Chapter 15

Corporate Governance in **Groups** of **Companies**

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The Chairman's Checklist

- ✓ Is the company part of a parent-subsidiary structure? Is the parent company's Supervisory Board aware of its role and, in particular, of its responsibilities in such structures?
- ✓ Is there economic justification for establishing subsidiaries and dependent companies?
- ✓ If the company is a parent company, how does the Supervisory Board ensure that it oversees the management of subsidiaries? Are binding instructions of the parent to the subsidiary legally and economically justified?
- ✓ How does the Supervisory Board of the parent company make sure that minority shareholders of subsidiaries are treated fairly?
- ✓ How does the Supervisory Board of the subsidiary ensure that the rights of its minority shareholders are not violated by the parent company through related party transactions and other mechanisms?
- ✓ Do all directors fully understand the legal and economic implications of holding structures and Financial and Industrial Groups?

Companies often adopt complex structures in response to legitimate business needs. Some companies create identifiable sub-divisions, i.e. representative offices or branches.[1] Others establish or acquire participation in yet other companies, creating

[1] Civil Code (CC), Article 55, Law on Joint Stock Companies (LJSC), Article 5, Clause 1. The decision to establish representative offices/branches is a strategic decision, taken by the Supervisory Board. Representative offices represent and protect the company's interests, while branches may fulfill additional business functions. Representative offices/branches have no independent legal personality. This has a number of implications. For one, the manager of the representative office/branch is a part of the management structure of the company, and should be appointed by the company's Executive Board. The manager's authority is defined in special by-laws, the power of attorney issued by the company, and the employment contract with the manager. In addition, the representative office/branch is subject to the same internal control procedures as the company, which is of particular importance since the company is liable for the actions of branches/representative offices.

subsidiaries or dependent companies with a separate legal existence. In doing so, they create a group of companies. Either way, the decision to diversify the company's structure has important governance implications.

While complex business structures may serve legitimate purposes, cross-shareholdings, pyramid structures, and other arrangements can make the company difficult to understand for shareholders and other investors. Special vigilance on the part of the Supervisory Board is called for since such structures have been used extensively to expropriate and circumvent the rights of (some) shareholders.

This chapter draws attention to the corporate governance and legal implications of groups of companies, including parent-subsidiary relations, holdings, and Financial and Industrial Groups (FIGs).

A. General Provisions on Groups of Companies

1. Relationships Between Companies

Companies set up or acquire control in other companies for a variety of legal and economic reasons. These include diversifying business operations, complying with legal and administrative requirements, enjoying the limited liability available to shareholders (of the parent), or identifying assets in separate legal entities for the purposes of secured borrowing. In such cases, companies remain independent legal personalities, with their own charter, governing bodies, and charter capital. Relationships between companies can vary in terms of:

- **The extent of share participation.** A Company can hold small or large blocks of shares in the charter capital of another company. Companies can further have reciprocal holdings in each other. Alternatively, companies may not have any share participation whatsoever, but base their relationships on contracts granting certain control rights.
- **The degree to which companies integrate or cooperate in their businesses.** Companies can be economically dependent on each other with varying degrees of intensity. This holds particularly true for different areas of

decision-making, such as strategic development, marketing, production, asset management, management of financial flows, human resources, or research and development.

- **Whether the group of companies includes both financial and non-financial institutions.** Groups of companies that include financial institutions may be registered as FIGs. Other groups may take the form of holdings.
- **Whether the companies are a part of a wider network of legal entities and the degree of complexity of this network.** Companies can be organized "vertically," that is with one parent company at the top. Such groups are often referred to as "holding companies." When there are several layers of holding companies, they are referred to as "pyramids." Companies can also be organized "horizontally," that is with several parent companies.

Best Practices: The EU defines groups of companies in its Seventh Company Law Directive on Consolidated Accounts.[2] Two basic types of relationships exist: vertical and horizontal.
Vertical control relationships exist when:

1. Company (A) controls the majority of the voting rights in Company (B);
2. Company (A) is a shareholder in Company (B), and has the right to appoint and dismiss the majority of the Supervisory Board members of Company (B);
3. Company (A) exercises "dominant influence" over Company (B) by means of a contract;
4. Company (A) exercises "dominant influence" over Company (B), by virtue of a provision in the company's charter;
5. Company (A) controls the majority of shares as a result of an agreement with other shareholders of Company (B);
6. Company (A) exerts "dominant influence" over Company (B) by means not mentioned above; or
7. Company (A) manages Company (B) on a unified basis.

