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LIABILITY OF MANAGEMENT, AUDITORS, AND OVERSIGHT PERSONNEL IN CREDIT INSTITUTIONS FACING INSOLVENCY

Florin-Georgian CREȚU
Orcid ID: 0009-0003-9999-2774
E-mail: florin.cretu@just.ro
Afiliation: Titu Maiorescu University, Bucharest

Abstract: *This article aims to analyze the liability of individuals holding management, control, or executive positions within credit institutions that have become insolvent, starting with the definition and characterization of these entities. It examines essential aspects regarding the active and passive procedural standing in liability actions, as well as the legal nature of the obligations incumbent upon these categories of persons. The study addresses the general conditions for the engagement of liability, the possibilities for exemption, and the necessary distinctions between applicable forms of liability. The approach highlights the complexity of the legal framework governing bank insolvency and proposes a balanced interpretation of the regulatory framework, aiming to ensure adequate protection for both creditors and the persons concerned.*

Keywords: *credit institution; legal liability; bank insolvency; executive management; exemption from liability.*

Introduction

As expected, due to the complexity and the multifaceted nature of the subject matter, insolvency proceedings generate *ex proceso* effects. This notion refers, in relation to the subject of the proceedings, to the possibility of vesting the insolvency judge with various incidental claims, which are not identical *mutatis mutandis* to those arising under general law but bear an indirect connection to the initial vesting. Among these

claims is the request to hold liable, under civil law, the persons responsible for the debtor's insolvency. Considering the multiple particularities governing the regime of credit institutions, the Romanian legislator has rightly opted to assign a special regime in this matter.

The Notion of Credit Institution

The core of the matter is represented by Article 3(1)(10) of Emergency Government Ordinance No. 99/2006 (Regarding credit institutions and capital adequacy (Official Gazette no. 1027 of December 27, 2006). The aforementioned normative act defines a credit institution as *"an entity whose activity consists of attracting deposits or other repayable funds from the public and granting credits on its own account."* This definition has been criticized (Postolache, 2012, p. 44), particularly with regard to the inappropriate use of the term *"entity"*, which could lead to confusion by suggesting that a natural person might qualify as a credit institution-an incompatible scenario considering the overall regulatory framework. Additionally, the definition has been criticized (Postolache, 2012, 44) for failing to specify the frequency with which the activities encompassed by the credit institutions' object should be conducted.

Overview of Liability. Active Procedural Standing

Traditionally (Cărpenaru, 2016, p. 813), it is noted that Law No. 85/2014 (Regarding the Procedures for the Prevention of Insolvency and Insolvency, Official Gazette no. 466 of June 25, 2014) does not regulate a punitive procedure; rather, this procedure aims either at safeguarding the debtor while simultaneously protecting the creditors, or exclusively at protecting the latter. However, as previously stated, the liability action constitutes a genuine incidental claim, founded on the rationale that certain persons "benefit" (Bufan, 2014, p. 807) from the possibility of being held liable for the debtor's insolvency, based on their status, level of experience, knowledge, and so forth.

It should be emphasized that the legal basis for the liability action is found in Articles 169-173 of Law No. 85/2014, Section 8, and more specifically, in the context of credit institutions, Articles 235-236 of the same normative act.

According to Article 169 of Law No. 85/2014, at the request of the judicial administrator or the judicial liquidator, the insolvency judge may order that part or all of the debtor's liabilities, where the debtor is a legal entity declared insolvent, be borne by members of the debtor's management and/or supervisory bodies, as well as any other persons who have contributed to the debtor's insolvency by committing one or more acts expressly provided by law, without exceeding the damage causally linked to such acts.

Thus, the jurisdiction to resolve the liability action lies with the insolvency judge, and the active procedural standing is expressly conferred by law upon the judicial administrator or judicial liquidator. It is important to highlight that this action is exercised within the insolvency procedure itself, constituting an incidental claim and not one filed after the procedure's closure (Cărpenaru, 2016, p. 814; in this regard, see Decision no. 126/2003 of the Bucharest Court of Appeal, 6th Commercial Division, cited in Neagu, 2011, p. 53, footnote 1).

The claim may also be filed by the chairman of the creditors' committee, based on the decision of the creditors' meeting, but subsidiarily, in cases where the judicial administrator or liquidator has not identified the culpable persons or has decided not to initiate the liability action (Neagu, 2011, p. 815). In accordance with Article 169(2) of Law No. 85/2014, the claim may also be submitted by a creditor holding more than 30% (Until the entry into force of Emergency Ordinance no. 88 of March 27, 2018, Official Gazette no. 840 of October 2, 2018), the threshold was 50%) of the total claims registered in the creditors' estate.

