

## СРАВНИТЕЛЬНОЕ ПРАВО

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**Single point of entry doctrine in the United States as a form of corporate liability: Possibilities of legal adoption in the Russian Federation***R. R. Kobenia*

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The article analyzes various aspects of the single point of entry bank resolution strategy in the United States and seeks to determine the viability of legally adopting this approach in the Russian Federation. The single point of entry strategy provides an alternative to “bailing out” large bank groups and bankruptcy proceedings via controlled liquidation of the parent company with simultaneous financial rehabilitation of the subsidiary bank. Orderly Liquidation Authority detailed by Title II of the Dodd-Frank Act provides a legislative framework for the single point of entry strategy, but due to the doctrine only existing as a guideline and not directly regulated by legislation, there are several gaps in legislation that cause various problems in both the practical implementation of the single point of entry doctrine and its scientific evaluation. The insufficiently studied topic of single point of entry doctrine as a form of corporate liability is also examined in the article. Russian legislation and court practices regarding bank rehabilitation and the doctrine of “piercing the corporate veil” are examined to determine the possibility of legally adopting the single point of entry doctrine due to similarities between doctrines. The flaws and merits of the single point of entry doctrine are studied while accounting for potential ways to overcome the legal gaps in the strategy. The article reaches the conclusion that while the single point of entry doctrine is far from perfect, the basic principles can be applied to Russian legislation and serve as a viable alternative to the prevalent “bailout” practice.

*Keywords:* bankruptcy, single point of entry, bank rehabilitation, vicarious liability, *piercing the corporate veil*.

## 1. Introduction

Single point of entry (henceforth — SPE) bank resolution is a doctrine used in the United States in which Orderly Liquidation Authority procedure set forth by the Dodd-Frank Act<sup>1</sup> (henceforth — Dodd-Frank Act) is used to resolve a solvent financial holding company instead of liquidating the insolvent subsidiary company, oftentimes a bank. During this process, bank regulators use authority provided by Title II of the Dodd-Frank Act to recapitalize the bank at the cost of liquidating the holding company. Thus, the single point of entry bank resolution doctrine combines traits of both a financial rehabilitation procedure and a form of corporate liability, as insolvency of a subsidiary company that is systemically important can be deemed sufficient to swiftly resolve the parent company in an administrative procedure without significant involvement of the courts.

Bank resolution in the U.S. is based on the “too big to fail” doctrine asserting that certain large banks are so important and interconnected that a failure of one of them could prove dangerous to the stability of the entire economic system. Therefore, the use of taxpayers’ money (“bailing out”) is justified to prevent banks’ default. The Dodd-Frank Act was passed in the wake of the Lehman Brothers Holdings Inc. bankruptcy in 2008 when the U.S. government first “bailed out” a large bank using taxpayers’ money. Title II of the Dodd-Frank Act detailed the Orderly Liquidation Authority that enables the Federal Deposit Insurance Corporation (henceforth — FDIC) to perform an organized liquidation of any financial institution deemed “systemically important” (most of such institutions are bank holding companies) in addition to commercial banks that are rehabilitated and resolved via the Prompt Corrective Action procedure under Chapter 7 of the Title 11 of the United States Code<sup>2</sup> (henceforth — U.S. Bankruptcy Code). Orderly Liquidation Authority became a basis for the aforementioned SPE strategy that was proposed by the Financial Stability Board in the year 2013<sup>3</sup> as a way to avoid spending taxpayers’ money in regard to supporting failing banks.

Currently most failing banks in Russia (Promsvyazbank PJSC, Bank Otkritie Financial Corporation PJSC, B&N Bank PJSC and others) are being bailed out by the Central Bank of the Russian Federation (henceforth — Bank of Russia) using taxpayers’ money — more than 2,8 trillion rubles<sup>4</sup> (approx. 40 billion U.S. dollars), a sum equal to Moscow’s yearly budget, was spent in the year 2018 on the financial rehabilitation of the aforementioned bank groups. Essentially, the Bank of Russia is following the “too big to fail” U.S. doctrine, seeking to avoid large bank failures at all costs. However, unlike in the U.S., Russian legislators did not develop an effective alternative to “bailing out” large banks, despite the enormous financial costs of doing so. A SPE strategy could prove to be the answer.

