

# Pre-Trial Prevention of Insolvency: Technology, Procedures, Innovations

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**Abstract:** *The purpose of this work is to determine the essence of pre-trial prevention of insolvency of an economic entity, consider the content of this phenomenon, and study its use in order to prevent the existing negative consequences of insolvency proceedings in the economy.*

*The methodological basis of the study comprises the general scientific dialectical method of cognition, which allows considering the institutions of law in the relationship, integrity, and development. Special and specific scientific methods are used: historical and legal, formal and logical, the method of comparative law.*

*In order to achieve this result, the following more specific tasks are proposed: to determine the place of pre-trial prevention of insolvency of an economic entity within the framework of the institution of insolvency; to isolate the structure of the phenomenon of pre-trial prevention of insolvency; to determine the essence of the specific aspects of pre-trial prevention of insolvency; to analyze the features of individual procedures and develop proposals for the legal regulation of their conduct; to develop proposals to improve domestic insolvency law in order to ensure the possibility of preventing the negative consequences of bankruptcies in the pre-trial stages.*

*Based on foreign experience, it is proposed to regulate the activities of domestic entrepreneurs in the field of pre-trial prevention of insolvency of economic entities at the legislative level.*

**Keywords:** *economic entity, insolvency (bankruptcy), legal regulation, legal status, pre-trial prevention.*

## I. INTRODUCTION

The institution of insolvency (bankruptcy) of foreign states has a long history.

The dynamics of changes in the current domestic legislation on bankruptcy, the extensive practice of its application, and the number of scientific studies suggest a significant relevance of insolvency problems for modern Russia.

Recently, the urgency of the problem has increased, due to the development of business relations and the need to ensure the stability of civil turnover.

The institution of insolvency is gradually becoming a natural and necessary element of the market economy. At the same time, in society, in general, the institution of bankruptcy is

still perceived as extremely negative and destructive. Indeed, despite the fact that the institution of insolvency is aimed at rehabilitation, any bankruptcy process has a number of negative consequences, such as: mass dismissal of employees, suspension of production, and destabilization of market relations due to nonpayment and liquidation of an economic entity. Often, the court procedure leads to an unreasonable delay in payment or complete nonpayment of salaries. In the case of ineffective arbitration management, violation of the balance of interests in the direction of unscrupulous creditors, it is possible to destroy the enterprise as a property complex, to unreasonably separate and dissolve it. As a consequence, the existing relationships in this area of the market substantially and unreasonably change, an economic entity, occupying its niche and capable to efficiently operate, disappears.

Market relations require the creation of an effective mechanism for eliminating unprofitable working entities from economic turnover. In this regard, the role of the insolvency institution increases, as it is intended to address the insolvency of individual legal entities.

In these circumstances, the study on the problems of pre-trial prevention of insolvency of an economic entity in Russia seems relevant. It allows formulating a number of definitions of basic concepts, revealing the content and essence of measures and procedures for the Russian economy.

## II. LITERATURE REVIEW

The sources include the provisions of civil and business law, philosophy, economics, and scientific works by Russian scientists on civil and business law.

In particular, the works by Zinchenko, Iontseva, Ioffe, Kavelin, Karelin, Kleandrov, Komissarova, Krashchenko, Kolinichenko, Kulagin, Laptev, Popondopulo, Svit, Stepanov, Telyukina, Tkachev, and others were used.

The works by the following authors: Alferov, Izuymov [1], [2], Sadykova, Liman, Korenkova, Ignatova, Bogdanova, Kilin, Korenkova, Samoylova, Shestakova, Steinfeld R., Steinfeld S., Weiss, Novolodskaya [3], Shokhnekh [4] also played an important role in the study.

Practical data on insolvency cases of the Supreme Arbitration Court of the Russian Federation and federal arbitration courts of districts were also studied: Central, North-Caucasian, Western-Siberian, Ural, Far East, arbitration courts of the Tyumen Region, Khanty-Mansi Autonomous District; Yamalo-Nenets Autonomous District.

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The work also analyzes a wide range of international documents of universal and regional nature, such as international treaties, resolutions of the UN General Assembly and the UN Security Council, documents of international conferences, reports of the UN Secretary-General, reports and other documents adopted within the framework of the UN Economic and Social Council, the UN Commission on human rights, as well as treaty bodies on human rights.

## III. PROPOSED METHODOLOGY

### A. General Description

The object of the study was the social relations that develop in the event of a crisis of payments in the activities of an economic entity at the pre-trial stages.

The subject of the study is the rules of law governing the procedure and conditions of pre-trial prevention of insolvency of an economic entity; modern scientific understanding of the features of this phenomenon, the definition of the concepts of pre-trial procedures, activities, legal status of participants, as well as the practice of implementation of bankruptcy law.

The methodological basis of the study comprises the general scientific dialectical method of cognition, which allows

considering the institutions of law in the relationship, integrity, and development. Special and specific scientific methods are used: historical and legal, formal and logical, the method of comparative law.

### B. Algorithm

The scientific novelty of the work is in the fact that one of the first comprehensive studies of the nature of pre-trial prevention of insolvency of an economic entity from broad paradigm concepts corresponding to modern scientific rationality is conducted. This created an integral legal structure that can be used to prevent and eliminate the financial difficulties of economic entities at the pre-trial stages.

Figs. 1 and 2 show a diagram of all stages of bankruptcy. The task was to consider the stage of pre-trial rehabilitation. As can be seen from the scheme, successful anti-crisis procedures will allow the organization to return to normal and eliminate the negative manifestation of bankruptcy. The ultimate goal of pre-trial procedures is to conclude a settlement agreement on acceptable terms between the parties to the process.