Regarding this latter aspect, earlier specialized literature questioned whether (Avram, 2007, pp. 8-9), pursuant to the provisions of Law No. 64/1995 (Regarding the procedure of judicial reorganization and bankruptcy, republished Official Gazette no. 130 of June 29, 1995,

republished under no. 1066 of November 17, 2004), the insolvency judge could act ex officio on a liability claim. It was considered that such an interpretation would be excluded, primarily due to the availability principle governing civil procedure.

During the period when Law No. 64/1995 was in force, the active procedural standing of the judicial administrator or liquidator was not recognized, on the grounds of their lack of interest, since they were *"not the injured parties, nor is there an express provision in this regard."* (Avram, 2007, p.9).

Attention must also be drawn to Article 235(2) of Law No. 85/2014, which contains derogatory provisions regarding active procedural standing: *"For the purpose of taking measures provided in Article 235, the insolvency judge may be notified by the judicial liquidator, a shareholder, any creditor, or the National Bank of Romania, based on data in the case file, and may order precautionary measures."*

Without delving too deeply into the discussion, during the period when Law No. 85/2006 was in force, doctrinal debate (Al Hajjar, 2012, pp. 204-205) arose regarding the impartiality of the insolvency judge in exercising the function stipulated in Article 11(1)(g), final phrase, concerning the notification of the criminal investigation authority when indications of offenses incriminated under Articles 143-145 of the normative act are found. Thus, the impartiality of the judge was called into question (Simona Al Hajjar, 2012, p. 205) when adjudicating the patrimonial action based on the illicit act identified with the criminal offense under investigation.

Passive Procedural Standing

Pursuant to the provisions of Article 36 of the Civil Procedure Code (Law no. 134/2010 on the Civil Procedure Code, republished, Official Gazette no. 247 of April 10, 2015), the passive procedural standing belongs to the person who committed the alleged unlawful act. In this context, reference is made to the members of the management

and/or supervisory bodies within the debtor legal entity, as well as any other persons who contributed to the debtor's insolvency through acts expressly regulated by law.

As is generally known, the administration of companies is not uniformly regulated across all forms of commercial companies (Al Hajjar, 2012, p. 221). Therefore, to determine the responsible persons, one must refer to the provisions of Law No. 31/1990 (hereinafter referred to as the Companies Law). In this regard, partnerships (general partnerships and limited partnerships) as well as limited liability companies may appoint multiple administrators through their associates (Cărpenaru, 2016, p.229). In the case of joint-stock companies, their administration and management present specific features. Thus, according to Article 137 of the Companies Law, a joint-stock company is administered by one or more administrators. When there are multiple administrators, they constitute a board of administrators, and according to Article 143 of the same normative act, the board of administrators may delegate the management of the company to one or more directors, appointing one of them as general director. This latter scenario concerns the unitary management system of joint-stock companies (Cărpenaru, 2016, p.341). Regarding the dualistic management system of joint-stock companies (Cărpenaru, 2016, p.349), the relevant concepts are the management board and the supervisory board, with the board of administrators being absent.

Moreover, in the matter of liability for the insolvency of credit institutions, it should be noted that the scope of persons liable, as provided by Article 235 of the Companies Law, is broader (Cărpenaru, 2016, p.834) than under "general law." Specifically, this scope includes: *"members of management bodies or directors/coordinators with internal control responsibilities of directorates, departments, or other similar structures; operational staff with internal control duties; auditors within the credit institution that has become insolvent."* Also relevant is the imperative condition laid down in Article 235, namely that these persons must have held such positions within the three years prior to the opening of insolvency proceedings.

