Code of the Russian Federation establishes the exhaustive range of assets that can form the authorized capital of economic organizations. Article 66.1 states that «investments by the economic organization member can be in the form of cash, property, shares in the authorized capital in other organizations

and state and municipal bonds. Furthermore, the investments subject to monetary valuation can be in the form of exclusive or other intellectual rights and license agreements».

Alongside, the articles of the legislative acts establish a wider variety of investment types that can be performed by participants in order to get hold of equity stock. Thus, Article 15 of the Federal Law of the Russian Federation «About the Organizations with Limited Liability» states: «Payment for the share in authorized capital can be in the form of cash, assets and other things, or property rights with any monetary value».

Similar statement is made in the Article 34 of the Federal Law of the Russian Federation «About Joint-Stock Organizations»: «Payment for shares, that are distributed amongst the participants of the organization during the process of establishment, additional shares, distributed via assignment, can be carried out through cash payments, securities and other valuables as well as property rights, or rights with any monetary value». Thus, there is a contradiction between norms in the Article 66.1 of the Civil Code of the Russian Federation regarding organizations with limited liability and joint-stock companies.

Given this, the statements in Article 66.1 determine possible limitations, for the types of property and assets included into the authorized capital, by the presence of federal laws. However nothing concerning the expansions of this range: «Laws or establishment documents of the economic organization can set out the types of property (explained in the 1st point of the Article), which can be used as a form of payment for the shares in the authorized capital of this economic organization».

We believe, that the statements in the Article 66.1 of the Civil Code of the Russian Federation, that establish the limitations regarding the property and assets used as payment for shares in the authorized capital, by enlarge satisfy the guarantee function of authorized capital explained in the legislation. Thus, Sukhanov (2002) has rightfully pointed out, that the opportunity of payment for the shares in authorized capital by virtually any type of asset/property will only lead to abuse. Besides, practice suggests, that norms establishing the size and order of authorized capital a normally avoided. This happens by investing highly non-liquid assets into the authorized capital that is hard to check (Rubeko, 2016). Such actions are normally performed in order to minimize investment responsibility of the shareholders. Given this, we can agree with Sukhanov (2002), that economic risk doesn't disappear, as it is simply being transferred onto the other parties, such as consumers. Therefore we are talking about breaching the key principal of civil rights the honesty of parties of civil interactions.

Following the above mentioned conclusions, we suppose that it is necessary to activate the Article 15 of the Federal Law of the Russian Federation «About organizations with limited liability» and Article 34 of the Federal Law of the

Russian Federation «About Joint-Stock Companies», with regard to the statements in the Article 66.1 of the Civil Code of the Russian Federation. This requires Article 15 and Article 34 specification, regarding the range of property and assets authorized by the Civil Code of the Russian Federation.

Monetary valuation of the property, used as payment for the share in authorized capital is decided by the members of the organization. At the moment, Article 66.2 of the Civil Code of the Russian Federation sets out a statement regarding the fact that «monetary evaluation of non-monetary investment into the authorized capital, should be carried out by an independent body. Members of the economic organization have no competence to evaluate the non-monetary investment above the number provided by the independent body». This article of the Civil Code of the Russian Federation allows for responsibility of the independent body, in case of over-valuation of property. In case of insufficient property/assets they bear subsidiary responsibility within the limits of the sum of overvaluation (for 5 years).

There are also contradictions with the Federal Law «About Limited Liability Companies», as the norms set out in the Article 15 of the given normative act establish the necessity to attract the independent body, only in case of «nominal value or increase in nominal value of the share in authorized capital, is greater than 20 thousand doubles».

Given this, the modern research contains proposals regarding both, the need to carry out independent valuation of market price of the assets regardless of the price (Kasianov, 2011), and the irrelevance of such independent valuation, as it will lead to unjustified time and financial costs (Kopilkova, 2014).

We believe, that in the given case, the norm of the Article 66.2 of the Civil Code of the Russian Federation are applicable, as it possesses the highest legal power. It is also necessary to involve the Article 15 of the Federal Law with regard to the Article 66.2, notable in the area of the need for independent valuation. Thus, the analysis of the order of formation of authorized capital has shown the need to attract special legislation in the sphere of investigation, with accordance to common statements of the Civil Code of the Russian Federation.

Discussion

Results of the study, show the need for the realization of the concepts of «hard» authorized capital to support the guarantee function of authorized capital, in accordance to the norms of modern legislation, which explains the need to increase the size of minimal authorized capital for Russian limited liability and joint-stock companies, up to the level of minimal authorized capital in European organizations. It is also necessary to the point out the need for a more narrow procedure of authorized capital formation in Russian economic organization. This is required in

order to provide guarantees for the shareholders, and as a result, guarantees for the creditors.

Conclusion

The results of the study have shown the importance of the role of authorized capital of economic organizations in providing guarantees for the interests of participants and creditors of economic organizations. For future improvements of legal regulations of authorized capital in economic organizations in Russia, we propose the following:

Firstly, in order to create an effective system of guarantees of creditor rights and to discourage the emergence of «one-day firms» it is necessary to increase the minimal size of authorized capital up to the level in European organizations. This will allow implementing the concept of «hard» authorized capital in Russian economic organizations, which is traditional for the countries with continental system of rights that Russia is leaning towards.