[2] See http://europa.eu.int/scadplus/leg/en/lvb/l26010.htm.

The Directive identifies two types of associative links that tie together horizontal groups:

1. Companies that are managed on a unified basis; or
2. Companies that are tied together through interlocking directorates.

Cash-flow links and cross-shareholdings are not specifically mentioned in this Directive, although they typically feature in horizontal groups as well.

2. Corporate Governance Issues in Groups of Companies

Relationships between companies serve modern commercial realities; yet they also give rise to some particular corporate governance issues that require management's and, in particular, the Supervisory Board's attention:

- **Lack of transparency of control and economic interdependence of a group of companies.** Complex ownership structures are often used to obscure control relationships between companies, making it virtually impossible to determine when transactions are being conducted in good faith, or when self-dealing, transfer pricing, and similar abuses occur. Just as important are situations in which such structures obscure liabilities or potential risks associated with other companies in the group.

Best Practices: Transparent ownership structures are important prerequisites in both the U.S. and EU. The same should hold true for Russian companies, and the following are some of the best practices for implementing this principle.

- Significant attention is given internationally to the disclosure of holdings and voting power in listed companies. For example, in the U.S., the disclosure of voting blocks in excess of 5% in listed companies is required; in the EU, this requirement is established at the level of voting power in excess of 10%.
- It is extremely important to provide adequate financial information on the economic interdependence of the group of companies. In the EU, for example, the consolidation of group accounts is a legal requirement since the adoption of the Seventh Company Law Directive in 1978. The EU system was recently updated and all listed companies in the EU will need to consolidate their financial reports according to International Financial Reporting Standards as of 2005.

- The EU deems coherent and accurate disclosure of group structure and intra-group relations as a crucial precondition for protecting the rights of shareholders and creditors. Thus, the parent company of each group is to be made responsible for appropriate disclosure practices.
- In addition to the above, the EU is particularly concerned about pyramidal groups that include listed companies, especially those placed on lower levels of the chain of control. In those cases, for example, the recommendation is made for securities markets not to accept for trading shares of holding companies whose sole or main assets are shareholdings in another listed company.

- **Ability of the dominant company to control the decision-making of its subsidiary, contrary to the interest of the subsidiary.** There is a real danger that a dependent company or subsidiary can be made to operate in the interests of the dominant or parent company, to its detriment.

Best Practices: German law, which contains comprehensive regulation on groups, envisages the possibility for a controlling company to issue mandatory instructions to the directors of the controlled company.

- In the case of contract-based groups, the instructions issued can even be to the detriment of the subsidiary as long as the interests of the group as a whole are served.
- The latter condition does not apply in the case of so-called integrated groups, whereby the participation in the subsidiary's capital exceeds 95%.
- With regard to the third category of groups recognized by German law, the *de facto* groups, the parent company cannot issue instructions disadvantageous to the subsidiary without providing compensation. Under this particular group structure, directors of the dependent company are required to prepare a "dependence report," listing the circumstances of its transactions, and disclose this report to the company's External Auditor.

French law accepts the notion of the group's predominance over its members' interests. When making decisions, the parent is thus entitled to take the group's interests into account and is not required to indemnify the subsidiary. However, two exceptions exist. First, the subsidiary may not enter into transactions with other group entities that would jeopardize its solvency. Second, that a certain "*quid pro quo*" between the parent and subsidiary exists, i.e. that a just balance be struck between the burden imposed on the subsidiary and the advantages it receives from its participation in the group.

Similarly, the 2004 OECD Principles of Corporate Governance (OECD Principles) mention that some countries are now moving toward controlling the negative effects [of groups of companies] by specifying that a transaction in favor of another group company must be offset by receiving a corresponding benefit from other companies of the group.[3]

- **The need to protect minority shareholders of dependent companies or subsidiaries against abuse by the controlling powers of the dominant company.** Minority shareholders in subsidiaries or dependent companies may be particularly vulnerable to abuses by controlling shareholders. Subsidiary or dependent companies are not generally publicly quoted, so minority shareholders may not receive full information or have the ability to sell their shares in the market.

