



nektorov, saveliev  
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# **Subsidiary Liability as a Nuclear Weapon of Russian Bankruptcy Law**

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### Definition and the principal difference from the joint liability

Subsidiary liability is the civil responsibility which is borne by an additional debtor for the principal debtor (in German: hilfsweise Haftung)

<b>Joint liability</b> 	<b>Subsidiary liability</b> 
there are multiple debtors	
The creditor can choose which of the debtors to sue first, or to sue all of them concurrently	The creditor must first sue the principal debtor and – if he fails – the subsidiary debtor.

### When can a subsidiary debtor be sued?



- ❖ if the principal debtor refused to satisfy the claim; or
- ❖ If the creditor did not receive a response from the principal debtor within a reasonable period of time.



### Essence of the subsidiary liability



- ❖ compensatory function for the creditors in the event of failure to fulfill their claims
- ❖ prevention of abuses aimed at causing losses to creditors by the company's members
- ❖ restoration of the obligations breached by the principal debtor



	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020 (until June)</b>
Claims submitted	3652	5107	6103	3035
%	39,5%	54,2%	56,9%	31%
Claims satisfied	1440	2767	3472	942
Amounts awarded, in RUB	103,2 bln.	330,3 bln.	440,5 bln.	136,7 bln.

### Who is the controlling person?



ability to influence the  
company



the period of having influence the company - no  
more than 3 years prior to / after the occurrence  
of features of bankruptcy, but before the court  
accepted the application for bankruptcy

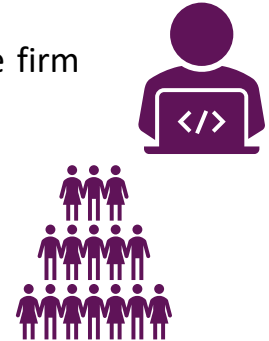


## CONCEPT OF CONTROLLING PERSON




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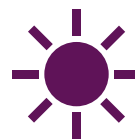
### Ability to influence the company

- ❖ a relative of the director or board member of the debtor company;
- ❖ a boss to the debtor company's director (e.g. the director is also the chief accountant of the firm headed by that person);
- ❖ Right to carry out transactions on behalf of the debtor company;
- ❖ Holding a key position in the debtor company (e.g. chief accountant, financial director or etc.);
- ❖ Being able to otherwise influence the debtor company's actions, including forcing the director to give certain instructions.



### 3 types of persons presumed to be controlling persons

<b>Directors</b> 	<b>Shareholders</b> 	<b>Beneficiaries from illegal conduct</b> 
<ul style="list-style-type: none"><li>❖ CEO</li><li>❖ Management company</li><li>❖ Member of executive body</li><li>❖ Liquidator</li><li>❖ Member of liquidation commission</li></ul>	<ul style="list-style-type: none"><li>❖ May dispose of 50 % shares</li><li>❖ Has more than half of charter capital</li><li>❖ more than half of the votes in the general meeting of participants</li><li>❖ the right to appoint (elect) the CEO</li></ul>	<ul style="list-style-type: none"><li>❖ Benefited from illegal or unfair conduct of persons specified in Article 53.1 para. 1 CC RF (person authorized to act on behalf of the entity)</li></ul>



### Pugachev Case

Facts confirming the status:

- ❖ Pugachev was a member of the Federation Council – the upper house of the Russian parliament. Concurrently, he held an office at the MezhpromBank;
- ❖ He conducted interviews with job applicants;
- ❖ He approved bonuses for bank employees;
- ❖ He participated in negotiations on behalf of the bank;
- ❖ He gave instructions (which were followed) to the bank's corporate governance bodies and structural subdivisions; and
- ❖ He stamped “approved” on documents which were subsequently actioned





## FACTUAL CONTROL OVER THE DEBTOR (COURT PRACTICE)

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### Maximov Case

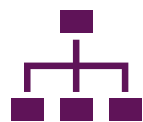
Evidence applied:



