Ivars Kronis, *Dr.iur., assoc. prof*
Baltic International Academy
Latvia

Criminal liability for delay of insolvency proceedings

Abstract. The article analyzes the legal norm, which provides for the criminal liability of the administrator and the representative of the debtor within the framework of legal entity insolvency proceedings or of the insolvent natural person in these proceedings. Up to now the criminal law science of Latvia discussed the issue of criminal aspects of delaying insolvency proceedings, however the authors, who researched them, did not go into details or analyzed them in conjunction with the previous insolvency regulation. This is indicative of the topicality of the theme, the importance of theoretical and practical research in the modern criminal law. By means of his thesis, the author wants to even if partially close this gap, examining the most important aspects of the theme.

Although the time passed after the effective date of the new Insolvency Law of November 1, 2010 is not enough to form legal practice in the criminal aspects related to delaying insolvency proceedings, it is the right moment to emphasize the urgency of the problem and to thoroughly evaluate the most important issues. Therefore, the purpose of the thesis is, analyzing peculiarities of offence as specified in Article 215 of the Criminal Law, to evaluate theoretical and practical aspects of its application. The empirical base of the research is formed by scientific theses and collections of articles, periodical editions and primary sources, legal acts, statistical data, Internet resources, other information in the public domain. To develop the thesis, the author used analytical, comparative, inductive and deductive methods of research.

Keywords: insolvency proceedings, administrator, creditor, debtor, criminal liability.

Ивар Кронис, *Dr.iur., доцент*
Балтийская Международная Академия
Латвия

Уголовная ответственность в случае нарушения сроков процедуры признания неплатежеспособности

Аннотация. В статье проанализирована правовая норма, предусматривающая уголовную ответственность администратора процесса неплатежеспособности и представителя должника в процессе неплатежеспособности юридического лица либо самого неплатежеспособного физического лица в данном процессе. В науке уголовного права Латвии до настоящего времени рассматривался вопрос уголовно-правовых аспектов воспрепятствования процессу неплатежеспособности, но авторы, которые исследовали данные аспекты, рассматривали их кратко либо анализировали во взаимосвязи с предыдущим правовым регулированием неплатежеспособности. Это свидетельствует об актуальности темы, значимости теоретического и практического исследования для нынешнего уголовного права. Своей статьей автор желает хотя бы частично восполнить этот пробел, рассмотрев наиболее важные вопросы, связанные с данной темой.

Несмотря на то, что после вступления в силу нового Закона о неплатежеспособности 1 ноября 2010 года прошло недостаточно времени для создания судебной практики в уголовно-правовых аспектах по воспрепятствованию процессу неплатежеспособности, это – подходящий момент для актуализации проблематики и углубленной оценки важнейших вопросов. Цель статьи – путём анализа особенностей деяния, предусмотренного статьей 215 Уголовного закона, дать оценку теоретических и практических аспектов ее применения. Эмпирическую базу исследования формируют научные работы и материалы сборников статей, периодические материалы и первоисточники, правовые акты, статистические данные, интернет-ресурсы и прочая публично доступная информация. Для разработки исследования были использованы аналитический, сравнительный, индуктивный и дедуктивный методы исследования.

Ключевые слова: процесс неплатежеспособности, администратор, кредитор, должник, уголовная ответственность.

Preface

The paper takes up an in-depth review of issues of criminal law pertaining to individual cases of insolvency proceedings by focusing on the issues of delayed insolvency proceedings.

In the science of Latvian criminal law issues of delayed insolvency proceedings have been inspected until now, however they have been viewed fragmentally or the analysis may have become outdated due to changes in the judicial regulation of insolvency proceedings. This is why this subject could be theoretically and practically relevant, inviting a discussion on the most essential nuances of the subject. Criminal law expert J. Baumanis in his newest monograph *„From the interpretation of norms of criminal law to quantum criminology"* has come to the conclusion that „if the norms of law get incompletely and imprecisely formulated, then any reference to them is judged as not fully founded. A more detailed analysis of the existing problems of criminal law theory can only be made based on a clear and unmistakable regulation of criminal liability." [1, 21] This article will evaluate the essence and efficiency of respective norms of law, determining criminal liability for committing a criminal offence in the field of insolvency.