### C. Flow Chart

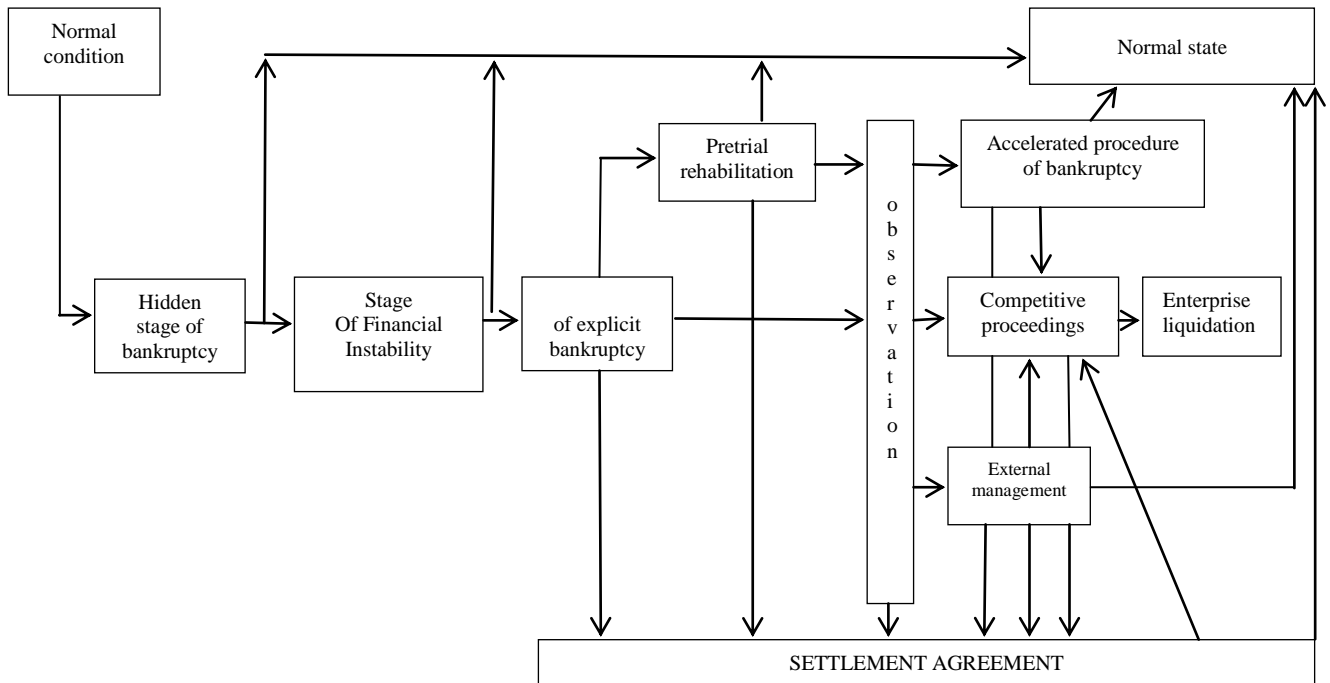
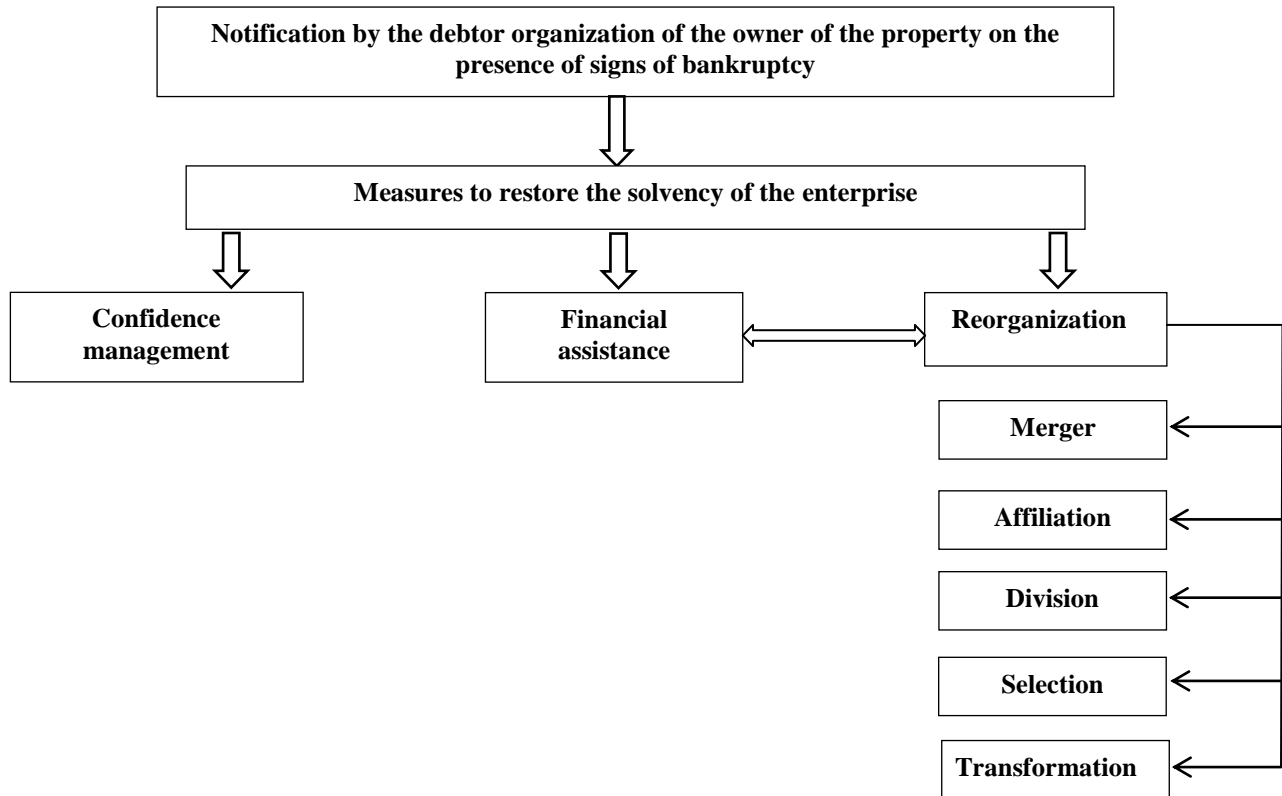