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<sup>1</sup> H. R. 4173 — Dodd-frank wall street reform and consumer protection act 2010. Accessed September 16, 2019. <https://www.sec.gov/answers/about-lawsshtml.html#df2010>.

<sup>2</sup> United States Code. Title 11 — Bankruptcy. Accessed September 16, 2019. <http://uscode.house.gov/browse/prelim@title11&edition=prelim>.

<sup>3</sup> Recovery and Resolution Planning for Systemically Important Financial Institutions: Guidance on Developing Effective Resolution Strategies. 2013. Accessed September 16, 2019. [www.fsb.org/wp-content/uploads/r\\_130716b.pdf?page\\_moved=1](http://www.fsb.org/wp-content/uploads/r_130716b.pdf?page_moved=1).

<sup>4</sup> “Rehabilitation cost Central Bank 2,8 trln rubles”. *Kommersant*. 2018. Accessed September 16, 2019. <https://www.kommersant.ru/doc/3674448>.

## 2. Basic research

### 2.1. *Single Point of Entry strategy*

As shown by the Lehman Brothers Holdings Inc. example, whose bankruptcy was one of the main causes of the financial crisis of 2007–2008 (Gelpert, Vernon 2019), U. S. Bankruptcy Code resolution is not always appropriate for large financial companies, many of which are bank holding companies. Such companies are called systemically important financial institutions (henceforth — SIFI). The legal status of the SIFIs is detailed in Title I of the Dodd-Frank Act. SIFIs are companies that are deemed by FDIC to be integral to the U. S. financial system. All bank holding companies that own more than 50 million dollars in assets are qualified as SIFIs, but the Financial Stability Oversight Council is authorized to qualify other companies as SIFIs as well. SIFIs are subjects to thorough monitoring by the bank regulators and each SIFI is required to submit a yearly rapid resolution plan (also sometimes called a “living will”) to the Federal Reserve Board that details its actions in case of a default that would help minimize the damage to the U. S. financial system.

Title II of the Dodd-Frank Act establishes the Orderly Liquidation Authority to provide an effective procedure for SIFI resolution. The main purpose of the Orderly Liquidation Authority is to grant bank regulators the means to minimize both the systematic risks to stability of the financial system and losses of the U. S. Department of the Treasury. In accordance with Section 203 of the Dodd-Frank Act, Orderly Liquidation Authority can be invoked by the Secretary of Treasury if the SIFI is in default or in danger of default to take control of it. The definition of “default or in danger of default” is provided by Section 203 (b) (4) of the Dodd-Frank Act, but it is quite ambiguous. There are four grounds to invoke the Orderly Liquidation Authority: “(A) a case has been, or likely will promptly be, commenced with respect to the financial company under the U. S. Bankruptcy Code; (B) the financial company has incurred, or is likely to incur, losses that will deplete all or substantially all of its capital, and there is no reasonable prospect for the company to avoid such depletion; (C) the assets of the financial company are, or are likely to be, less than its obligations to creditors and others; (D) the financial company is, or is likely to be, unable to pay its obligations (other than those subject to a bona fide dispute) in the normal course of business”. Due to ambiguity of the legislation, the exact means of assessing SIFI’s financial state lies within the discretion of the Secretary of the Treasury. This provision is often critiqued by the scientific community as a gap in the legislation (Kupiec, Wallison 2015, 188).

After receiving the approval of two-thirds of the voting members of the Financial Stability Oversight Council and the United States District Court for the District of Columbia, the orderly liquidation commences. The Secretary takes control of the SIFI and appoints the FDIC as its receiver. In addition to usual rights held by receivers in Prompt Corrective Action, the normal procedure for liquidating banks provided for by Chapter 7 of the U. S. Bankruptcy Code, the FDIC has more discretion in handling the process. While Prompt Corrective Action can end with the company being rehabilitated, there is only one outcome to Orderly Liquidation Authority — termination of the SIFI.

This limitation is a subject of critique from the legal community (Skeel 2015, 116) as it is generally accepted that reorganization is more efficient for a company’s creditors. Title II Orderly Liquidation Authority is also critiqued for not providing any new tools to

avoid disrupting the U.S. financial system — only allowing bank regulators to liquidate bank holding companies under their supervision.