Even though the time since the new *Insolvency Law* (IL) [2] came into force on November 1 of 2010 is sufficient for the establishment of a judicial practice in the criminal law aspects of delayed insolvency proceedings, this article is dedicated more to raise awareness of theoretical problems and an in-depth evaluation of the most essential issues.

Aim of the paper. The aim of the article is to evaluate the theoretical and practical aspects of enforcement by analysing the peculiarities of the criminal offence as intended by the Criminal law (CL) [3] Section 215.

Material and method. The empirical basis of the research consists of scientific works and collections of papers, articles in recurring publications and primary sources, legislative acts, statistical data, internet resources, as well as other publically available information. In the development of the research, analytical, comparative, inductive and active research methods have been used.

Results and discussion

Section 215 of the *Criminal law "Delay of insolvency proceedings"* has experienced many essential amendments since its initial version, namely, changes have been made to its previous title i. e., *Violation of the rules of insolvency proceedings*, and in relation to the implemented reform of criminal punishment [4] the Paragraph one of the section has been removed [5;6;7]. In relation to this, it should be noted that Section 166^{36} of the *Latvian Administrative Violations Code* (LAVC) stipulates liability for violations of rules of insolvency proceedings if it is done by a person involved in the insolvency proceedings. Thereby in individual cases there arises a mutual overlapping of features of the judicial structure, and the person who exercises recordkeeping in the case of administrative violations has an obligation to commit case files to the investigative institution. If no constituent elements of criminal offence are established during the investigation within the framework of criminal proceedings, a debtor's representative might be subject to administrative liability with delay for carrying out a violation of Section 166^{36} of LAVC.

There are two types of insolvency proceedings differentiated in the *Insolvency Law: the insolvency proceeding of legal persons and those of natural*

persons (IL Sections 4, 5). *Legal Protection Proceedings* (see. IL Section 3) as regulated by insolvency rights are not insolvency proceedings. Consequently the liability specified in Section 215 of CL is not applicable to this type of proceedings, but it is specified in Section 215 *"Violation of Legal Protection Proceedings Regulations"*.

The insolvency proceedings of a legal person are an aggregate of measures of a legal nature, within the scope of which the claims of creditors are settled from the property of a debtor, in order to promote the honouring of the debtor's obligations (IL Section 4 Paragraph one). This process is not deemed as a debt collection mechanism, which is why its initiation does not mean that the creditors' claims will be satisfied in full. This process is directed by a court appointed administrator of insolvency proceedings, who executes the imposed demands of the proceedings, which includes overtaking of documents and property from the representatives of the debtor; evaluating the claims of the creditors; ensuring termination of creditor's contracts; recovering the debts of debtors, selling the property of the debtor; satisfying the claims of the creditors using the means obtained. After the insolvency proceedings have been completed, the legal person is excluded from the particular public register.

However, the aim of the insolvency proceedings of the natural person is to satisfy the claims of creditors as much as possible from the property of a debtor and provide the opportunity for a debtor whose property and income is insufficient to cover the entire obligations to be released from the obligations which have not been honoured and to restore solvency. (IL Section 5 Paragraph one). If the natural person has fulfilled the plan for extinguishing obligations, the remaining, uncovered debt obligations are fully extinguished, and the creditors lose the right to claims against the natural person. The insolvency proceedings of the natural person consist of two consecutive proceedings, namely, bankruptcy proceedings are initiated after the declaration of insolvency proceedings and after their completion that is approved by the court, the court simultaneously evaluates whether the procedure to extinguish obligations is to be declared.

The insolvency proceedings are explicitly regulated in the law and depending on the amount of assets and transactions of the insolvent person, as well as type of proceedings (insolvency proceedings of the legal or natural person) can take up from a few months to several years, for instance, if proceedings are initiated for the recovery of debts, recovery of losses, recognition of transactions as invalid etc. In regards to the insolvent natural person, the period for the procedure of extinguishing obligations as specified in Section 155 of IL can take up to three years.