Fig. 1. Stages of bankruptcy



**Fig. 2. Principal procedure of pre-trial rehabilitation**

Successful implementation of these procedures will have positive impact on the Russian legislation on pre-trial rehabilitation of legal entities. As a result of the study, there will be proposed some conclusions and recommendations required for the practical implementation of the goals and objectives of the work.

#### IV. RESULT ANALYSIS

##### A. Historical and Legal Review of Pre-Trial Prevention of Insolvency in Legislation

The current state of Russian legislation makes it possible to unambiguously determine the fact that the number of legal regulations of pre-trial prevention of bankruptcy is not great. At the same time, the institution of insolvency occupies a significant place in the system of legislation, is dynamically developing and improving. Insolvency rules are actively applied and are essential for practice, which generates attention from science.

Pre-trial prevention of bankruptcy, apparently, can be considered as an integral part of the institution of insolvency as a whole, because it has the same goals, a similar range of subjects and the content of relations among them, and is aimed at ensuring the stability of civil turnover.

This thesis is supported by the structure of legal regulations on insolvency. So the Federal law "On Insolvency (Bankruptcy)" No. 127-FZ as of October 26, 2002 (hereinafter the Law) contains provisions governing the conduct of pre-trial rehabilitation; the Federal law "On Insolvency (Bankruptcy) of Credit Organizations" No. 40-FZ as of February 25, 1999 covers measures on prevention of bankruptcy of credit institutions.

Thus, it can be argued that the history of the development of legislation on pre-trial prevention of insolvency is a segment

of the history of the development of bankruptcy legislation. At the same time, the rules on pre-trial prevention of bankruptcy, if they ever existed in a separate time period, had never been of significant importance in the business environment.

It is difficult to find an exact answer to the question of when the institution of insolvency first appeared and developed in the history of human society. Obviously, some economic, trade relations are inherent in society, and the development of these relations at some stage inevitably leads to the problem of repayment of debt, which in the law of ancient human communities and states was solved by foreclosing on the identity of the debtor (from sale into slavery to dismemberment of the debtor's body).

In the Russian legislation, insolvency is first mentioned in the first known source of old Russian law – Russkaya Pravda, but it was not developed in the future. It practically disappears in the middle ages and revives only in the 18th century.

This historical fact, however, allows concluding that the institution of insolvency in the historical retrospective of Russian legislation has certain distinctive features and milestones. Interesting points about pre-trial prevention of bankruptcy are also found in [5].

Let us consider the general features of the Russkaya Pravda.

Russkaya Pravda is the first monument of Russian law; it is obvious that the insolvency rules do not occupy much space here. Nevertheless, these provisions were sufficient and exhaustive for their time. In addition, there is no doubt about their successful practical application. First of all, insolvency (bankruptcy) had the purpose of satisfaction of creditors' claims.

At the same time, the recovery was addressed directly to the identity of the debtor; there was a sequence of satisfaction of claims and there was provided the division of insolvency into ordinary and malicious.

It is obvious that this rule is aimed at pre-trial prevention of bankruptcy, and therefore, it can be concluded that the first appearance of this kind of rules in the Russian legislation was in the Code of Laws of Ivan III. It is also interesting that this rule is similar to the provisions of French law, the insolvency system of which is currently the only example of radically for-debtor legislation.

Thus, some elements of insolvency (bankruptcy) first appear in the ancient Russian legislation, but it is too early to talk about the emergence of the relevant legal institution. These grounds are too small; besides, since they had hardly appeared and did not receive further development, they practically disappeared from the Russian law for quite a long period, in general, for about five hundred years. The reasons for this incident may be hidden in the peculiarities of the formation and development of Russian society. Russia is quite isolated from European civilization, closed. At the same time, it was constantly exposed to invasions from the East. These economic and social conditions do not create the ground for the development of insolvency relations, as they entail constant disruption of the stable development of trade, credit, and this is what creates favorable conditions for the development of insolvency in Europe.

Thus, in the legislation of Italy, Germany, and France in the middle ages, there was a breakthrough in the development of insolvency and the corresponding legal institution was born. Creditors, feeling the financial futility of foreclosure on the personality of the debtor or its physical destruction, begin to strive for the fullest possible satisfaction of their claims at the expense of the debtor's property; thus, the emphasis is shifted towards the collateral security of any debt. Penalties of a personal nature are limited to the dishonest behavior of the debtor.

In Russia, the institution of insolvency in its modern form comes and takes its place in capitalist relations only in the 18th century.

The clerical-codification direction, according to Shershenevich, implied the development of competitive Charters. "In 1740, the Senate passed the bankruptcy statute, but it was not applied in life, and even its legal force was ignored. Subsequently, the Senate found it possible to refer to the "lack of a bankruptcy statute in Russia". As a result, in the second half of the 18th century, there were several projects that have not received the force of law. These were bills of 1753, 1763, 1768" [6].