Best Practices: Some important areas of concern for companies wishing to follow good corporate governance in terms of minority shareholder protection in groups include:

- Providing minority shareholders with reliable information on the company's management and the actual relations between companies.
- Providing security for the profit interests of the subsidiary's shareholders. Under German law for example, minority shareholders can be offered security in the form of a guaranteed dividend, the amount of which is determined in relation to past or future profits.
- Minority shareholders have the right to withdraw from the company against an appropriate compensation, when the dominant company has acquired 90% (for example, in the U.K.) or 95% (in France) of the company.

- **The need to protect creditors of the dependent company or the subsidiary against fraud or under-capitalization of the subsidiary.** Creditors may also find themselves in a weaker position with respect to their ability to receive

[3] OECD Principles of Corporate Governance, Annotations to Principle II on the Equitable Treatment of Shareholders, Section A.2. See also: www.oecd.org.

the payments that they are due. Some potential responses are mentioned below:

Best Practices: Creditors of the subsidiary could be protected by a variety of means, such as:

- The obligation of the dominant company to compensate creditors for any annual deficits of the subsidiary (as is the case, for example, in Germany); or
- Extending the liability of the parent for the debt of the subsidiary under specific circumstances (France, Spain, and the Netherlands).

3. Groups of Companies in the Company Law

The Company Law does not recognize groups of companies as a single legal entity. It does, however, regulate the relationships between parent companies and their dependent or subsidiary companies for the purposes of protecting shareholder and creditor interests.[4]

Best Practices: Legal systems the world over are confronted with issues of groups of companies. Some have developed formal rules; others have left developments to case law. Formal regulation has mainly been developed in Germany, Portugal, and in some Eastern European countries. Brazil and Senegal are examples where group law has formally been introduced in company law, although it is unclear how the law is actually applied. Other jurisdictions, such as the U.S., have extensive rulings on groups of companies, developed by the courts, but no laws on groups.

In the absence of regulation on groups, Russian companies — wishing to follow good corporate governance practices — should regulate their group structure in the company charter, in particular, the main governance rights and responsibilities between the parent and its subsidiaries. The charter provisions may further be complemented with a specific by-law on the group.

[4] LJSC, Article 6.

4. Groups of Companies in Other Areas of Legislation

Tax and Antimonopoly laws both have significant implications for a company's decision to use group mechanisms. These laws place important constraints on companies, limiting their ability to create and/or expand their group structure.

Moreover these laws have their own definition as to whether a group of companies may be characterized as interdependent (apart from the corporate parent-subsidiary relationship).

a) Interdependent Companies under Tax Legislation

The Tax Code provides for a special definition of interdependent companies for tax purposes.[5] The main legal consequences which it envisages with regard to interdependent companies, relate to the tax regime of transactions concluded between these companies.[6] The regime aims to regulate a company's ability to trade commodities or transfer assets at prices below market rates.

Mutual dependence exists when a relationship between companies is capable of affecting the terms or economic results of their activities or the activities of persons represented by them. More specifically, the Tax Code identifies the following cases of interdependent companies:

- A company has direct and/or indirect participation in another company exceeding in total 20% of its capital.

Mini-Cases 1–3:

1. **Direct ownership:** Company (A) owns 21% of shares of Company (B).
2. **Indirect ownership:** Company (A) owns 50% of shares of Company (B). Company (B) owns 50% of shares of Company (C). The participation of Company (A) in Company (C) is calculated as the multiple of the direct participation by Company (A) in Company (B), and Company (B) in Company (C), hence 25%.

[5] Tax Code, Article 20.

[6] Tax Code, Article 40.

3. **Combination of direct and indirect ownership:** Company (A) owns 16% of shares of Company (C) directly, and 50% of shares of (B), which in turn holds 10% of shares of Company (C). Company (A) thus indirectly holds 5% of shares in Company (C) through its ownership in Company (B). Thus, the total direct and indirect ownership of Company (A) in Company (C) amounts to 21% of shares of Company (C).