According to the general rule, all property of the debtor both as a legal person and a natural person has to be sold over the course of six months during the insolvency proceedings after the proclamation of the respective proceedings. The administrator may extend the term for selling the non-pledged property of the debtor for up to six months. (IL Section 111 Paragraph 6, 7). Whereas in regards to the natural person, if the secured creditor and debtor have entered into an agreement to keep the dwelling which is encumbered by a pledge, and this agreement is comparable with the interests of the other creditors, then this property is not sold. (IL Section 146 Paragraph 2). Furthermore, according to Paragraph seven of Section 111 of IL, if it is impossible to sell the debtor's property or the property sales costs exceed the projected revenues, the administrator shall exclude it from the plan for the sale of the property and shall, without delay, notify all creditors thereof in accordance with the procedures laid down in Section 81 of IL, inviting them to retain the property to themselves at its initial price.

Insolvency proceedings can be initiated only if the court has proclaimed them, namely, the insolvency proceedings of a legal person shall be commenced from the day when the court has proclaimed insolvency proceedings by the adjudication and shall take place until the day when the court takes a decision to terminate the insolvency proceedings. (IL Section 4 Paragraph 2). But the insolvency proceedings of a natural person shall be commenced from the day when the court has proclaimed insolvency proceedings by the adjudication and take shall place until the day when the court takes a decision to terminate the insolvency proceedings. (IL Section 5 Paragraph 2).

The offence specified in Section 215 of CL consists of two parts which impose criminal liability for the two special subjects, namely:

1) the administrator of the insolvency proceedings and
2) the representative of the debtor (in the insolvency proceedings of a legal person) or the insolvent natural person (in the insolvency proceedings of a natural person.

From the above mentioned it follows that criminal liability for delaying insolvency proceedings for creditors, interested persons, or other third parties is not specified, even though these persons can take up actions that delay insolvency proceedings because they are directly involved in each of the proceedings.

Only a natural person, who is appointed to the position of the administrator and who has the rights and obligations as specified by the Insolvency Law may be the administrator of insolvency proceedings, moreover within scope of the activities of the position, administrators can be equated to public officials. Consequently the administrator is one of the guarantees of a lawful and efficient process for insolvency proceedings, and to secure this, Paragraph two of Section 215 of CL imposes criminal liability to the administrator for:

1) failing to provide the information to the court, creditors' meeting or other institutions or persons as specified by the law or deceiving them, as well as
2) engaging in transactions in favour of one or several creditors to the detriment of the remaining creditors.

The criminal offence is formally defined because it is deemed as completed at the moment of carrying out the aforementioned actions or at the moment of the subject’s inactivity [9,190].

Since ensuring the process for insolvency proceedings requires information, documentation and property, Paragraph three of Section 215 of CL imposes criminal liability to a representative of the debtor or an insolvent natural person for:

1) impeding the course of insolvency proceedings, which is manifested in the conduct of the representative of the debtor or the natural person as evading participation in adjudication of the matter or the meeting of creditors of the legal person subject of the insolvency proceedings,
2) failing to provide or concealing the information prescribed by law and requested by the court or by the administrator, illegal alienation of property, concealing property or transactions, non-transference, concealing, destroying or forging documents or other intentional acts which delay the course of the insolvency proceedings.

The criminal offences mentioned in Section 215 of CL are less serious crimes (paragraph two of the section) or serious crimes (paragraph three of the section), and punishment for the criminal offences mentioned in the article ranges from community service or fine to deprivation of liberty for up to 5 years. Thereby they are deemed as serious offences by the Insolvency Law that impose criminal liability. At the same time, it must be concluded that there is in fact criminal liability for offences (for instance, evading participation in adjudication of the matter or the meeting of

creditors, failing to provide information and other intentional actions) that cannot cause any serious harm to public interests which is why they should be decriminalized, establishing only an administrative liability regardless of the frequency with which they are committed [10;11].

The group object of criminal offences specified by Section 215 of CL is the interests of the national economy in the sphere of capital companies department and economic activities. But, looking at the direct object of offence, specified by Section 215 of CL, it is: the lawful and efficient process of insolvency proceedings, that can be disturbed in certain cases if the respective person does not perform actions that are specified by the legislative acts regulating insolvency proceedings, or performs actions that are specified by Section 215 of CL.