Thus, the 18th century in the history of Russian bankruptcy law occupies a special place. During this period, the institution of insolvency becomes really popular and begins to develop dynamically after hundreds of years of oblivion. The result is the bankruptcy statute of 1800.

As one can see, Shershenevich saw in this provision a way to prevent bankruptcy. Indeed, a pre-trial transaction between the debtor and creditors can be seen as debt restructuring or, given the variety of scientific approaches to the definition of pre-trial rehabilitation, a prototype of the latter. In other words, the bankruptcy statute of 1800 was undoubtedly a

significant step in the development of both the entire insolvency law and the legislation on pre-trial prevention of bankruptcy. It is only regrettable that although the institution of bankruptcy itself has significantly changed and improved over the past two centuries, the legal rules on the prevention of bankruptcy were not increased in number, and their content practically remains at the same level.

In 1832, the Charter about trading inconsistency was adopted. Its main significance is that it further differentiated insolvency into commercial and noncommercial since it actually replaced the first part of the Charter of 1800, devoted to the bankruptcy of persons entered into the commercial class. The second part, concerning nobles and officials, continued to operate. The Charter of 1832 did not bring substantial, fundamental changes. Practically, the bankruptcy legislation had not been subject to any major changes until 1917; however, it had evolved and improved [7].

It should be further noted that the above-mentioned features of the Charter of 1800 as a whole are the characteristics of the entire institution of insolvency in the pre-revolutionary Russian legislation. These basic principles remained unchanged until 1917. At the same time, work on optimization of the functioning of insolvency, detail, and concretization of rules had been constantly conducted. Drafts of new charters and other rules were created and considered. In general, at the beginning of the 20th century, in the domestic legislation until 1917 bankruptcy or commercial insolvency was considered a "position of the merchant recognized by the court, when the entire amount of his property was not enough for full payment of debts. Insolvency could be unhappy, careless (simple bankruptcy) or fraudulent (malicious bankruptcy)" [8].

Regarding the pre-trial prevention of bankruptcy, it should be mentioned that in pre-revolutionary history, this phenomenon was not known to the law. Some rules that affected this issue in one way or another were lost in the insolvency system, which generally did not pay attention to the problems of possible prevention of bankruptcy and restoration of the solvency of a potential debtor.

1921 can be considered the beginning of the next stage in the development of Russian insolvency law when the country introduced a new economic policy. Its main features were such that the institution of insolvency as a whole became necessary, so the Civil Code of the RSFSR, adopted in 1922, contained rules on insolvency. However, according to modern scientists, certain advantages were given to state enterprises and institutions compared to private ones; this provision was justified by scientists. The rejection of the discretionary nature in the assignment of officials in a competitive process should be noted. Creditors were completely excluded from participation in the process, including the selection of managers. All such issues were resolved by government agencies, i.e. specific officials.

Indeed, if during the period of the new economic policy in the economy of the RSFSR there were any market elements, at the end of this short stage, they finally disappeared. Together with them, the institution of insolvency has disappeared from the law. It was not in demand in the administrative and planned economy and therefore, was forgotten for several decades.



The Soviet period in the history of Russian insolvency law is a kind of black hole. It had not been developed. By the end of the 20th century, it remained at the same level as a hundred years ago.

However, the development of the state and society as a whole continued.

This was an extremely interesting period in the history of Russia. There were many bodies and structures involved in the control and supervision of the distribution of products. These structures also monitored the financial condition of economic entities. In these circumstances, it is possible to talk about the existence of monitoring of financial and economic activities, which today is one of the main tools of pre-trial prevention of insolvency of an economic entity [9].

The beginning of the modern period of development of the insolvency law can be considered December 25, 1990, when the law of the RSFSR "On Enterprises and Entrepreneurship" mentioned insolvency for the first time after a long break; paragraph 3 of Article 24 said: "The enterprise which is not fulfilling the obligations according to calculations can be declared insolvent (bankrupt) according to the legislation of the RSFSR in a judicial order". It is obvious that this rule was just a declaration – there was no mechanism for its implementation. Nevertheless, it became the basis that determined the vector of further development of domestic legislation and, at present, it is quite obvious that bankruptcy is one of the most dynamically developing, unstable, problematic and at the same time necessary institutions of modern Russian law. 15 years later, the third law on bankruptcy is in force, and in pre-revolutionary Russia, in fact, there were only two.

The first law of new Russia, dedicated to the regulation of bankruptcy relations, appeared on November 19, 1992. The period of its operation was about five years. In scientific research, its position was perceived ambiguously. This fact is not surprising in general; on the contrary, it looks natural: it is difficult to assume that after nearly a hundred years of neglect of insolvency, lack of practice and theoretical development, there was a regulation of a high level of legal writing.

Referring to the direct content of the 1992 Law, it is necessary to highlight the main characteristics of the institution of insolvency, as well as some provisions interesting from the point of view of pre-trial prevention of bankruptcy. One of the main points – the criterion of bankruptcy – is nonpayment. According to Art. 1, insolvency (bankruptcy) of the enterprise is understood as inability to satisfy requirements of creditors on payment for goods (works, services), including inability to provide obligatory payments in the budget and off-budget funds, in connection with excess of obligations of the debtor over its property or in connection with the unsatisfactory structure of balance of the debtor. It is interesting here that the concept of an unsatisfactory balance sheet structure contained in the Law did not allow distinguishing the criteria of such a structure. In this regard, a year and a half after the entry into force of the Law, its provisions were specified in the Decree of the Government of the Russian Federation dated May 20, 1994 No. 498 "On Some Measures for the Implementation of the Insolvency (Bankruptcy) Legislation of Enterprises".