- Courts have recognized two companies as being interdependent based on criteria other than those described in the examples above, e.g. when the relations between them can influence the results of transactions in providing goods, labor, or services.

b) Groups of Persons and Affiliated Persons under Antimonopoly Law

The Law on Competition and Restricting Monopoly Activities on the Commodities Markets (Antimonopoly Law) has its own definition of groups of persons and affiliated persons for the purposes of antimonopoly control. The emergence of groups or affiliation relationships requires notification or preliminary approval by the Ministry of Antimonopoly Policy and Entrepreneurship Support (MAP).[7] The question of whether such groups or affiliations exist under Antimonopoly Law must be examined independently of the question as to whether such companies form a dominant-dependent or parent-subsidiary relationship under the Company Law and/or an interdependent relationship under the Tax Code.

Under Antimonopoly Law, a group of companies exists in the following situations, as presented in Table 1:[8]

[7] Law on Competition and Restricting Monopoly Activities on the Commodities Markets (Antimonopoly Law), Article 18. Table 1 only covers those relationships mentioned in Article 18 that relate to companies.

[8] Antimonopoly Law, Article 4.

Table 1: Company Relations under Antimonopoly Law	
Direct Relationships	**Indirect Relationships**
• Based on an agreement, Company (A) has the right of disposal of more than 50% of voting shares of another Company (B). This right of disposal can take a direct or indirect form, including on the basis of a contract. The Antimonopoly Law specifies that indirect participation means the possibility for *de facto* control through a third person with regard to which Company (A) has the same rights. • Company (A) has the right to determine the decisions of Company (B), including the conditions for its entrepreneurial activity, on the basis of a contract or other form, or to fulfill the functions of the executive bodies of Company (B) by virtue of a contract. • Company (A) has the right to appoint the General Director and/or more than 50% of Executive Board members of Company (B), or, on the basis of its proposal more than 50% of members of the Supervisory Board or collective body have been elected.	• The same individuals (or their relatives) or persons proposed by one of the companies represent more than 50% of Executive Board or Supervisory Board membership of Companies (A) and (B), or upon the proposal of one of the companies, more than 50% of members of the Supervisory Board or collective executive body of Companies (A) and (B) have been elected. • Employees of Company (A) are the General Director or more than 50% of members of the Supervisory Board or a collective executive body of Company (B). • The same individuals (or their relatives) have the right of disposal with more than 50% of voting shares in both Companies (A) and (B). • The individuals or legal entities who have the right of disposal over more than 50% of voting shares of Company (A) are at the same time the persons constituting more than 50% of members of the Supervisory Board or collective executive body of Company (B). • Companies (A) and (B) are members of the same FIG.

For the purposes of antimonopoly control, companies are considered to be affiliated persons when:[9]

- Companies (A) and (B) belong to the same group of companies;
- Company (A) has the right to dispose of more than 20% of voting shares of Company (B); or
- The members of the executive bodies and the Supervisory Board of Company (A) are affiliated persons to Company (B), when both companies are members of the same FIG.

➜ *For more on affiliated parties, see Part III, Chapter 12, Section B.1.*

[9] Antimonopoly Law, Article 4. The list includes only those relationships listed in Article 4 that relate to companies.

B. Specific Group Structures

Specific group structures or regimes are differentiated from one another, depending on the legal regulation and their economic features. In many cases, these structures may overlap or exist simultaneously. Such structures will refer to:

- Parent-subsidiary;
- Dominant-dependent;
- Holding structures; and
- FIGs.

1. Parent-Subsidiary Company Structures

a) Definition of Parent and Subsidiary Companies

Companies (A) and (B) are defined as parent and subsidiary companies when Company (A) can control decisions adopted by Company (B) by virtue of:[10]

- Predominant participation in the capital of Company (B); or
- A contract to that effect executed between the two companies; or
- Other forms of control.

Thus, there are no strict formal criteria for the definition of parent-subsidiary relationships. It requires the examination of the degree and nature of the influence of the parent company over subsidiary decision-making. This approach allows for a greater degree of flexibility in reflecting the different relations between companies. At the same time, a clear definition of a parent-subsidiary relationship is imperative under the Company Law, which attaches important consequences to situations in which shareholder or creditor interests are put at risk.