Regarding passive procedural standing (*"In the case at hand, it can be found that the defendants J.D., J.J.Ș., and J.J.E. can be held liable in the legal relationship under trial, and that the creditors' interest can be achieved against them. Thus, according to articles 774 and 777 of the Civil Code, the heirs of the deceased contribute to the payment of the debts and burdens of the inheritance, in proportion to their share of the inheritance; by debts and burdens of the inheritance are understood the obligations of the deceased regardless of their origin..."*; Cluj Court of Appeal, Commercial, Administrative and Fiscal Litigation Section, Civil Decision no. 375/15.02.2010 apud Neagu, 2011, pp. 81-92), specialized literature unanimously accepts the possibility of civil liability also being engaged for the patrimonial responsibility of "de facto managers" (Luiza Neagu, 2011, p. 815, footnote 2, and the cited specialized literature). However, I consider it necessary to clarify certain aspects regarding this notion: first, by "de facto manager," we understand, preliminarily, persons exercising decision-making prerogatives in the company without having been formally appointed-even illegally-to any position specified by law (Even if the described situation acquires criminal connotations, it is necessary to take into account the provisions of Article 169, paragraph (8), which expressly provide for the possibility of cumulating criminal liability with civil liability). Secondly, this includes administrators who have been unlawfully invested with their position (Al Hajjar, 2012, pp. 225 et seq, with the specification that the author distinguishes between de facto administrators and apparent administrators).

Legal Nature of Liability

The legal nature of liability has raised numerous issues in the specialized literature (Avram, 2007, pp.30-31), which remain relevant to this day. In this regard, two main opinions have been highlighted: the first classifies the liability as tortious, while the second (Cărpenaru, 2016, p.814.) qualifies the liability, depending on its source, as either contractual or tortious. Without delving too deeply into details, we align with the opinion that this constitutes genuine tort liability (Avram, 2007,

p.31), since *"the capacity that the persons held in relation to the debtor, with respect to whom liability is invoked, is considered in the text of Article 138 solely for the purpose of delimiting the scope of persons to whom the regulated liability applies, and not as an element of the composition of such liability."*

Exoneration from Liability

In addition to the traditional grounds for exoneration from liability (Pop, Popa, & Vidu, 2012, pp. 428 et seq), Law No. 85/2014 introduces two special causes for exoneration. Thus, according to Article 169(5), liability shall not be incurred if, within the collegial governing bodies of the legal entity, the persons concerned opposed the acts or deeds that contributed to the state of insolvency or were absent from the decisions that contributed to the insolvency and subsequently recorded their opposition to those decisions. Therefore, this provision essentially materializes the absence of imputability, as there is no causal link between the unlawful act and the prejudice.

Similarly, according to paragraph (6), liability shall not be incurred if, during the month preceding the cessation of payments, payments were made in good faith in execution of an agreement with creditors, concluded following extrajudicial negotiations for the restructuring of the debtor's debts, provided that the agreement was likely to lead to the debtor's financial recovery and was not intended to harm and/or discriminate against the creditors. A particularly interesting aspect of this exoneration ground is the requirement that the agreement be capable of leading to the debtor's financial recovery; thus, it involves at least a prospective assessment by the insolvency judge regarding the imminent effects of the contract.

Conditions of Liability

Given the tortious nature of the liability, the conditions are those provided by Article 1357 of the Civil Code (Law no. 287/2009 regarding

the Civil Code, republished, Official Gazette no. 409 of June 11, 2011), namely the unlawful act, damage, causal link, and fault. Regarding the unlawful act, it should be noted that it is specifically circumscribed by the legal text, which enumerates eight general acts[1], to which three additional acts specific to credit institutions are added.

The first special unlawful act concerns the *"granting of loans in violation of prudential requirements approved by the applicable regulations, as well as non-compliance with the internal rules in force."* This category of civil wrongdoing addresses the specific principles applicable to credit institutions, from which negative result obligations derive in the field of credit granting. As noted, violation of the obligations imposed by the internal regulations as well as by Government Emergency Ordinance No. 99/2006 generates an "additional exposure of the institution to the intrinsic risk of any lending activity." (Bufan, 2014**,** p.879).

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[1] These acts are:
a) They used the goods or credits of the legal entity for their own benefit or for the benefit of another person;
b) They carried out production, trade, or service activities in their personal interest, under the cover of the legal entity;
c) They, in their personal interest, ordered the continuation of an activity which obviously led the legal entity to insolvency;
d) They kept fictitious accounting records, caused some accounting documents to disappear, or did not keep accounting in accordance with the law. In the case of failure to hand over accounting documents to the judicial administrator or judicial liquidator, both fault and the causal link between the act and the prejudice are presumed. This presumption is relative;
e) They embezzled or concealed part of the legal entity's assets or fictitiously increased its liabilities;
f) They used ruinous means to procure funds for the legal entity, with the purpose of delaying insolvency;
g) In the month prior to insolvency, they paid or ordered preferential payment to one creditor to the detriment of the other creditors;
h) Any other intentional act that contributed to the debtor's state of insolvency, established according to the rules of the insolvency procedure.