The SPOE (Single Point of Entry) strategy, however, resolves the default of a financial institution with a complicated corporate structure by taking control over the parent company, as per the Orderly Liquidation Authority, and using its assets to financially rehabilitate its banking subsidiaries without ever placing the bank itself in receivership or disrupting its operation. To complete this goal, the SPOE strategy proposes for the SIFI to transfer most assets to a special bridge bank that would only be operating as long as the financial aid is needed by its banking subsidiaries. Since the newly created bridge company lacks any significant debt or claims against them, it would be able to acquire additional funding from private sources, forming the Orderly Liquidation Fund. The bridge company does have authority to gain loans from the U.S. Treasury, but the debt must be returned and cannot be reimbursed using taxpayers' money.

While the bridge company is occupied with financial rehabilitation of the bank subsidiaries, the SIFI itself goes through administrative bankruptcy procedure similar to Prompt Corrective Action receivership, in which claims of the SIFI's creditors would determine proportional interests of all the claimants for the assets of the both the SIFI and the bridge company. After the bank subsidiaries are rehabilitated, the SIFI would be dissolved as dictated by the Orderly Liquidation Authority, while the bridge bank would be returned to the private sector. Claimants of the SIFI will be reimbursed for their losses via equity, debt or securities of the newly created company as determined by the receiver.

Another important aspect of the SPOE strategy that needs to be considered is that it is, essentially, a form of corporate liability — namely vicarious corporate liability. At its very core, the SPOE strategy uses Section 203 of the Dodd-Frank Act to initiate Orderly Liquidation Authority on the assumption that subsidiary bank failure would also make the parent company bankrupt. Then, the Secretary of the U.S. Treasury and FDIC not only temporarily nationalize property of the parent company, but also take away corporate control of the holding company from the shareholders. Since the holding company usually owns controlling shares in its subsidiaries bank, regulators take away corporate control over the potentially solvent companies in the bank holding group.

It is important to note that under Section 204 of the Dodd-Frank Act it is stated that in Orderly Liquidation Authority creditors and shareholders are the ones will be bearing the losses of the SIFI. Since Orderly Liquidation Authority provides a framework for the SPOE strategy, creditors and shareholders of the parent company are the ones who bear the material losses of the SPOE strategy. It is also important to emphasize that the losses of creditors and shareholders are somewhat limited. As mentioned before, claims to the SIFI become claims in the receivership of the parent company. The claims are eventually partially satisfied using the receivership by means of the receivership estate — consisting of the equity in the bridge bank, the assets that were not transferred to it, such as senior unsecured debt, and subordinated debt, and later with equity, debt or securities of the bridge bank.

Despite the fact that the shareholders are likely to get some corporate control over the newly created bridge holding company after the SPOE strategy ends and the SIFI is liquidated, the corporate rights of the shareholders are disregarded during the receivership. It can be a most serious issue due to the administrative nature of receivership with little judicial control over the procedure, as only the court approval for entering into Orderly Liquidation Authority can be appealed to higher courts.

SPOE provides a strategy that not only makes it possible to minimize losses of the U.S. Department of the Treasury by avoiding the need to “bail out” the bank, but it also limits the bankruptcy effects to the top-tier company in the banking group, allowing its subsidiaries to continue effective operation and preserve their own value. The SPOE strategy is also much more likely to be used by the bank regulators for complex financial intuitions, as it is much more realistic to successfully take over a single parent company and restructure the group’s assets and liabilities from the top compared to taking over individual subsidiaries with the sole purpose of terminating them. Another important benefit of the SPOE strategy is the ability to limit the negative effects on the financial system to one banking group, avoiding bank default and external effects on the U.S. financial system.

However, the SPOE strategy is not without its downsides. The most important downside stems from the aforementioned poor definition of “default or in danger of default”, as sometimes the failure of a subsidiary bank would not cause the failure of the parent holding company, which is especially likely in the case of larger bank groups. In this case, the Secretary of the U.S. Treasury cannot use the Orderly Liquidation Authority and, by extension, SPE. Instead, the Secretary has to resort to Chapter 7 U.S. Bankruptcy Code resolution of the bank itself, despite the fact that it proves to be inefficient for such large financial institutions (Skeel 2014).