The following types of parent-subsidiary relationships exist under the Company Law:

1) *Parent Company as a Predominant Shareholder of the Subsidiary*

The Company Law does not contain an exact percentage of share participation needed to qualify as a parent company. The requirement for "predominance" must be satisfied in specific cases in conjunction with the possibility to determine the decisions of the subsidiary company. Two factors in particular must be taken into account:

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[10] CC, Article 105, Clause 1; LJSC, Article 6, Clause 2.

- The actual share ownership in the capital of a company; and
- The type of quorum and voting majority required by the charter for the decision-making of the company.

➜ *For more information on the quorum and voting majorities of the General Meeting of Shareholders (GMS), Part III, see Chapter 8, Sections C.3 and E.*

Table 2 illustrates the level of control in a company based upon the percentage of share ownership.

Table 2: Examples of Predominant Participation

Participation in the Capital of Another Company	Control Implications
100%	The parent company (A) has full control over the decision-making of its subsidiary Company (B).
75% to 100%	Company (A) controls all decisions of the subsidiary's GMS, which — according to the Company Law or the charter — require 3/4-majority of voting shares or more.
50% to 75%	Company (A) controls all decisions of the subsidiary's GMS, which require a simple majority.

2) *Contractual Relationship*

A contract between two companies can provide that Company (A) is able to control decisions of Company (B). This means that even if Company (A) does not have a predominant participation in the charter capital of Company (B), a contract can provide for certain control rights. Such control rights include the right to appoint and dismiss directors and/or managers, approve or veto certain transactions, or instruct the company to act in a specific manner.

Russian law does not provide specific regulation with regard to the contents or the form of a contract that will influence the decision-making of a subsidiary. Some level of control can result from different types of contracts, such as joint ventures, bank credits, pledges of securities, or asset management contracts.

In these cases, specific rules applicable to individual contracts need to be observed. It is important to note that the provisions of the contract must be consistent with relevant legislation.

3) *Other Relationships*

The Company Law does not exhaust the cases in which a company has the potential to control the decisions of another company, thus qualifying as a parent-subsidiary relationship. In concrete circumstances, specific tests will be needed to identify such relationships (see examples in Mini-cases 4 and 5).

Mini-Cases 4 and 5.

4. **Pyramidal structures:** Company (A) has majority control of Company (B), and Company (B) has majority control of Company (C). As a result, Company (A) only controls Company (C) indirectly, but its control can be as effective as that of direct control. (A) is thus considered a parent company of (C).
5. **Control of affiliated companies:** Neither Company (A) nor Company (B) have majority control of Company (C). Yet, together companies (A) and (B) can have sufficient control to determine the decisions of Company (C). Both (A) and (B) are considered parent companies when they exercise control over (C).

b) Parent-Subsidiary Relations and the Decision-Making of the Subsidiary

A parent company and its subsidiary are separate legal entities that are legally independent from each other. The decision-making of the subsidiary, however, is by definition subject to the influence of the parent company. This section describes the mechanisms through which this influence occurs. Such mechanisms frequently exist in combination.

A parent company is able to influence decisions of a subsidiary through standard governance mechanisms available to controlling shareholders (shareholders with a predominant participation in the charter capital of the subsidiary), including the ability to:

- Directly control the outcome of issues that fall under the decision-making authority of the subsidiary's GMS;
- Nominate and elect representatives to the Supervisory Board of the subsidiary; and
- Nominate and elect representatives to the executive bodies of the subsidiary.

Best Practices: It is good practice to authorize the Executive Board of the parent company to complete certain tasks related to subsidiaries, such as to:[11]

- Set agenda for the GMS of wholly-owned subsidiaries, except when this authority is vested in the Supervisory Board of the parent;
- Appoint representatives of the parent company to the GMS of wholly-owned subsidiaries and issue voting instructions to them; and
- Nominate candidates for the Supervisory Board, the executive bodies, or other bodies in companies in which it participates.

Executive Board members or the General Director of the parent company frequently sit on the Supervisory Board or the executive bodies of the subsidiary. For this, the prior consent of the parent company's Supervisory Board is needed.[12]

Best Practices: It is important in such cases to ensure that the General Director of the parent has enough time to fulfill his tasks in both legal entities, but most importantly at the parent level.[13] Establishing an Executive Board at the parent level to spread managerial responsibilities or prohibiting side activities per contract are means of achieving this end.