The 1992 law also established the division of bankruptcy proceedings into three types: reorganization, liquidation, settlement agreement and established jurisdiction of bankruptcy cases to arbitration courts. At the same time, reorganization procedures (external management and rehabilitation) have always been carried out within the framework of the judicial process, under the supervision of the court, but the liquidation of the debtor (bankruptcy proceedings) could be extrajudicial (Section VII of the law). In addition, the Law provided the possibility of out-of-court settlement of disputes between the debtor and creditors through negotiations and the granting of deferral or installment payments to the debtor. The result of such a procedure could be the continuation of the debtor's activities (Article 50 of the law). Article 6 of the Law established the obligation of pre-trial settlement of the dispute by sending a claim to the debtor and providing a period for repayment of the debt.

Thus, the 1992 Law undoubtedly contained a number of provisions aimed at pre-trial prevention of bankruptcy, but, firstly, these provisions were not originally intended to effectively and timely prevent the occurrence of insolvency, and secondly, their practical application in the conditions of reality did not allow achieving such a result. After all, with the appearance of the Law of 1992 in Russia, the formation of the institution of insolvency only began; there were the first practice and theoretical development. The implementation of the insolvency Law of 1992 did not begin immediately after its entry into force. Those who had to execute it were not ready for the application of the law. Considerable preparatory work was required to establish the necessary institutional and legal prerequisites. In addition, the Law of 1992 came into force before the adoption of the new Constitution and the Civil Code, so after five years of its operation, a new Federal law No. 6-FZ "On Insolvency (Bankruptcy)" as of January 8, 1998 was developed and adopted; it entered into force on March 1, 1998.

The new legal regulation significantly changed the characteristics of the domestic institution of insolvency. This regulation, compared to the previous one, was much more voluminous, logically consistent and more clearly structured. First of all, it changed the criterion of bankruptcy. Now insolvency, i.e. bankruptcy is referred to as the recognized by the arbitration court or declared by the debtor inability of the debtor to satisfy the claims of creditors on monetary obligations and (or) to perform the obligation to pay obligatory payments if these obligations are not performed by it within three months from the date of their becoming due. These circumstances are the grounds for initiating legal proceedings. The provisions relating to bankruptcy procedures have significantly changed. The monitoring procedure has been added (the main goal was to ensure the safety of property); the procedure for the rehabilitation of external management (now it is the only judicial procedure aimed at restoring solvency) and bankruptcy proceedings has been regulated in more detail. For the first time, there are rules establishing the legal status of the arbitration manager.

For the purposes of this study, it is significant that the Law of 1998 for the first time contains such words as measures to prevent the bankruptcy of organizations,

while Chapter II is called "Prevention of bankruptcy"; in reality, it contains two articles.

The first indicates the range of subjects (founders (participants) of the debtor – legal person, owner of the property of the debtor – the unitary enterprise, federal executive authorities, executive authorities of constituent entities of the Russian Federation, bodies of local self-government) and requires them to take timely measures to prevent bankruptcy. The second is devoted to pre-trial rehabilitation (in the new law, rehabilitation is a pre-trial procedure) and defines the latter as financial assistance to the debtor by third parties. Within the meaning of the Law, the range of these persons is not limited, but first of all, they include owners, founders, and creditors [10].

The introduction of the chapter on the prevention of bankruptcy in the new Law seems to indicate the emerging need of the business environment for such rules. On the one hand, such provisions of the Law are a significant step forward; on the other hand, the practical implementation of the obligation to take preventive measures is impossible. There is no mechanism, and the conditions of reality during the period of application of the Law become unacceptable for such actions. The institution of insolvency is turning into a tool for robbing business, "redistribution of property".

By the beginning of the 21st century, this fact had virtually become universally recognized. This is said by all, including famous scientists.

In general, with regard to the Federal insolvency law of 1998, it seems legitimate to conclude that this law was indeed a significant step forward in the development of domestic legislation on bankruptcy; however, due to the specifics of the period of development of Russia at the turn of the 21st century, it was inconsistent with the general condition of Russian society, the judicial system, and state structures. In this regard, on October 26, 2002, the President of the Russian Federation signed a new Federal Law No. 127-FZ "On Insolvency (Bankruptcy)". This law is also perceived ambiguously. It did not become a panacea for all the problems associated with the bankruptcy of organizations. Despite the introduction of significant changes, this is still a valid legal regulation, and therefore, the consideration of its characteristics within the framework of the history of domestic legislation is unacceptable. It is believed that the historical and legal review of the legislation on pre-trial prevention of bankruptcy can be finished by the characteristics of the 1998 Law.

At the same time, the history of pre-trial prevention of insolvency (bankruptcy) as a phenomenon, as a certain sphere of social relations, which are in the dynamics and constant development, is not limited only to the publication and implementation of legal regulations and their content in different periods of time. It is also the activity of a certain circle of people: individual entrepreneurs, citizens, legal entities, and state bodies.

In this situation, the existence of a special state body in the Russian Federation for more than ten years is of particular interest. Its main tasks were, in particular: development and implementation of measures for financial rehabilitation and restructuring of insolvent organizations, as well as the implementation of state policy to prevent the bankruptcy of persons engaged in business activities in accordance with

civil law. Here, the Federal Service for Financial Recovery and Bankruptcy (hereinafter referred to as the FSFR) should be noted, first established by the Council of Ministers – the Government of the Russian Federation No. 926 on September 20, 1993.