Another issue regarding the initiation of the SPOE strategy is the fact that the bank regulators might either not see a default coming or decide to not intervene. Since invoking the SPOE strategy is a right, not an obligation of the regulators, it can be a potential issue. Another downside directly stems from the harm that the SPOE strategy can do to the parent company, its shareholders and creditors. Aware of potential nationalization, investor risks would increase drastically prior to bankruptcy, scaring potential investors away and potentially worsening the existing financial situation as existing shareholders might be desperate to sell their shares and avoid losing their assets. All of those problems will further aggravate financial problems arising from a large proportion of creditors seeking to protect their interests at the same time.

It is noted by researchers (Simmons 2014) that it is critical for the bank holding company to have enough capitalization for the SPOE strategy to be effective. While the liabilities of the parent company are not transferred to the bridge bank, the transferred resources must be sufficient to absorb the losses of its subsidiaries and preferably be enough for the resulting company to function properly after the rehabilitation procedures are over.

## ***2.2. Russian legal framework for bank rehabilitation***

Russian bank rehabilitation bears many similarities to the U.S. regulation on the subject matter, but due to it being a part of the Romano-Germanic legal branch it is much more detailed and defined in its implementation. However, it is also lacking in a few regards.

According to Sec. 189.9 of the Federal Law No. 127-FZ of October 26, 2002 “On insolvency (Bankruptcy)”<sup>5</sup>, the following measures can be implemented to prevent the bankruptcy of a banking organization, before withdrawal of the banking license:

- 1) financial rehabilitation of a bank;

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<sup>5</sup> Hereinafter all references to Russian legal acts are given by ATP “ConsultantPlus”. Accessed September 16, 2019. <http://www.consultant.ru>.

- 2) the appointment of a temporary administration;
- 3) reorganization of the bank;
- 4) measures to prevent bankruptcy of a bank that has a banking license to attract individuals' resources into deposits as well as open and keep individuals' bank accounts which are carried out with the participation of the Deposit Insurance Agency of Russia (henceforth — DIA) or the Bank of Russia represented by the Management company of the Fund for the Consolidation of the Banking Sector (henceforth — Management company).

It should be noted that, much like in the U.S., implementation of the measures for financial rehabilitation in the presence of the grounds specified in the law is at the discretion of the bank regulators and not an obligation. Proposals to impose a duty of the timely application of measures to prevent bank failure have been presented since 2004, but their use is still optional (Yulova 2004, 72–76). It is especially important to note that while in the U.S. the lack of such an obligation could be justified by ill-defined terminology, it is not the case in the Russian Federation.

According to statistics provided by Fitch Ratings 2013, until September 1, 2017, out of 346 banks that lost their licenses, only 35 were rehabilitated (Kholiavko, Borisiak 2017). It is obvious that the Bank of Russia, as a banking regulator, could have taken measures to prevent bank failure in more than 10% of cases. It seems reasonable to establish two lists of grounds for invoking rehabilitation procedures in which less serious violations give the Bank of Russia the right to initiate rehabilitation procedures and more serious violations provide a duty to do so, in much the same way that the grounds for revoking a banking license from a bank are organized.

The rehabilitation measures implemented with the participation of the DIA are subject to special procedure. First, the signs of an unstable financial situation, threatening the interests of its creditors (depositors), should be detected in the bank's activities. Second, the Bank of Russia must decide on sending representatives of the Bank of Russia and representatives of the DIA to the bank in order to analyze the financial situation of the bank and to decide whether to send a proposal to the DIA to take action to prevent bankruptcy. The report, compiled on the basis of the results of the said audit, serves as the basis for making a decision on the participation of the DIA in the implementation of measures to prevent bankruptcy.

The Bank of Russia itself can also participate in bank rehabilitation via the Management Company, in accordance with the decision of the Board of Directors of the Bank of Russia. The main function of the Fund for the Consolidation of the Banking Sector is to provide financial assistance with taxpayers' money by acquiring shares of a mutual investment fund formed by the Management Company, whose assets include 75% of ordinary shares of the bank in the form of a joint stock company bank (shares in the share capital, which provide the right to vote in the amount of at least three-quarters of the votes of the total votes of the bank's participants in the form of a limited liability company). In fact, the bank is temporary nationalized with the procedure mirroring Title II provisions of the Dodd-Frank Act, but without a required liquidation of the bank itself and carried out in regard to the bank, not its parent company.