Secondly, it is necessary to create a definite and transparent system of legal order of formation of authorized capital of economic organizations and integration of norms of special legislation regarding economic organizations in accordance to the norms of the Russian Civil Code. This will give an opportunity for the shareholders to comply with the order of formation of authorized capital, which will eventually improve the guarantees of counteragents and creditor rights protection.

References

- Arslan-Ayaydin, O.D. Barnum, M.B. Karan and Ozdemir, H.A. 2014. How is Moral Hazard Related to Financing R&D and Innovation. *European Research Studies Journal*, 17(4), 111-132.
- Bashmakov, A.I., Popov, V.V., Zhedyaevskii, N.D., Chikichev, N.D. and Voyakin, A.E. 2015. Generic Heurorithm of Innovation Management from Generating Ideas to Commercialization. *European Research Studies Journal*, 18(4), 47 -56.
- Civil Code of the RF (part 1). 1994. № 51-FL (changes as of 03.07.2016) // Collection of the RF Legislation, № 32, p. 3301.
- Ermakova, A.N., Vaytsekhovskaya, S.S., Malitskaya, V.B., Prodanova, N.A. 2016. Investment attractiveness of small innovational business under the conditions of globalization and integration. *European Research Studies Journal*, 19(2), Special Issue, 258-267.
- Federal Law of the RF «About limited liability companies». 1998. № 14-FL, Collection of the RF Legislation, № 7. p. 785.
- Federal Law of the RF «About Joint-Stock Companies». 1995. № 208-FL, Collection of the RF Legislation, № 1. p. 1.
- Fillipova, S.Y. 2012. About Functions of Authorized Capital in the Context of Evaluation of Legislation in Economic Organizations // *Entrepreneurship Rights*, № 1, 19-22.
- Glavina, S. 2015. Influence of Globalization on the Regional Capital Markets and

- Consequences; Evidence from Warsaw Stock Exchange. *European Research Studies Journal*, 18(2), 117-134.
- Goncharov, A. 2011. Denmark Capital Protection Doctrine // *EJ – Lawyer*, № 16, 1-5.
- Gutnikov, O.V. 2015. Legal Parties Types in Russian Civil Right // *Legal Parties in the Russian Civil Right: Monography. Types of Legal Parties in the Russian Legislation / response from A.V. Gabo*, p. 352.
- Dubrovitskaya, E. 2008. *European Corporate Right*. - Wolters Clover, p. 226.
- Kasianov, A.S. 2011. *Methods of Exclusive Rights Management: auto reference dissertation, PhD in Law science*, p. 34.
- Kopilikova, N.M. 2014. *Ways of Exclusive Rights Management // Culture: Management, Economy, Rights*, № 2. p. 7-11.
- Lukasevicius, A. and Lapinskaite, I. 2014. *Strategy of Sustainable Development in Investment Portfolio Case*. *European Research Studies Journal*, 17(4), 3-18.
- Macijauskas, L. and Maditinos, I.D. 2014. *Looking for Synergy with Momentum in Main Asset Classes*. *European Research Studies Journal*, 17(3), 3-16.
- Makarova, O.A. 2010. *Corporate Right: Lecture Course - Wolters Clover*, p. 420.
- Nejad, K.M. 2014. *Clustering Stock Exchange data by Using Evolutionary Algorithms for Portfolio Management*. *European Research Studies Journal*, 17(4), 55-66.
- Rubenko, G.L. 2016. *Authorized Capital of Economic Organizations: Problems of Legal Regulation // Lawyer*, № 10, 28-32.
- Sayapina, I.A. 2005. *Functions and Structure of Authorized Capital on Limited Liability Companies // Right and Politics*, № 6, 13-18.
- Shitkina, S.I. 2011. *Corporate Right: introductory course / Cnorus*, p. 1072.
- Skvortsova, T.A. 2013. *The state, corporation and individual: correlation of rights, economic interests and ways of their realization: Peer-reviewed materials digest (collective monograph) published following the results of the LXV International Research and Practice Conference and the III stage of the Championship in Economic Sciences and Management, Juridical Sciences, London: IASHE*, 67-69.
- Sukhanov, E.A. 2002. *Problems of Legislative Development in Commercial Organizations // Economy and Right*, № 5, 50-59.
- Sukhanov, E.A. 2014. *Comparative Corporate Right. Statute*, p. 456.
- Shapkina, G.S. 2001. *New Changes in Joint-Stock Legislation (changes and additions to the Federal Law «About Joint-Stock Companies»)*. *Authorized Capital // Newsletter VAS RF*, № 12, 102-103.
- Theriou, G.N. 2015. *Strategic Management Process and the Importance of Structured Formality, Financial and Non-Financial Information*. *European Research Studies Journal*, 18(2), 3-28.
- Ushakov, D., Shieh, C.J. 2013. *Modern innovative entrepreneurship: economic efficiency and organizational structure*, № 3, 38-46.
- Xudaykulov, M. 2014. *The principles of forming management in joint-stock companies // Eastern European Scientific Journal*, № 3, 80-82.