It could be regarded that every subject's action that is specified by Section 215 of CL extends insolvency proceedings, which in turn means that its lawful and efficient process is obstructed [12].

The objective side of the criminal offence specified by Section 215 of CL can manifest as an intentional action by the administrator – failing to provide of information to the court, creditors' meeting, or other institutions or persons or deceiving them, as well as engaging in transactions in favour of one or several creditors to the detriment of the remaining creditors.

As I. Sokolovska, the deputy of the chief of Economic Crime Enforcement Department of The State Police, said in an interview, the subjective side of the criminal offence as specified by Section 215 of CL is characterized by direct intent. The problem arises in the process, when police is examining applications, and it is not possible to establish this direct intent, and accordingly decisions are made to refuse to initiate criminal proceedings or to terminate them. [13]

In reference to the previously mentioned, it should be noted that in practice there is often a problem in the distinguishing between civil and criminal liability, namely, in situations when the possible criminal offence is not self-evident. It is necessary to bring to attention and analyse those signs that might indicate a criminal offence. Often situations arise when while examining applications of persons, law enforcement agencies decide to refuse to initiate criminal proceedings justifying it with the civil law nature of elements of a criminal offence and the legal relationships although in reality such decisions are made due to insufficient care in the evaluation of actual circumstances. [14, 19]

As stated in Clause 2 of Paragraph three of Section 26 of the Insolvency Law, the general duty of the administrator is to provide information regarding the course of the relevant proceedings to the court, the creditors, the Insolvency Administration and other persons and institutions specified in laws and regulations. Besides in the insolvency proceedings of a legal person the administrator informs creditors about: 1) the plan for the sale of the debtor's property; 2) the non-existence of property in the debtor's establishment; 3) the amount of the remuneration of the administrator; 4) the expenses of the insolvency proceedings of a legal person; 5) the plan for settling the claims of creditors; 6) the intention to renounce the claims; 7) the intention to enter into a settlement; 8) the intention to perform the cessation of the right to claim; 9) the extension of the deadline for selling of non-pledged property. The administrator shall notify the creditors of other matters which have significance during the course of the insolvency proceedings of a legal person (see IL Section 81). In case the administrator does not provide information, the court can remove the administrator and appoint another one for the insolvency proceedings.

Based on the conclusions of case-law, a situation is possible when the administrator does not provide information to the newly appointed administrator [15]. Paragraph two of Section 24 of the Insolvency Law states that in the case of change

of administrators, that is, if the previous administrator resigns or is removed from office, until the deadline specified by the court which shall not exceed 10 days, the previous administrator shall compile a deed of document and property delivery and acceptance which shall be signed by the previous administrator and the new administrator. A review of the activities of the previous administrator shall be appended to the deed of property delivery and acceptance. If the drawing up of a deed of document and property delivery and acceptance and a review of activities is not objectively possible, the new administrator, when commencing the fulfilment of duties, shall draw up a report on the actual situation and notify the creditors thereof (IL Section 24. Clause 4).

Concerning the creditor's meetings, which are not obligatory in the insolvency proceedings, creditors decide only on five issues: 1) remuneration of the administrator; 2) proposal for the removal of the administrator; 3) approval of the expenses of insolvency proceedings; 4) the manner of selling the debtor's property or the extension of deadline for the sale thereof; 5) further handling of the property that has been excluded from the plan for the sale of the property (see IL Section 89, Section 111, Paragraph seven, Section 115 Paragraph 2.1). Consequently the competence and necessity of the creditors' meeting is quite limited. It should be taken into consideration that providing information depends on the special rules in the law of every type of insolvency proceedings.

In turn, deceiving can manifest as providing of false or incomplete information about the most important issues of the insolvency proceedings. For instance, on the issue of creditor claims, the law states that every creditor, who has submitted a creditor claim, and representative of the debtor has the right to get acquainted with the submitted claims of the creditors and the evidence for their validity. In practice individual creditors invite a sworn bailiff [16] for the establishment of the legal fact in order to have confidence in the credibility of creditor claims and the continuity of documents without informing creditors. Criminally liable are the transactions made by the administrator that have been made in favour of one creditor to the detriment of the remaining creditors if a creditor gains more rights than he could gain by taking part in the insolvency proceedings in accordance with the procedure laid down by law. [12].

