

# Reform of participation in shared construction as a condition for urban development

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**Abstract.** The article deals with the issues of reforming the institution of shared construction. The relevance of the research topic is determined, firstly, by the special social role of the institution of shared construction in providing citizens with housing, and secondly, by the currently implemented large-scale reform of this institution, requiring systematic scientific reflection. The reasons for appearance and main directions of development of this institution from the moment of its appearance, its influence on the realization of the constitutional rights of citizens are shown. The ambiguity of the legal qualification of this treaty is noted as one of the causes of problems in law enforcement practice. An important area of research is analysis of regulatory framework for reform of institution of participation in shared construction and related (providing) economic and legal institutions (deposit insurance system, escrow agreement, etc.). The legal regulation of contractual basis of the formed project financing system is subject to the detailed analysis. The study allows formulating a number of conclusions about the role of reform of shared construction in the development of cities.

## 1 Introduction

The issue of providing citizens with housing has always been very acute both in the USSR and in modern Russia. According to the Federal State Statistics Service, the number of families registered as needing residential premises in 2000 was 5,419,000, in 2010 - 2,821,000, in 2015 - 2,612,000 [1]. These figures indicate that even with positive dynamics in solving the problem of providing citizens with housing, it remains relevant for a significant number of citizens.

In the context of transition to the market-based business model, the need arose to search for new legal forms of providing citizens with housing. The lack of experience in regulating such issues in the market conditions did not allow for the adaptation of classic contractual models (purchase and sale, contract, simple partnership agreement). In the early 2000s, with a view to activating housing construction and solving the problems of providing

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citizens with housing, Federal Law No. 214 was adopted (hereinafter also the law on shared construction), securing a new named type of contract - an agreement on participation in shared construction. The controversial history of this institution forced the highest state authorities of the Russian Federation to initiate a large-scale reform of participatory construction, with the stated goal of moving to a system of project financing. Such cardinal changes in a very sensitive sector of the economy undoubtedly require scientific study by methods of various branches of knowledge.

The purpose of the study is to provide scientific understanding of the main directions of reform of legislation on participation in shared construction, assessing its role in sustainable urban development. To achieve this goal, the following research objectives are formulated: to reveal the nature of the relationship of participation in shared construction; to compile statistics on the number of concluded contracts for participation in shared construction; to analyze the current regulatory framework and acts of interpretation of law; to determine the main directions of the reform of participation in shared construction; to highlight expected positive results of the reform and possible risks in its implementation; to determine the role of the reform in sustainable urban development.

The scientific novelty of the study consists in a comprehensive study of the institution of participation in shared construction and related (providing) economic and legal institutions (deposit insurance system, escrow agreement, etc.) during the period of reforming legislation.

## **2 Review of research literature**

The issues studied in this article regarding the qualification of contract for participation in the shared construction were considered in the works of R. S. Bevzenko, K. I. Sklovsky, A. A. Makovskaya, E. V. Reztsova, I. I. Kharitoshin and other authors. They have expressed different views on the legal nature of this treaty. On the subject of the reform of institution of shared construction and its influence on development of the housing market and, as a consequence, on development of cities, O.V. Teveleva, A.R. Kirsanov, T.I. Kubasova, Yu. E.Ostryakova discussed in the literature. In accordance with the stated objectives of the study, doctrinal assessment of the institution of shared construction is a direct subject of study; therefore, the positions of individual authors are disclosed in sections of the article “Results” and “Discussion”:

## **3 Methods**

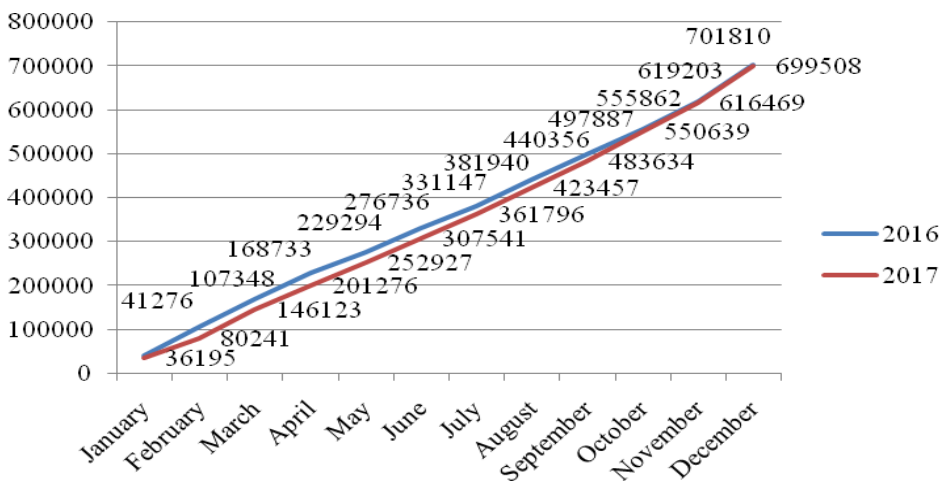
The study is based on the traditional domestic theory of scientific methods and methods of legal research in the interpretations of G.P. Schedrovitsky, D.A. Kerimov, V.M. Raw, S.S. Alekseev, A.F. Cherdantsev and other representatives of Russian and Soviet philosophy and theory of law. The following scientific methods were used in the work: formal-logical method of interpreting law, method of system analysis, method of legal forecasting, and certain elements of historical-legal method of research. The formal-logical method of interpreting law as the main method of legal research is based on the textual nature of legal norms. The use of traditional methods of interpretation of legal texts (grammatical, systematic, historical-political, genetic, teleological, etc.) will allow comprehensive analysis of legal texts involved in the study, identify contradictions between the norms, ambiguous meanings of the terms used, make recommendations for improvement of current regulatory framework. Application of this method will allow analyzing regulatory legal acts governing participation in shared construction. System analysis method in relation to the legal side of participation in shared construction will