The second unlawful act pertains to the "incorrect reflection" (Bufan, 2014, p.879) of the financial situation, other accounting situations, or reports in violation of legal provisions. It is worth noting that Article 152 of Government Emergency Ordinance No. 99/2006 imposes strict positive obligations on credit institutions regarding financial statements *("...with respect to the defendant's obligation to keep the registers required by law, the condition imposed by the legislator is that the failure to fulfill this obligation, namely not keeping accounting records in accordance with the law, must have contributed to the company's insolvency. Therefore, the mere fact that the defendant did not keep the accounting according to Romanian law is not sufficient to engage their liability in the absence of proof of a causal link..."* Bucharest Court of Appeal, 6th Commercial Section, Commercial Decision no. 249/R/12.02.2010 apud L. Neagu, 2011, pp. 103-106). These are subject to annual audit and publication (Neagu, 2011, pp. 103-106).

The last special manifestation of civil wrongdoing concerns a passive attitude (Neagu, 2011, pp. 103-106), consisting in the failure, within internal verification actions, to identify and report, by neglecting service duties, the acts that led to fraud and mismanagement of assets.

Regarding the other conditions for triggering tort liability, no further clarifications are deemed necessary, as they follow the common legal regime provided by the Civil Code. One clarification must be made with reference to Article 169 of Law No. 85/2014, indicating that the insolvency judge may order that part or all of the debtor's liabilities be borne as damages, but without exceeding the prejudice causally linked to the respective act.

Another substantive law issue is that, if multiple persons have contributed, concurrently or successively, to the unlawful activity, their liability is joint and several (Article 169, paragraph (4) of Law 85/2014).

Procedural Aspects

In this matter, certain special procedural rules apply. Primarily, the claim is adjudicated in accordance with the provisions of common law, namely the Civil Procedure Code. It has been judiciously noted (Cărpenaru, 2016, p.818) that given the purpose of the action, the claim can only be resolved after the debtor's liabilities are known, through the preparation of the final creditors' table, respectively the final consolidated creditors' table." The decision rendered is subject to appeal (Cărpenaru, 2016, p. 819) and shall be communicated to the National Trade Register Office.

Last but not least, the law provides for a special incapacity to exercise certain rights: Article 169 paragraph (10) states that *"a person against whom a final judgment imposing liability has been rendered may no longer be appointed as administrator or, if already serving as an administrator in other companies, shall be deprived of this right for a period of 10 years from the date the judgment becomes final."*

From a procedural standpoint, Law No. 85/2014 also grants the possibility to the insolvency judge to be seized with a request for precautionary measures. Such a request may constitute a main claim or an incidental claim. According to Article 172 of the aforementioned law, the posting of a bond amounting to 10% of the claim value is mandatory for the initiation of this procedure.

Enforcement will be carried out, according to Article 173 of the law, in accordance with the provisions of the Civil Procedure Code.

Finally, pursuant to Article 170 of the law, the liability action is subject to a statute of limitations of 3 years. This period begins from the date the person who contributed to the debtor's insolvency became known or should have become known, but no later than 2 years from the date of the opening of the insolvency proceedings[1].

[1] The legal text complies with the general rule on the matter set out in Article 2517 of the Civil Code. Furthermore, it is consistent with the general rules of civil law regarding the commencement of the limitation period, establishing both a subjective moment (the

Any funds recovered shall be included in the debtor's estate (Cărpenaru, 2016, p. 805) and will follow the legal regime provided by Law No. 85/2014.

Conclusions

The regulation concerning the liability of management bodies for the debtor's insolvency is welcome. I consider that it represents a genuine procedure aimed at safeguarding the debtor's situation while simultaneously providing protection for creditors. Additionally, the regulation is efficient due to the promptness that characterizes the procedure before the insolvency judge, with the claim essentially constituting either a principal or an incidental request.

The expansion of the scope of liable persons aligns with prudential rules in banking law, thereby establishing a standard of proof that is considerably easier to meet compared to general cases (particularly with respect to the notion of the de facto administrator, a concept that is difficult to apply in banking law).

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date on which the person became aware) and an objective moment (the date on which the person ought to have become aware). Finally, the law also establishes a *dies ad quo* (rather than a *dies ad quem*) of two years from the date on which the insolvency proceedings were opened, thus marking the starting point of the three-year limitation period.

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