It is possible to consider bankruptcy prevention measures for banking institutions by examining financial recovery. The main goal of financial rehabilitation is to restore the capital of the failing bank to the value at which banking standards, set by the Bank of

Russia, will be met and the bank can return to stable operation. During financial rehabilitation, the following measures are applied: financial assistance by the shareholders and other private sector parties to the bank, restructuring of assets and liabilities, changing the organizational structure and adjusting the size of the share capital and equity. The Bank of Russia also holds the right to send a request for the implementation of measures for financial recovery to the bank. In this case, the bank loses the right to distribute profits between its shareholders, declare and pay dividends and meet the founders' claims for buying back shares of the bank, if such actions will lead to violation of mandatory standards established by the Bank of Russia.

The temporary administration for managing a banking organization is a special governing body of a bank appointed by the Bank of Russia. The introduction of a temporary administration is an exception to the legal principle of non-interference in the operational activities of banks. It can be argued that the introduction of a temporary administration by the Bank of Russia has as its main goal the prevention of encroachment on the interests of third parties and public interests, the restoration of normal possibilities for exercising the rights of creditors and depositors and eliminating the threat to the stability of the banking system.

The temporary administration is appointed for a period of six months if one or more of the requirements indicated in section 189.26 of the Bankruptcy Code is present. An extension of the temporary administration can be granted up to 18 months total, up to 6 months of added duration at a time. During the temporary administration, the powers of governing bodies of the bank can either be limited or suspended, which is determined at the discretion of the Bank of Russia, which either limits the legal capacity of the bank or suspends it altogether. A distinctive feature of the temporary administration is its rigid and compulsory nature, which consists in the consolidation of administrative control over the activities of a bank during the period when the temporary administration is introduced.

A court appeal against the decision to appoint a temporary administration to manage a bank, as well as the use of measures to secure claims against the bank, does not suspend the activities of a temporary administration to manage a bank. Therefore, the activities of the temporary administration cannot be suspended until a judicial act resolving the dispute is issued. Therefore, the suspension of the temporary administration is possible only when the goals for which it was introduced were achieved or if the commercial bank was declared bankrupt or by a court decision.

When the powers of the executive bodies of the bank are limited, they are restricted in carrying out certain transactions. These transactions are related to the transfer of immovable property of a bank into rent, pledge, its investment into the share capital of third parties and otherwise disposing of property a bank whose book value is more than 1 % of the book value of the bank's assets (Article 189.30 of Federal law "On insolvency (bankruptcy)", 26.10.2002 No. 127-FZ). A bank is also restricted from obtaining and issuing loans, issuing guarantees, assignment of claims, acceptance and forgiveness of debt, novation, compensation, fiduciary management as well as transactions with persons affiliated with the bank on its own will — consent of the temporary administration is required to carry such transactions out.

When the powers of the executive bodies of the bank are suspended, the temporary administration independently decides on all transactions, with the exception of transac-

tions related to the transfer of immovable property of a bank into rent, pledge, its investment into the share capital of third parties and otherwise disposing of property a bank whose book value is more than 5% of the book value of the assets of bank which includes obtaining and issuing loans, issuing guarantees, assignment of claims, acceptance and forgiveness of debt, novation, compensation and fiduciary management. The temporary administration does not have the right to enter into such transactions and makes them only upon receiving the consent of the board of directors or general meeting of the bank's shareholders.

During the term of the temporary administration, a moratorium on the satisfaction of creditors' claims can be issued if the powers of the executive bodies of the bank are suspended. The moratorium is introduced for a period of no more than three months, extendable up to the duration of the temporary administration by adding up to three months at a time. The moratorium applies only to monetary obligations and obligations to make mandatory payments that arose before the appointment of a temporary administration to manage the bank.