The success of the insolvency proceedings mainly depends on the actions of a debtor's representatives transferring documentation and property to the administrator, therefore Paragraph there of Section 215 of CL states that from the objective side the criminal offence takes active action (evading participation in adjudication of the matter or the meeting of creditors of a in the insolvency proceedings of a legal person, concealing the information prescribed by ;law and requested by the court or by the administrator, illegal alienation of property, concealing property or transactions, concealing, destroying or forging documents or other intentional acts which delay the course of the insolvency proceedings), as well as inaction(failing to provide the information prescribed by law and requested by the court or by the administrator, failing to transfer documents that delays the process of insolvency proceedings), if it is done by not only a representative of a debtor or an insolvent natural person, but also the administrator of insolvency proceedings (special subjects).

A representative of a debtor in the insolvency proceedings of a legal person according to Paragraph one of Section 68 of IL is appointed by the administrator, by observing the following order: 1) a member of an executive authority who is entitled to represent the debtor separately; 2) another member of an executive authority; 3) the head of a supervisory body; 4) another member of a supervisory body; 5) a participant (shareholder), who has the greatest number of votes.

Paragraph one of Section 72.1 of IL imposes civil liability to members of the board of a capital company, namely, they shall be jointly liable for the losses incurred by the debtor (insolvent company), if they have failed to provide the debtor's accounting documents to the administrator of the insolvency proceedings, or the documents are in a state, which does not allow obtaining a true and fair view of the debtor's transactions and the state of property within the last three years preceding the proclamation of the insolvency proceedings..

For this reason in practice shortly before the proclamation of insolvency proceedings, the participants and the board are replaced with third-country nationals (for instance, citizens of The Russian Federation, citizens of The Republic of Kazakhstan etc.) indicating that they have taken over all property and documentation. This way the board tries to evade responsibility, thus impeding the proceedings.

After the proclamation of insolvency proceedings, representatives of the debtor are obliged to prepare lists and documents to be handed over to the administrator, as well as notify the administrator and the court of the address of the new place of residence during the course of the entire proceedings (see IL Section 70). If the administrator is not given the documents of the debtor, the administrator does not have information about the concluded contracts. As a result these transactions may be continued. Of course the execution of this obligation takes time and resources, but debtors tend to excuse themselves claiming that they cannot afford a bookkeeper, accountant, or that they are busy due to legal relationships connected to the job. Such an excuse is not justified because obligation is specified in the law, and it follows from the liability of the member of the board. It should be noted that the debtor’s representatives cannot ask any payment from the administrator for carrying out of such duties during the insolvency proceedings.

Situations when former board members of the insolvent company hide their property and transactions is quite a widespread phenomenon, and it takes a long time for the administrator to recover the property of a capital company [17,12]. Recovery of property is a complicated process, and it often goes on for several years. If the members of the board without supporting documentation have withdrawn money from the capital company or given the property belonging to the capital company to someone as a gift, constituent elements of an intended criminal offence as stated in Section 179 of CL [17, 12] can be established. In practice, prior to the initiation of the insolvency proceedings, the board members pay out the remaining money in wages or pay off any previously taken loans.

Interested persons also have a significant role in the insolvency proceedings, namely, in the proceedings of a legal person: 1) the participants (shareholders) of a debtor or members of a partnership, members of an administrative body; 2) the proctor and person with a commercial power of attorney; 3) the person who is married to or is in relation or affinity to the second degree with the founder, participant (shareholder) of the debtor, or member of a partnership or member of an administrative body; 4) a creditor who is in one group of companies with the debtor. These interested persons in regards to the debtor shall be recognised if they have been in this status for the preceding five years prior to the day of proclamation of the insolvency proceedings of the debtor. (IL Section 72) In the proceedings of natural persons: 1) the debtor’s spouse; 2) a person who is in relation or affinity to the debtor to the second degree; 3) the debtor's guardian or trustee; 4) a commercial company in which the debtor has a decisive influence within the meaning of the Group of Companies Law. As an interested person in relation to a debtor shall be considered such person who has been in this status within the last five years prior to the initiation of the matter of insolvency proceedings of a natural person. (IL Section 131).