Russian law allows parent companies to issue mandatory instructions to their subsidiaries. This right is, however, only allowed if predetermined in the contract between the two companies or charter of the subsidiary company.[14]

c) Protecting Shareholders of the Subsidiary

When a subsidiary is not 100% owned by the parent company, there are, by definition, other shareholders. Depending on the amount and type of their holdings, such shareholders may affect the decision-making of the subsidiary and exercise minority shareholder rights.

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[11] FCSM Code, Chapter 4, Section 1.1.4.

[12] LJSC, Article 69, Clause 3.

[13] FCSM Code, Chapter 4 Section 2.1.4.

[14] CC, Article 105, Clause 2; LJSC, Article 6, Clause 3.

In addition to the general rules protecting minority shareholders, the parent company is directly liable when it deliberately damages the interests of the subsidiary.[15] Such liability emerges when:

- The parent company has exercised its rights to influence the actions of the subsidiary; and
- As a result of this, the subsidiary has incurred losses; and
- The parent company has acted knowing that, by such act, the subsidiary will likely suffer losses.

The Company Law does not vest this right with the subsidiary itself, but instead with its shareholders. Accordingly, shareholders must file their claim on behalf of, and in the interest of, the subsidiary and against the parent company.

d) Protecting Creditors of the Subsidiary

A parent company can endanger the interests of the subsidiary's creditors in a variety of ways, ranging from obfuscating risks involved in contracts between the subsidiary and its creditors, to transferring assets between parent and subsidiary companies. Creditors of the subsidiary enjoy the general protection granted to creditors of commercial companies by Russian law.

Additional guarantees to creditors of a subsidiary exist. For example, the subsidiary is not liable for any debts of its parent company.[16] Further, the parent company — at least in principle — also enjoys limited liability with respect to the debts of its subsidiary. There are, however, a number of important exceptions to this rule.

1) *The Parent Company Has the Right to Give Mandatory Instructions*[17]

A parent company is liable for the debts of its subsidiary, when:

- The parent company has the right to issue mandatory instructions to the subsidiary; and
- This right has been envisaged in a contract between the parent company and the subsidiary, or in the charter of the subsidiary; and

[15] CC, Article 105, Clause 3; LJSC, Article 6, Clause 3.

[16] CC, Article 105, Clause 2; LJSC, Article 6, Clause 3.

[17] CC, Article 105, Clause 2; LJSC, Article 6, Clause 3.

- The debt of the subsidiary was incurred as a part of a transaction fulfilling such mandatory instructions.

In such circumstances, joint and several liability of the parent company for the debts of the subsidiary exists. This means that a creditor can choose to direct its claim, or a part of it, to the subsidiary or to the parent, or to both.[18] If the claim is directed to the subsidiary but no satisfaction of the claim, or only a partial satisfaction, is received, the creditor can direct the claim (in full or the outstanding part of the claim) to the parent company. Thus, the parent company remains liable until the full amount of the debt has been satisfied.

2) *The Subsidiary's Insolvency Has Been Caused by the Parent Company*

A parent company can also be held liable for the debts of its subsidiary, when:[19]

- The subsidiary has become insolvent (bankrupt); and
- The insolvency of the subsidiary has been caused by the parent company, by exercising its rights and/or influence; and
- The parent company acted knowing that such action would result in the insolvency of the subsidiary.

The purpose of this exemption from the limited liability rule is to prevent parent companies from deliberately causing the bankruptcy of the subsidiary and thereby defrauding its creditors. (A great number of insolvencies in Russia during the mid- to late 1990s were in fact deliberately and fraudulently caused by parent companies and went un-punished due to poor enforcement mechanisms.) In such cases, the Company Law provides for the liability of the parent in addition to that of the insolvent subsidiary. This means that the subsidiary remains the main debtor, to which the creditor directs all claims first.[20] Only if the subsidiary is unable to satisfy the claim or fails to react to the claim within a reasonable time can the parent company be held liable.

e) Establishing Subsidiaries

Subsidiaries can be established by founding a new company, through the reorganization of an existing company or by acquiring shares of an existing company.

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[18] CC, Article 323.

[19] CC, Article 105, Clause 2; LJSC, Article 6, Clause 3. See also: Insolvency Law, Article 10, Clause 4.