The establishment of such a body seems to have been due to the historical period of development of the country as a whole, when, as a result of the transition from one economic system to another, the vast majority of enterprises previously receiving significant funds from the state, as a result of their inability to participate in market relations came to financial collapse without this support. In such a situation, the state, through the creation of the above service, was striving to rectify the situation and, if possible, to ensure the financial recovery of at least the largest enterprises where the state was present as the owner or founder [11].

In reality, the FSFR was designed to monitor the financial condition of economic entities on the basis of the provided financial statements, calculate some indicators of solvency and keep records of solvency.

According to the results of monitoring, the FSFR also developed proposals for the government of the Russian Federation on the financial recovery of enterprises. The real results of such work were far from the tasks prescribed in the relevant decision of the Government of the Russian Federation.

The result of the activity was the abolition of the FSFR by decree of the President as of 09.03.2004 No. 314 with the transfer of the function of adoption of legal regulations in the established field of activity to the Ministry of economic development and trade, and the function of representing the interests of the Russian Federation to creditors in bankruptcy proceedings – to the Federal tax service. Thus, the state refused from such monitoring and participation in the financial recovery of economic entities, however, in general, the issues of pre-trial prevention of insolvency have not been excluded from the sphere of state interests, as it will be seen further.

In general, any assessment of the activities of the public insolvency authority is not the purpose of this study. It is the fact of such activities in Russia that is of interest.

### **B. The Modern Stage of Development of Pre-Trial Prevention of Insolvency of an Economic Entity in Russia**

The current period of development of legislation on pre-trial prevention of bankruptcy of economic entities is quite interesting. Thus, at first glance, the number of legal regulations devoted to these issues is disproportionately small; however, with a closer look at the regulatory framework, it becomes obvious that such a conclusion is premature.

Indeed, at first glance, the rules on pre-trial prevention of bankruptcy of organizations are contained in only three federal laws: as of February 25, 1999 No. 40-FZ "On Insolvency (Bankruptcy) of Credit Institutions", as of July 9, 2002 No. 83-FZ "On Financial Recovery of Agricultural Producers", as of October 26, 2002 No. 127-FZ "On Insolvency (Bankruptcy)". However, at the same time, legal norms that are aimed at preventing the deterioration of the financial condition of

economic entities can be found in other existing legal regulations that, at first glance, are not related to the institution of insolvency.

So, part 1 of Article 73 of the Federal law "On Joint-Stock Companies" No. 208-FZ as of December 26, 1995 establishes restriction on redemption by a joint-stock company of the ordinary shares placed by it if, at the time of their acquisition, the company meets the criteria of insolvency (bankruptcy) according to legal regulations of the Russian Federation on insolvency (bankruptcy) of the enterprises or the specified criteria appear as a result of acquisition of these shares. This restriction is also applied to preferred shares. Thus, it is obvious that the current legislation on the legal regulation of general issues of organization and activity of economic entities (business partnerships and companies) does not ignore the problem of ensuring the stable financial condition of such entities [12].

Given the fact that such examples are numerous (the establishment of a special order for the conclusion of large transactions, transactions with interest in one way or another aims to minimize the possibility of deterioration, destabilization of the financial condition of society, and therefore, in the end, to prevent its bankruptcy), it can be argued that the prevention of bankruptcy as such is one of the goals of civil law. The issue of the absence at the federal level of a special regulation dealing with these problems is likely to require a solution in the near future. There are real prerequisites for this; for example, when addressing the rule-making of the Government of the Russian Federation over the past ten years, one can find a sufficient number of resolutions, in one way or another devoted to the issues of pre-trial prevention of insolvency.

The list of such regulations as a whole includes about a hundred, which indicates the current practice of the state aimed at supporting individual economic entities, improving their financial condition through debt restructuring, as one of the measures of pre-trial prevention of insolvency [13].

Debt restructuring, in general, is one of the most common ways of pre-trial prevention of insolvency, as evidenced by the presence at the federal level of a law entirely devoted to restructuring. This is the Federal Law as of July 9, 2002 No. 83-FZ "On Financial Recovery of Agricultural Producers". This regulation defines the procedure for restructuring, the essence of the restructuring agreement, and its essential terms. Not all of its provisions are unambiguous and perfect; there are also issues of its practical application, which will certainly allow referring to this legal regulation in the future in the framework of this study more than once. In the meantime, the fact of its existence as a confirmation of a significant step forward in the development of domestic legislation on pre-trial prevention of insolvency should be mentioned. This is the first attempt to regulate the phenomenon under study by an independent legal regulation at the level of federal law.

Also, the issues of pre-trial prevention of insolvency are regulated in sufficient detail by the Federal Law as of February 25, 1999 No. 40-FZ "On Insolvency (Bankruptcy) of Credit Institutions". Thus, Chapter II of the Law is fully devoted to the financial recovery of a credit institution. Article 7, among others, lists financial recovery measures:

providing financial assistance to a credit institution by its founders (participants) and other persons; changing the structure of assets and liabilities of a credit institution; changing the organizational structure of a credit institution; bringing into line the size of the authorized capital of a credit institution and the share of its own funds (capital). The following articles describe these measures, their content, and procedure in more detail. Article 13 regulates the planning of financial rehabilitation measures. Articles 14 and 15 deal with liability for breach or failure to comply with the requirements of Chapter II. It should be mentioned in particular that the chapter underwent significant changes in 2004 when the considered law was amended. This fact once again testifies to the increased attention to the problems of pre-trial prevention of insolvency on the part of the legislator.