If by the time the temporary administration expires there are still grounds for its appointment, the temporary administration sends a petition to the Bank of Russia to withdraw the banking license from the bank. The temporary administration appointed by the Bank of Russia, after the revocation of the license from the banking organization, acts from the date of its appointment until the day the court of arbitration renders a decision declaring the banking organization bankrupt and opens bankruptcy proceedings or until the court rules on the appointment of a liquidator.

Another bankruptcy prevention measure that can be applied by the Bank of Russia is reorganization. Such a forced reorganization is carried out in the form of either a merger or accession. The Bank of Russia also has the right to send a request for its reorganization to a bank. After receiving a demand for the reorganization of a bank, its CEO must, within five days of receiving it, contact the governing bodies of the bank demanding the bank's reorganization. The management bodies of the banking organization are obliged, in turn, to notify the Bank of Russia of their decision no later than ten days after receiving the request. Reorganization is not a widespread measure for bankruptcy prevention in Russia due to the disadvantages it carries for financially stable organizations and the insufficient degree of legislative regulation.

The last pre-trial bank rehabilitation measure is the participation of the DIA or the Managing Company in the implementation of measures to prevent a bank from being subject to the procedure discussed above. The DIA or the Management Company acts in principles of good faith, reasonableness, sufficient awareness of the financial situation of the bank and, ideally, attempts to minimize the expenditure of taxpayers' money. The following measures to prevent bank bankruptcy are used:

- providing financial assistance — also known as bailout. Financial assistance may be provided to maintain liquidity or to replenish funds, for example, in the form of a contribution to the bank's share capital that is being rehabilitated;
- the organization of an auction for the sale of property that is collateral for the fulfillment of a bank's obligations, including ones to the Bank of Russia;
- performing the functions of a temporary administration for managing a bank with a legal status identical to the legal status of a temporary administration of the Bank of Russia;



- implementation of other methods provided by the decision on the participation of the DIA in the implementation of measures to prevent bankruptcy.

Also, the DIA or the Management Company has the right to acquire shares of the bank that is being rehabilitated in the event of the voluntary alienation of the corresponding number of shares (shares) by the owners of the bank, as well as through the procedure of compulsory reduction of the share capital in accordance with the amount of equity and subsequent issue of shares.

After the procedure of reducing the share capital, additional shares may be issued by the bank, which will be fully or partially acquired by the DIA or the Management Company. The shares of the DIA, the Management Company and (or) the investor in the bank's share capital following the results of this procedure should be at least 75 % of ordinary shares of the bank in the form of a joint-stock company (Article 189.49 of Federal law "On insolvency (bankruptcy)", 26.10.2002 No. 127-FZ) (shares in the share capital providing at least three quarters of votes of the total number of participants' votes in the form of a limited liability company) — which in essence means nationalization of the bank. It is also important to note that the procedure in question is not covered by the rules governing the procedure for coordinating actions on the issue of shares with the governing bodies of the bank and government authorities, which speeds up the process of rehabilitation. The Bankruptcy Code also contains provisions obliging the DIA or the Management Company to sell the shares of the bank being rehabilitated upon receiving an offer to sell these shares from the private sector. This measure exists to prevent the restriction of competition in the banking services industry and to prevent the concentration of capital in the hands of the DIA and, accordingly, in the hands of the state. The sale is carried out in form of a public auction. It is important to note just how similar the aforementioned procedure is to the Orderly Liquidation Authority established by the Dodd-Frank Act — the only significant differences being that it is applied to banks, not bank holding companies, and that it does not have to result in a company's liquidation.

### *2.3. Russian legal framework for piercing the corporate veil*

The main idea of "piercing the corporate veil" legal doctrine is to hold the controlling person liable for a subsidiary's obligations in outstanding circumstances. While the term "piercing the corporate veil" does not appear in Russian legislation, the phenomenon still exists. Several legislative provisions provide for the cases in which it is possible to ignore a corporation's separate legal identity to collect debts from that company's owners — namely either the parent company or the shareholders.

There are several legal provisions that allow for the vicarious liability of the controlling person.