[20] CC, Article 399.

A subsidiary can be created by founding a new company. The parent company can:

- Invest the entire amount of the initial charter capital, thus becoming the only shareholder of a fully-owned subsidiary; or
- Contribute to the initial charter capital and become the majority shareholder of the subsidiary, along with other companies or individual shareholders.

In this case, the parent company needs to comply with all legal requirements regulating the founding of a new company in the respective legal form, for example a joint stock company or limited liability company.[21]

Accordingly, the parent company is subject to the duties and liabilities of the founders of a company, as specified in Table 3.

Table 3: Liabilities and Notification Requirements of the Parent Company as a Founder

Legal Source	Duties and Liabilities
The Company Law	• Joint and several liability for debts incurred in the process of forming the new company;[22] and • To take all steps and actions necessary for the state registration of the company.[23]
Securities Legislation	➜ *For the requirements as to founders, see Part III, Chapter 11.*
Antimonopoly Legislation	• Founders need to notify the MAP within 45 days of the state registration if the sum of the founders' assets, according to the last balance sheet, exceeds 200 thousand times the minimum wage.[24]
Tax Legislation	• The company needs to notify the tax authorities at its location about its participation in the new company within 30 days.[25]

A subsidiary can also be created through the reorganization of a company in the form of split-up or spin-off.

➜ *For more on company reorganization, see Part V, Chapter 16.*

[21] CC, Article 51.

[22] LJSC, Article 10, Clause 3.

[23] LJSC, Articles 11 and 13, Law on State Registration of Legal Persons, Articles 12 and 13.

[24] Antimonopoly Law, Article 17, Clause 5.

[25] Tax Code, Article 23, Clause 2.

A company can finally acquire shares in an already existing company. In such cases, the following requirements apply:

- The acquiring company must notify and disclose the acquisition of 20% of voting shares of the acquired company, and any subsequent 5% increases thereof, to the Federal Commission for the Securities Market (FCSM) within a month of the acquisition or increase.[26]
- When the acquiring company has the right of disposal of more than 20% of voting shares of the acquired company, the company must:
  - Seek the consent of the antimonopoly body *ex ante*, when the sum of the assets of the founders according to the last balancesheet exceeds 200 thousand times the minimum wage or when one of the founding companies (or the persons who have a predominant participation in the capital of such a company) has a market share of more than 35%;[27] and
  - Notify the MAP, when the sum of the founders' assets according to the last balance sheet exceeds 100 thousand times the minimum wage.[28]

2. Dominant-Dependent Company Structures

Another type of regime in a group of companies is that between dominant and dependent companies, which is regulated by the Company Law. The legal regime regulating dominant-dependent companies is quite similar to that of the parent-subsidiary regime, though, differences exist. The main difference between dependent companies and subsidiaries relates to the degree of control exercised by the parent/dominant company, and the legal obligations toward minority shareholders and creditors of subsidiary/dependent companies.

Thus, Company (B) is considered dependent on Company (A) when Company (A) holds more than 20% of the voting shares in Company (B).[29] Dependency consequently occurs on the satisfaction of a formal criterion (the acquisition of a percentage of voting shares) and not the nature of the relationship between the companies.

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[26] CC, Article 106, Clause 2; LJSC, Article 6, Clause 4.

[27] Antimonopoly Law, Article 18, Clauses 1 and 2.

[28] Antimonopoly Law, Article 18, Clause 6.

[29] CC, Article 106, Clause 1; LJSC, Article 6, Clause 4.

When dependent company structures exist, the following should be kept in mind:

- **Disclosure Obligation:** Company (B) is obliged to disclose its 20% stake in (A), as determined by the FCSM;[30] and

➜ *For more information on such disclosure requirements, see Part IV, Chapter 13, Section B.3.*

- **Rules on Related Party Transactions:** The acquisition of more than 20% of shares in another company triggers special provisions of the Company Law when these two companies engage in certain transactions.[31]

➜ *For more on related party transactions, see Part III, Chapter 12, Section C.*

Other than these two rules, the Company Law does not regulate relations between the dominant and dependent companies.