Against this background, the provisions of the Federal Law as of October 26, 2002 No. 127-FZ "On Insolvency (Bankruptcy)" look outdated, because it contains only two articles on pre-trial prevention of insolvency. Their essence resolves into the following: firstly, it establishes the obligation of the potential debtor's managers to inform the founders of the occurrence of signs of bankruptcy; secondly, the founders have a general obligation to take measures to prevent bankruptcy; thirdly, it establishes the possibility of taking such measures by creditors or other persons under an agreement with the debtor; fourthly, it implies the possibility of providing financial assistance to the debtor by all of the above persons [14].

It is necessary to consider the fact that if one compares legal regulations devoted to the pre-judicial prevention of insolvency of the economic entity contained in all three laws on bankruptcy operating in the Russian Federation, only the rules of the first of these acts (the Law of the Russian Federation as of November 19, 1992 "On insolvency (bankruptcy) of enterprises") have a significant difference. Provisions of the Federal Laws No. 6-FZ as of January 8, 1998 and No. 127-FZ as of October 26, 2002 "On Insolvency (Bankruptcy)" concerning the prevention of bankruptcy are almost completely identical.

The law of 1992 provided for the possibility of out-of-court procedures, expressed in the negotiations of the debtor with creditors, by the results of which, the decision to continue the activities of the debtor or to carry out its voluntary liquidation was adopted. The procedure and conditions of such negotiations were not regulated by the law, and it was left to the discretion of the participants. In the event of a decision to continue the debtor's activities, its solvency could be restored only through the restructuring of its debt on the basis of an agreement with creditors that established deferrals, installments or discounts on the amount of the debt.

The conclusion is obvious that all three bankruptcy laws that existed in new Russia did not contain a developed regulatory framework governing pre-trial prevention of insolvency, but did not leave it unnoticed. At the same time, since 1998 there have been no changes in the regulation of this problem, although the existing provisions are obviously outdated and are not applied in practice.

At the end of the 20th and the beginning of the 21st centuries, in the Russian legal science, interest



in the problems of insolvency increased primarily due to the significant amount of practice and imperfection of the current legislation.

Over the past fifteen years, three federal laws have been adopted on the problem, as well as special laws (for example, on the insolvency of credit institutions). The amount of scientific articles, monographs devoted to various aspects of bankruptcy is large; there are also Ph.D. and doctoral theses. There are also studies directly focused on the problems of prevention of insolvency, although their number in the total amount of research on the problem of bankruptcy today is small.

Most of the research is devoted to general issues of insolvency, the nature of bankruptcy, the status of the arbitration manager, insolvency procedures, participation of creditors in bankruptcy proceedings, their status, position, etc. In accordance with the purpose of this study, the works devoted to general theoretical issues of the essence of bankruptcy and the definition of basic terms are the most interesting, since the general provisions of the institution of insolvency form the basis for the development of legislation on pre-trial prevention of insolvency of an economic entity [15].

The legal relationship between the debtor and creditors is also not deprived of the public aspect, especially in respect of pre-trial prevention of insolvency. First, there is a plurality of creditors in these relations, and the state represented by a representative authority may be one of the creditors. If the debt to the budget is large, there is significant public interest. Second, in the case of insolvency of a city-forming enterprise (for example), its collapse will affect the interests of the entire population. The degree of publicity is preserved. Therefore, in the author's opinion, the public nature of insolvency relations is not determined solely by the participation of the arbitration court.

Indeed, there is a shift in emphasis towards the restoration of solvency. At the same time, the current practice is that the number of debtors who restored solvency in the course of judicial procedures is negligible. There are also a small number of creditors whose claims were fully satisfied in a bankruptcy case. These circumstances give rise to the study of the possibility of resolving the problem of nonpayment of an economic entity at the pre-trial stage, with the participation in this process of creditors, independent mediators, experts on crisis management, etc.

Today, if a business entity is brought before the arbitration court for insolvency, it will be liquidated (there are only some exceptions when solvency is restored). It is obvious that the introduction of new rehabilitation procedures, such as financial recovery, cannot affect the situation.

Unfortunately, in practice, the bankruptcy process is initiated by creditors in the case when the debtor already has a multimillion debt and has lost most of the property. In such circumstances, the "anti-crisis" specialist is no longer able to help. According to the author, insolvency can be prevented and overcome only before the trial. This is possible provided that the debtor monitors its financial condition and responds in a timely manner to emerging problems, as well as in cooperation with creditors.

However, the existing research on the problem, in fact, only "sets a standard" for further work in this direction. Despite the urgency of the problem, it is very little developed. There is no unity of terminology, clear legal structures, legal means to prevent bankruptcy, a holistic concept of legal regulation of these relations [15].

Statements and proposals to improve the legal regulation of pre-trial prevention of insolvency are rare today. They have only been pronounced but have not yet been discussed, appreciated and perceived in practice.

According to the authors, it is an urgent problem to determine the range of persons in respect of which it is possible to prevent bankruptcy. To address this issue, first of all, it is necessary to determine who can be bankrupted today, who, what entities are exposed to the threat of insolvency today. After all, bankruptcy can be prevented only for those who are threatened by it. The current bankruptcy law contains a legal definition of the debtor. This is a citizen, including an individual entrepreneur, or a legal entity that has proved unable to satisfy creditors' claims for monetary obligations and (or) perform the obligation to pay mandatory payments within the period established by this federal law.

In this case, under certain circumstances, any legal entity, a citizen, including an individual entrepreneur, can be declared bankrupt.

Without a doubt, each of these actors is able to take measures to avoid the unpleasant status of bankrupt. In this regard, pre-trial prevention of their insolvency can be considered. However, at the pre-trial stages, it is not quite correct to talk about debtors, because they at that time might not have debts to anyone, but take measures to prevent bankruptcy. This is why the term "debtor" is not applicable to the scope of pre-trial prevention.