**Witness statements**



**Data from corporate information system**



**Holding structure of the group**

**Ability to give informal binding instructions**

## EXTRAORDINARY CASES OF BRINGING TO SUBSIDIARY LIABILITY (1)

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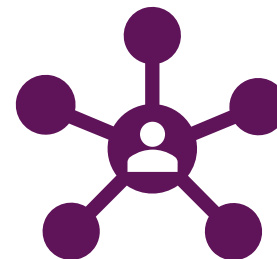
### Track Case – controlling relatives

Circumstances:

- ❖ Persons were relatives or kins;
- ❖ Deal was concluded between the Debtor and OOO SK Liga: delivery of goods (price per contract: 34 million RUB), the value of which was actually equal to 1.3 billion RUB;

Reasoning and findings of the court:

- ❖ Divorce itself has no legal significance for determining of affiliation and interest;
- ❖ the chosen model of behavior differs from the behavior of ordinary persons in commercial activity;
- ❖ The scheme is built on a trust relationship that excludes elements of entrepreneurial risk;
- ❖ The main purpose – the extraction of "family" income from the activities of the debtor.

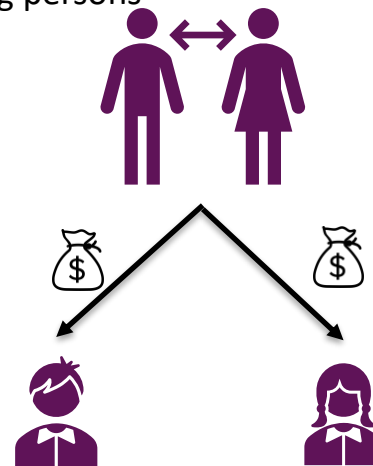


### Alliance Case – controlling minors

Circumstances:

- ❖ Parents were found to be controlling persons;
- ❖ They have donated to their children (one of which were a minor) expensive property by making gift agreements;
- ❖ Supreme Court (SC) at first stated: there is no evidence that children are controlling persons; rather, they were used by parents as instruments of hiding property. SC remanded the case to the first instance court.

Controlling persons



**Can a minor be brought to subsidiary liability?**

Ruling of the Supreme Court of the Russian Federation dated 23 December 2019 in case No. A40-131425/2016, Ruling of the Arbitrazh Court of city of Moscow dated 27 October 2020 in case No. № A40-131425/16-30-203B

## GROUNDS FOR BRINGING TO SUBSIDIARY LIABILITY

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❖ Transactions have caused proprietary damage to creditors



❖ Loss of accounting and (or) reporting documentation, distortion, and inaccuracy of information



❖ Offenses entailed criminal, administrative or tax liability of the debtor or its directors and officers



❖ Loss of constituent and other documents of the company



## GROUNDS FOR BRINGING TO SUBSIDIARY LIABILITY (2)

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❖ Failure to enter information on the facts of activities of legal entities in state registers



❖ Failure to submit (late submission) of the debtor's application to declare itself bankrupt to the court



❖ Actions (inaction) that significantly worsened the financial situation of the debtor after the onset of the objective bankruptcy



### Factors to be considered by the court



- ❖ Ground(s) for bringing the controlling person to subsidiary liability
- ❖ Number of controlling persons
- ❖ The degree of mens rea of each controlling person
- ❖ Degree of real damages suffered by creditors

### Burden of proof

#### Who?



- Insolvency manager
- Creditors

#### What shall be demonstrated?

- (i) the person to be held liable has the status of a controlling person and
- (ii) the creditors' claims may not be satisfied as a result of the controlling person's actions (inaction)

## CONSEQUENCES OF BRINGING TO SUBSIDIARY LIABILITY

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### Petition for personal bankruptcy

General rule: after the settlements with creditors are completed, a bankrupt natural person **is released** from further satisfaction of creditors' claims, including those that were not declared during the restructuring of such person's debts or the sale of property

### Subsidiary liability

Personal bankruptcy does not release the person from subsidiary liability.



## Контакты

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