allow, on the one hand, to consider it as a system consisting of elements, and to reveal their influence on qualities of the whole, on the other hand, to see contract of participation in shared construction in the system of other legal phenomena, to describe their relationship. Method of legal forecasting will make it possible to formulate scientifically based assumptions about development of institution of participation in shared construction to the general scenarios version of this method. The study also uses elements of historical and legal research method in form of concrete historical research method, expressed in fixing individual events and facts in development of the research object.

Empirical basis of the work includes current legislation and established judicial practice. Statistics of the Rosreestr on the number of concluded share participation agreements in construction has been studied. Analysis of economic consequences of the realization of amendments to the current Federal Law No. 214 "On participation in the shared construction of apartment buildings and other real estate objects and on amendments to some legislative acts of the Russian Federation", as well as the order of the Ministry of Construction of the Russian Federation No. 560 "On the approval of criteria the attribution of citizens whose money was attracted for the construction of apartment buildings and whose rights were violated, among affected citizens and the rules for maintaining register of affected citizens "and the resolution of the Plenum a SAC RF No. 54 "On some issues of resolving disputes arising from contracts about real estate".

## 4 Results

With all the ambiguity of legal qualification of this contract, it initially possessed indisputable advantages in the form of a rigid connection of supply and demand at the initial stage of construction, which avoided the risk of overproduction and the impossibility of selling finished housing, a much more affordable price of the property at the start of construction (the so-called "stage of the pit"), the possibility of a phased payment of housing under construction. The attractiveness of the equity construction mechanism is also obvious to the developer: the funds raised by the interest holders are free, unlike bank financing, which you must always pay for.



**Fig. 1.** Dynamics of changes in the number of registered contracts in the Russian Federation

According to Rosreestr, in 2016, the service registered 701,810 contracts of participation in shared construction, in 2017 - 699,508. This is 0.3% less than the same indicator of 2016 (701,810 registrations of the contracts). Compared to the same period of 2015, the number of contracts increased by 3.0% (then 679,197 contracts were registered).

At the same time, implementation of the shared construction mechanism in Russian reality almost immediately gave rise to a number of serious problems, summarized under the capacious name of the problem of “deceived co-investors”. At the level of regulatory and legal consolidation, this status is referred to as “affected citizens”, which recognition requires submission of application and compliance with the criteria established by the Ministry of Construction in order No. 560.

Analysis of law enforcement practice shows that the most common problems associated with implementation of the contract for participation in shared construction were, firstly, builder’s bankruptcy, and secondly, unscrupulous actions on his part, when construction is either not conducted or is conducted with significant violation of requirements for quality, time and other parameters. The cases of conclusion of more than one contracts of participation in shared construction in relation to one room with different persons are described. Since the victims in such cases are citizens who satisfy their housing needs, the problems of deceived real estate investors have special social significance.

The need for systemic reform of legislation on shared construction was noted in the program documents of the President of Russia. On November 5, 2017, list of instructions from the President of the Russian Federation was approved following by meeting with members of the Government on improving participation in shared construction. Among these instructions is the need to develop an action plan (roadmap) for phased replacement of citizens' funds attracted to create apartment buildings and other real estate, bank lending and other forms of financing that minimize the risks for citizens in terms of three years. This action plan was approved on December 21, 2017, it establishes a programmatic vision of new target model for financing housing construction, as well as stages of reforming the legislation on shared construction.

The target model for financing housing construction suggests different ideology of relations between developer and participant in shared construction. As it was shown earlier in this article, one of the causes of the system problem of “defrauded real estate investors” is the receipt of funds by participants in shared construction into the ownership of the developer at the initial stage of construction. The reform involves concentration of funds of participants in shared construction on escrow accounts or other special accounts, access to these accounts appear to the developer no earlier than the circumstances specified in clause 6 of article. 15.5 of the law on shared construction (putting an apartment building into operation, state registration of property rights in respect of single shared construction object included in apartment building, or placing this information in a single information system for housing construction).

Implementation of new model of participation in shared construction takes place in three stages: preparatory (from 12/21/2017 to 30.06.2018), transitional (from 1.07.2018 to 30.06.2019) and final (from 1.07.2019 on December 31, 2019).