Since transactions between debtors and interested persons are very widespread in practice, Section 96 of IL gives a chance to challenge these transactions from the point of view of the Civil Law, however it does not stop these persons from concluding transactions, which creates losses and complicates the process. Other types of encumbering of property are also widespread, for instance transfer of residential or non-residential premises to the use of other persons. [18].

Conclusion

To sum up the above mentioned, it may be concluded that the legislator disproportionately asks for a certain type of behaviour from the administrator, but such demands are not imposed on the other parties involved in the proceedings, for instance, a creditor, interested person or debtor. The disproportion can also be noticed in the fact that all decisions or actions by the administrator can be appealed, and the administrator can be removed, but bringing proceedings against other involved persons that delay insolvency proceedings is limited. Therefore the criminal liability for delaying insolvency proceedings should be imposed on a wider range of persons, while at the same time aligning the Section 215 of CL with the liability specified by Section 16636 of LAVC.

References

1. Baumanis J. From Interpretation of criminal law rules till quantum criminology. Riga: Latvijas Vēstnesis, 2017;
2. Insolvency Law: law of the Republic of Latvia, Latvijas Vēstnesis, 06.08.2010., No. 124 (4316);**3.** Criminal Law: law of the Republic of Latvia, Latvijas Vēstnesis, 08.07.1998., No. 199/200 (1260/1261);
3. About Conception of Criminal Sanctions Policy. 09.01.2009. Cabinet Order No. 6/LV, 6 (3992), 13.01.2009;
2. **5.** Amendments to the Criminal Law: law of the Republic of Latvia, Latvijas Vēstnesis, 10.11.2010., No. 178 (4370), Point 38;
3. **6.** Amendments to the Criminal Law: law of the Republic of Latvia, Latvijas Vēstnesis, 29.12.2007., No. 208 (3784);
4. Amendments to the Criminal Law: law of the Republic of Latvia, Latvijas Vēstnesis, 27.12.2012., No. 202 (4805);
5. Latvian Administrative Violations Code: law of the Republic of Latvia, Ziņotājs, 01.07.1984., No. 51;
6. Hamkova D., Krastiņš U., Liholaja V. Commentary on Criminal Law. Third part (XVIII – XXV[1] section). Riga: Tiesu namu aģentūra, 2016;
7. Annotation of the Draft Law Amendments to the Criminal Law (No. 794/Lp12). Available: http://titania.saeima.lv/LIVS12/saeimalivs12.nsf/0/1995DC23D08AA716C225808E002F9306?OpenDocument#b, viewed 16.05.2017.;
8. Letter No. 1-10/64 (15.02.2017.) from the Association of the Certified Administrators of Insolvency Proceedings of Latvia. Available: http://titania.saeima.lv/LIVS12/SaeimaLIVS12.nsf/0/9A66018A47A74FF6C22580C900444088?OpenDocument, viewed 16.05.2017.;
9. Bērziņš J. Criminal Law Aspects of Insolvency Proceedings. Jurista Vārds, 16.10.2007., No. 42 (495);
10. Luksa M. Risks of insolvency proceedings: enough talking, start doing! Available: https://lvportals.lv/norises/279349-maksatnespejas-procesa-riski-pietiks-runat-jasak-darit-2016, viewed 17.05.2018.;
11. Smans A. Civil and criminal liability interconnectedness and abstraction. Jurista Vārds, 13.03.2018., No.11 (1017);
12. Supreme Court Department of Criminal Justice of the Republic of Latvia 10.02.2015. ruling in case No. SKK-5/2015;
13. Law On Bailiffs Section 74, first paragraph, point 2: law of the Republic of Latvia, Latvijas Vēstnesis, 13.11.2002., No. 165 (2740);
14. Kuļkova D. Reflection of criminal law aspects in insolvency and legal protection proceedings in Latvia. Administratīvā un Krimināla Justīcija, No. 3 (52), 2010;
15. Neiland R. Fictive rental contracts. Jurista Vārds, 20.09.2016., No. 38 (941).