However, cases of bankruptcy of citizens who are not individual entrepreneurs are not inherent in modern Russia. Is it required to talk about preventing their bankruptcy? For this reason, it is believed that the term "debtor" is not applicable in this study (except in some special cases).

In this regard, the range of subjects includes legal entities and individual entrepreneurs. As for the use of a single term (in accordance with the purpose of scientific research), the authors assume the use of the term "economic entities". This term is primarily used in antimonopoly legislation; it is also used in some scientific studies. Its application is due to the fact that this term most fully outlines the range of entities in respect of which measures to prevent bankruptcy can be taken. The opinion of Belykh is quite fair: pointing to the differences between this term and the term "business entities", he, in particular, notes: "They relate to each other in the same way as the economic and entrepreneurial activity. Economic entities do not always acquire the status of entrepreneurs. For example, nonprofit organizations usually do not do business, although perform the economic activity" [16].

Thus, the use of the term "economic entity" will successfully bypass some conflicts of terms. The authors believe that any legal entity can be declared bankrupt under the current law, but since not any legal entity can be considered a subject of business law, the term that will unconditionally unite commercial and noncommercial organizations in this respect is



more acceptable for the designation of the subject of insolvency.

The authors consider as universal the term "economic entity", which is a collective concept and combines individual entrepreneurs and legal entities.

1. As a result of generalization of existing scientific approaches to the definition of terms related to the problem of research and analysis of legislation, it is proposed to distinguish between prevention of insolvency and prevention of bankruptcy, which makes it possible to determine the status of an economic entity as insolvent in judicial proceedings (except for bankruptcy proceedings). At this stage, it becomes possible to prevent its bankruptcy in the course of rehabilitation and monitoring procedures. In these cases, before the initiation of bankruptcy proceedings, upon the occurrence of the insolvency of an economic entity or the threat of insolvency, pre-trial prevention of insolvency of an economic entity is conducted.

2. The necessity of improvement and unification of terminology in the sphere of legal regulation of relations of pre-trial prevention of insolvency is argued. The authors propose the use of the term "pre-trial prevention of insolvency of an economic entity". It is proposed to define it as the actions of an economic entity (legal entity, individual entrepreneur), performed by it independently or in cooperation with creditors, third parties, aimed at pre-trial prevention of insolvency (prevention of improper performance of monetary obligations to creditors), and when it occurs, at pre-trial restoration of solvency.

3. The necessity of using independent out-of-court procedures for pre-trial restoration of the solvency of an economic entity is justified. For pre-trial stages, it is proposed to define such procedures as a set of consistent (and if necessary, simultaneous) measures applied to an economic entity in consultation with its creditors in order to eliminate the inherent signs of bankruptcy, without initiating bankruptcy proceedings. This will make it possible to more clearly define the status of an economic entity with signs of bankruptcy before initiating bankruptcy proceedings against it and to regulate its relations with creditors within the framework of restoring its solvency.

4. As a result of the analysis of the study of the development of scientific thought, legislation, practice of law enforcement, the concept of "pre-trial rehabilitation" is formulated as follows: this is an independent pre-trial procedure in which the interested parties (subjects of rehabilitation), through the conclusion of transactions (one or more – at their discretion), provide the economic entity with the opportunity to release additional funds to eliminate its inherent signs of bankruptcy, without initiating bankruptcy proceedings.

5. The necessity of unification of definitions of the term "debt restructuring" is justified. The authors propose to define this phenomenon as an independent extrajudicial procedure, in which the debtor and all its creditors, on the basis of their free will, through negotiations, decide to establish common conditions and terms of repayment of the debtor's debt to each of the creditors with the provision of a single time period for settlements and further restoration of solvency. The result is an agreement between the debtor and

its creditors on debt restructuring.

## V. CONCLUSION

Summing up the review of the domestic legislation on pre-trial prevention of insolvency, the following conclusions shall be made.

Russian legislation on insolvency (bankruptcy) has a history of development of about 1 thousand years. At the same time, pre-trial prevention of bankruptcy of economic entities was somehow manifested during this period, but did not receive the proper level of attention and degree of development.

The most dynamic development of legislation on pre-trial prevention of insolvency is beginning now, which is due to the development of the business environment and the gradual increase in demand for the practice of legal regulations of this kind due to an increase in interest in the preservation of business.

The legal regulations devoted to pre-trial prevention of bankruptcy are now beginning to be isolated in separate regulations of various hierarchical levels. This suggests the urgent need to create in the near future a full codified regulation, fully aimed at addressing these issues at the level of federal law.

At the present stage of development of the Russian legal science, the study of pre-trial prevention of insolvency is of particular relevance. This phenomenon has been studied to a very small extent. The range of the issues to be resolved is quite wide, which is illustrated by the lack of a single term to refer to the range of persons for whom pre-trial prevention of insolvency is possible.

In contrast to the Russian legislation, the legal regulation of pre-trial prevention of insolvency is present in the legislation of most foreign countries, regardless of its focus on ensuring primarily the interests of creditors or a debtor in the bankruptcy process.

In the legislation of most foreign countries, the legal rules on pre-trial prevention of insolvency are included in the regulations governing the insolvency (bankruptcy) of economic entities, that is, they are part of the institution of insolvency and do not form an independent unit.

The legislation of most foreign countries has various means to ensure pre-trial prevention of insolvency.

The current situation in the Russian practice of withdrawal of assets of the debtor in the pre-bankruptcy period allows considering the possibility of borrowing some foreign provisions and bringing them into domestic legislation.

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