The first provision is liability of the controlling persons during insolvency (bankruptcy). It is important to note that even beneficiaries that are not legally affiliated with the subsidiary, but did control it and profited from it, can be held vicariously liable in bankruptcy. The second such provision is liability of the parent company arising from the obligations of the subsidiary in civil law — section 3 Article 67.3 of the Russian Civil Code (Part one) from 30.11.1994 No. 51-FZ. This provision does not define the criteria for applying this ruling, but there are several aspects that Russian courts analyze in such cases (Shevchenko 2016): whether the parent company or beneficiary were controlling the

subsidiary; whether there was economic rationale for both the parent company and subsidiary's actions; whether the parent and subsidiary acted in their own interests, whether there was an abuse of the corporate legal identity and whether such abuse had an illicit purpose. These provisions, when supported by principles of Russian civil law such as reasonableness of conduct, acting in good faith and prevention of the abuse of rights, allowed for the legal adoption of a common law concept initially alien to the Russian legal system that is part of Romano-Germanic legal branch (Spirina 2014).

The third provision is detailed in the Russian Tax Code (Part one) from 31.07.1998 No. 146-FZ subsection 2 of section 2 of Article 45 that allows the Tax Service to seek taxes in a court procedure from the parent company instead of its subsidiary if the revenue from goods sold (services provided) by the subsidiary is received by the parent company. There are several other tax law court cases involving piercing the corporate veil in situations when the corporate legal identity of the subsidiary was only used for the purpose of tax evasion and thus benefited the parent company (Shitkina 2013). It is important to note that due to tax law being a part of public law, the necessity of upholding public interest justifies the application of "piercing the corporate veil" doctrine.

#### *2.4. Possibilities of legal adoption of the single point of entry doctrine in Russia*

Currently most banks in Russia are being rehabilitated under the direction of the Managing Company, and, as was previously mentioned, the Managing Company extensively uses budget funds to fund the bailout of large failing banks. This situation is far from ideal, but currently other bankruptcy prevention measures have proven to be only marginally effective.

Researchers note (Tarasenko 2016) that the procedures associated with pre-trial bank rehabilitation are not sufficiently effective. Banks avoid the use of these procedures by concealing their real financial situation. Most assets of the overwhelming majority of bankrupt banks are artificially generated by internal postings involving banking companies as a result of suspicious transactions.

Banking regulators and legislators seem to be aware of the problem and are trying to resolve it. Bankruptcy prevention of banks is constantly evolving, the last innovation being the introduction of the Management Company in 2017. There is also one example of the use of the "bail-in" mechanism adopted from foreign practice of bank bankruptcy prevention. On April 19, 2017, the Board of Directors of the Bank of Russia approved changes to the DIA's Participation Plan in the implementation of measures to prevent the bankruptcy of the Bank AK PERESVET (JSC)<sup>6</sup>. This procedure allowed to rehabilitate the bank with creditor funds instead of budget funds. The Bank's creditors expressed a desire to take part in financial rehabilitation by converting funds placed in the Bank in the amount of 69,7 billion rubles into 20-year subordinated bonds. It is interesting to note that, unlike the foreign "bail-in" procedure, as a result of which creditors become shareholders, creditors of JSC PERESVET (JSC) did not receive shares.

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<sup>6</sup> "About rehabilitation measures of AKB 'PERESVET' (AO)". *Press-tsentr Tsentral'nogo banka Rossiiskoi Federatsii*. 2017. Accessed September 16, 2019. [http://cbr.ru/press/PR/?file=19042017\\_133539ik2017-04-19T13\\_35\\_04.htm](http://cbr.ru/press/PR/?file=19042017_133539ik2017-04-19T13_35_04.htm).

The possibility of introducing such a measure has been a topic of discussion since 2015 (Isaeva, Sharmok 2016). The researchers note that the introduction of such a mechanism would not only reduce government spending on bank rehabilitation, but would also allow for the protection of bank creditors' rights more effectively. According to statistics provided by the DIA, claims of the first-priority creditors are satisfied on average by 54,3 %, and the third priority only 6,1 %. It can be more profitable for the majority of creditors to convert claims that are satisfied to such a small extent than to get such an incomplete satisfaction of their claims. However, such a procedure can only be applied to smaller banks, whose creditors can afford to receive securities instead of their claims. Obviously, such an approach would not work with large financial institutions that provide their banking services to millions of individuals and hundreds of thousands of companies.