In course of the already completed preparatory stage, significant updating of regulatory framework was carried out.

At the second stage (it continues at the time of this writing), structuring of relations between developer and participant in shared construction is possible both using escrow accounts and using so-called “Bank escort”, by opening a bank account for settlements on each building permit.

Serious guarantee of the rights of participants in shared construction is introduction of the rule on subsidiary liability of persons who actually have ability to determine actions of developer (including beneficial owners) for damages caused by their fault to citizens

participating in shared construction (clause 4 of Article 23.2 of the law on shared construction).

In addition to these changes, concerning regulation of actual contract of participation in shared construction, related legislation has also been substantially updated.

## 5 Discussion

Legislation on participation in shared construction contains currently a number of not entirely successful formulations, and judicial practice on certain disputed issues is still controversial. At one time (prior to introduction of the law on participation in shared construction), judicial practice considered the contract of participation in shared construction as a work agreement that obliged to create and transfer property to the ownership of counterparty. In the legal literature there are various arguments against such qualifications, for example, a participant in shared construction does not have the powers that customer has under construction contract (the right to assign tasks to the contractor, monitor construction progress, etc.), the interest holder is not burdened characteristic for the customer (provision of construction materials, provision of necessary services to the contractor, etc.) (EA Sukhanov, N.K. Evstratova). The main qualifying sign of a contract for participation in shared construction is its subject - a part of a building that cannot physically be created as an independent object (residential or non-residential premises in a house can be built only during the construction of the house as a whole), while under the construction contract the contractor undertakes construct a specific object on the instructions of the customer (and not a separate part of it) (E.I. Voinitskaya).

Some authors attributed the contract of participation in shared construction to an investment contract, and the contract price transferred to the developer was defined as the amount of investment. The study of delimitation of the contract of participation in shared construction and investment agreement was dealt with by A.G. Kuzenkov. According to his study, these types of contracts can be attributed to two independent types of civil law contract.

To the most correct qualification of the contract of participation in shared construction can be attributed the contract of sale of the future real estate. (R.S. Bevzenko).

In science, very cautious views are expressed regarding the success of the reforms being implemented. The forecasted reasons for worsening situation in the housing market, such as the need to replenish working capital due to stricter requirements for developers (and as a result, development of gray schemes), as well as unresolved question of sufficiency of money in the banking system to finance housing construction (O V. Teveleva); unsystematic nature of new stringent requirements for developers (A. R. Kirsanov); weaker competition and monopolization in the field of housing construction (T.I. Kubasova).

The doctrine also presents positive assessment of the reform of shared construction, with an emphasis on the targeting nature of funding; significant risk reduction; control of banks over construction stages (Yu. E. Ostryakova), and possibility of using alternative methods of housing financing (building savings banks, issuing one-tranche housing bonds, etc.) was justified (T. V. Svetnik).

## 6 Conclusion

One of the most important elements of shared construction system is escrow account. The emergence of escrow accounts in the Russian legal reality is connected with the entry into force of Federal Law No. 212, which added paragraph 3 to Chapter 45 of the Civil Code of the Russian Federation, containing four articles that reinforce the basis for legal

regulation of escrow accounts. The complexity of emergence of this legal structure is not included in the subject of this study; they are disclosed in more detail in specialized publications. Features of the opening, maintenance and closure of escrow accounts for settlements under contract for participation in shared construction are established by Art. 15.5 of the law on shared construction.

Since banks become one of the central subjects in new project financing scheme, legislator had to resolve the issue of guarantees to participant in shared construction in the case of problems with solvency of this group of subjects. One of the main institutions that ensure citizens' confidence in banking sector of the economy is deposit insurance system. As known, the total limit of compensation for deposits of individuals in banks is set at one million four hundred thousand rubles. The price of real estate in most cases exceeds this limit, therefore, as part of the ongoing reform, it was necessary to create special rules for insuring funds placed on an escrow account that is open for settlements under contract for participation in shared construction. These new rules were enshrined in Federal Law No. 175, where the central one is to increase the maximum amount of compensation under such escrow agreements to ten million rubles.

During the final stage of the reform, there will be final transition to the use of escrow accounts when attracting funds from participants in shared construction for construction of property.

Thus, it can be stated that as a result of the systemic reform of civil legislation, the foundations of regulatory framework for transition to the model of project construction financing have been formed. The use of escrow accounts (in conjunction with changed rules of deposit insurance system) makes it possible to fundamentally solve the problem of security of interests of citizens participating.

We believe that the fears of opponents of the reform are partly justified, in particular, in assessments of upcoming rise in housing prices for final consumers. At the same time, ideology of currently implemented reform is primarily aimed at protecting interests of the weakest side of participants in the housing construction process - citizens in need of housing. On the other hand, the reform brings housing construction processes in line with generally accepted international standards, using the latest legal designs. Civilized housing market is a necessary strategic condition for sustainable development of Russian cities.

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