3. Holding Companies

The holding company concept was introduced by Presidential Decree in relation to groups of companies created in the process of transforming state-owned enterprises (SOEs) into joint stock companies for privatization.[32] A holding company is defined as a company whose assets include control shares of another company or a group of companies.[33] Control shares are defined as any form of share participation that ensures the unconditional right of approving or rejecting specific decisions of the GMS and its executive bodies.

4. Financial and Industrial Groups

Russian law recognizes the existence of FIGs. FIGs are created for the purposes of technological or economic integration based on:[34]

[30] LJSC, Article 6, Clause 4.

[31] LJSC, Article 81, Clause 1.

[32] Decree No. 1392, the President of the Russian Federation, Temporary Statute of Holding Companies Established in the Process of Transforming State Companies Into Joint Stock Companies (Decree No. 1392), 16 November 1992. Note that following this decree, a draft law on holdings has been discussed by the State Duma, but has yet to be adopted.

[33] Decree No. 1392, Clause 1.1.

[34] Law on Financial and Industrial Groups, Article 2.

- Legal entities acting as parent and subsidiary companies. In this case, both the parent company and the subsidiary form the FIG;[35] or
- Legal entities that have fully or partially unified their tangible or intangible assets on the basis of a contract for the establishment of a FIG.

Central to the FIG is a legal entity established by a contract between all parties, or a parent company authorized by law or contract to act as one.[36]

The most important legal requirements applicable to FIGs are:

- The establishment of the FIG is subject to state registration;[37]
- In the cases set forth by tax legislation, the contract for the establishment of a FIG can provide for tax consolidation of the members of the FIG.[38] Similarly, the contract can provide for accounting consolidation;[39]
- The participants in the FIG bear joint and several liability for the debts incurred by the central company in realizing the activities of the group. The specific aspects of this liability are regulated by the contract for the establishment of the FIG;[40]
- The FIG is required to prepare an annual report within 90 days of the end of the fiscal year.[41] The report must reflect the results of the inspection of an independent External Auditor. This report is submitted to all participants of the group and to the authorized state body; and
- The FIG is subject to annual state control, including the possibility of an audit.[42]

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35 Law on Financial and Industrial Groups, Article 3, Clause 5.

36 Law on Financial and Industrial Groups, Article 11, Clause 1.

37 Law on Financial and Industrial Groups, Article 5.

38 Such provisions have not been made to date.

39 Law on Financial and Industrial Groups, Article 13. Also, see Regulation No. 24, the Council of Ministers, on the Procedure for Keeping Consolidated Accounts, Reports, and Books of Financial and Industrial Groups, 9 January 1997.

40 Law on Financial and Industrial Groups, Article 14.

41 Law on Financial and Industrial Groups, Article 16.

42 Law on Financial and Industrial Groups, Article 17.

C. Summary Table

Table 4: Summary of Corporate Governance in Groups of Companies

	Legal relationship in another company recognized	**Legal consequences**
Dependent companies (the Company Law)	Holding 20% or more of voting shares	Disclosure obligation
		Applicability of provisions regarding related party transaction
Parent-subsidiary (the Company Law)	Possibility to control decisions by virtue of: • Predominant share participation (typically, more than 50%), • Contract, or • Other.	The parent can issue mandatory instructions regarding the business of the subsidiary if provided in the subsidiary's charter or the contract between parent and subsidiary.
		Extended liability of the parent for debts of the subsidiary if: • The debts are incurred in exercise of the parent's right to issue mandatory instructions (and parent *mala fide*), or • The insolvency of the subsidiary has been brought about by the parent (and parent *mala fide*).
		The parent is liable to the subsidiary's shareholders for losses caused deliberately.
Interdependent companies (Tax Code)	• Direct or indirect participation exceeding 20% • Other relationship with effect on the results of the transactions in realizing goods or providing labor or services, when recognized by a court.	Notification obligation and tax liability.
Groups of persons (Antimonopoly Law)	Direct or indirect relationships. ➜ *See Section A.4.b in this Chapter*	Requirements for notification or *ex ante* approval.
Affiliated persons (Antimonopoly Law)	➜ *See section A.4.b in this Chapter*	Requirements for notification or *ex ante* approval.
Financial and Industrial Group (Law on Financial and Industrial Groups)	Group of companies based on: • A parent-subsidiary relationship; • A special contract for the establishment of the FIG.	Requirements for state registration and enhanced state regulation.