The SPOE strategy is in many ways appropriate for the Russian legal system and can be legally adopted. The main issue is adopting a concept that in its very nature ignores the corporate identity of the bank itself — a concept contradicting the very basics of what a company is under Russian corporate law. However, as it was mentioned before, the Russian legal system already acknowledges the prevalence of public interest to the interests of companies and their legal identities in many cases. In civil law, a parent company can be held accountable for a subsidiary's responsibility. In bankruptcy prevention procedures, bank governing bodies can be stripped of their powers and the bank can be nationalized. During bankruptcy itself, a controlling person can be held accountable for a company's debts even if they were not formally affiliated with it. In tax law, corporate legal identity can be ignored if that identity is used for tax evasion purposes. A holding bank's parent company is essentially liable and can use its assets to rehabilitate a failing bank by utilizing a Dodd-Frank based procedure that already exists in a slightly changed form for when the DIA or the Management Company participate in bank rehabilitation.

Another issue is formulating grounds for invoking the SPOE strategy. In the U.S. an ill-defined "default or in danger of default" term is used to assume that a holding company would be insolvent after the subsidiary bank goes bankrupt. Introducing a term that lacks clear juridical technique would be a mistake. Instead, using the SPOE strategy can be seen as an additional bank bankruptcy prevention measure, added to the Sec. 189.9 of the Bankruptcy Code and further detailed later in Title 4.1. It would also be important to keep the required court approval for initiation of the procedure — preferably in the form of summary judgment to preserve the ability to intervene timely. It would be wise to avoid receipting Orderly Liquidation Authority's requirement to liquidate the holding company and keep the procedure itself as similar to current bank rehabilitation as possible.

A few similarities show just how noninvasive this adoption can be. First, banks are often owned by the holding companies, and those holdings are regulated by banking law (Article 4 of Federal Law from 02.12.1990 No. 395-1 "On banks and banking activity"). In fact, bank holding companies are the only ones in Russian legislation that have their own regulation — other holdings are subject to the same rules as any other company. Another similarity is the fact that the Bank of Russia, much like the FDIC, has a list of systemically important banks (Ruchkina 2018). And while their bankruptcy is not regulated separately and the list itself is only comprised of banks, the existence of such a list illustrates similarities in bank regulators' mindsets.

It is worth noting that the current Russian legislation does not provide for the possibility of developing and submitting an independent financial rehabilitation plan to the

Bank of Russia. Such an opportunity, as some authors note, would serve as an incentive to develop plans to restore the bank's solvency, which would be more effective than the measures applied by the temporary administration (Ramzanov 2012). It would be especially appropriate for the SPOE strategy, as rehabilitating a large bank might be problematic even with access to the bank holding company's funds. It would also be appropriate to impose additional minimum asset requirements upon the bank holding companies for the regulators to be able to recapitalize the failing subsidiary bank in case of its failure using the SPOE strategy.

### 3. Conclusion

In conclusion, it should be noted that currently the main problem of the bankruptcy prevention measures in Russia is the lack of effective alternatives for "bailing out" the failing bank. However, bankruptcy prevention measures are being actively developed. Adding the SPOE strategy to the existing list of bankruptcy prevention measures would allow bank regulators to carry out bankruptcy prevention measures in the most efficient way. The SPOE strategy is, in many ways, similar to both Russian legislation on the matter of bank rehabilitation and the Russian doctrine of piercing the corporate veil. This similarity facilitates an assessment of viability of legally adopting the single point of entry bank resolution doctrine in Russia.

Adoption of the SPOE strategy would benefit the Russian bankruptcy system for banks in several ways. First, banks would be rehabilitated more effectively with less budget funds spent than in the currently prevalent bailout strategy. Second, it will serve to prevent abuses by bank's holding company, as such actions might provoke effective nationalization of the company. Third, numerous similarities in national legislation and bank resolution practices will likely make legal adoption noninvasive and effective, complimenting existing bank rehabilitation system without disrupting it. SPOE strategy is not a universal solution to bank bankruptcy, and nor it is perfect, but we believe that its basic aspects can be integrated into the Russian legal system to create a viable alternative to the prevalent practice of bailing out banks using budget funds.

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