

Newsletter

Bankruptcy moratorium expiration: the Supreme Court of the Russian Federation clarifies a number of key issues

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Dear Ladies and Gentlemen,

On January 7th 2021, the bankruptcy moratorium, which had been in effect since April last year, expired. The main conditions of the bankruptcy moratorium were described earlier in details: in *newsletters* "*Moratorium on bankruptcy proceedings*" and "*Russian bankruptcy moratorium extended until January, 2021*"

Now, the time has come to summarize one of the main legal developments of the year, and complement it with consideration of the key clarifications of the Resolution of **the Plenary session of the Supreme Court of the Russian Federation** of December 24th 2020. These clarifications are devoted to the application of the provisions of the bankruptcy moratorium.

1. Who was subject to the moratorium?

In different periods of the moratorium, up to half a million companies, and one and a half million individual entrepreneurs, were subject to the moratorium regime. According to **Interfax**, this is about one seventh of the companies registered in the Russian Federation and about 40% of individual entrepreneurs.

During the moratorium period, the list of persons, falling under it, was repeatedly amended. For instance, since October 1st 2020, in accordance with the Resolution of the Government, the moratorium ceased to apply to strategic and systemically-important enterprises.

In this context, the Supreme Court of the Russian Federation noted that the moratorium did not apply retrospectively. This means that if the company's area of industry is included in the governmental list, the moratorium is valid from the moment of such an inclusion, rather than from the date of moratorium. Moreover, the Supreme Court of the Russian Federation noted that the moratorium did not apply to the persons against whom bankruptcy proceedings had already been initiated, on the day the moratorium was introduced.

2. Moratorium – a remedy against a subsidiary liability claims in bankruptcy?

According to the provisions of Art. 9.1 of the Bankruptcy Law, during the moratorium period, the debtor's obligation, to file a bankruptcy petition, is suspended. According to these provisions, there is no threat of the debtor's management subsidiary liability for failure to apply for bankruptcy.

However, according to the above-mentioned Resolution of the Plenary session of the Supreme Court of the Russian Federation, if there were signs of an economic crisis in the company before a pandemic, and its management was aware of the absence of any opportunity to overcome the crisis, in such a case, the controlling persons could still be held liable for failure to file a bankruptcy petition.

The above clarifications are primarily aimed at constraining bad-faith directors who leave the company and use the moratorium only as an excuse not to fulfill their obligations to creditors.

The issue of calculating financial sanctions for the debtor is resolved in a similar way: as a general rule, they are not charged, but the counterparty has the right to prove that the debtor did not, in fact, suffer from the pandemic. Then, the court is entitled to grant the claim in terms of financial sanctions, ignoring the rules on the bankruptcy moratorium.

3. How can creditors defend against debtor's assets stripping during the moratorium?

The current legislation proceeds from the fact that the bankruptcy moratorium does not prevent filing a claim to the court for debt collection and obtaining interim measures, in the form of assets freezing. This mechanism allows to effectively obtain the necessary protection in most cases.

In addition, the Supreme Court of the Russian Federation allowed creditors to apply for claw back of the transactions performed during the moratorium, without initiation of a bankruptcy case. This applies to the transactions deliberately aimed at violating the rights and interests of the debtor's creditors, for example, the sale of property at an obviously-understated price. These transactions are subject to invalidation on general civil grounds - Art. 10 (2), Art. 168 of the Civil Code of the Russian Federation.

This clarification is of the most critical significance, as it opens up the opportunity for creditors to challenge transactions on bankruptcy grounds, without initiating a bankruptcy case, thus saving time and resources.

In addition, challenging transactions in a bankruptcy case remains an effective tool in the hands of creditors, within which the so-called "suspicion period" is extended for the period of the moratorium, provided that the bankruptcy petition is filed no later than 3 months from the date of its cancellation.

4. What are the peculiarities of considering a bankruptcy case in respect of debtors under moratorium?

Obviously, despite the temporary support of many businesses by the moratorium, many of them will subsequently face bankruptcy. In this regard, we would like to draw your attention to the following most significant clarifications:

A. **The debtor is presumed to have entered into transactions, during the moratorium, in the ordinary course of business**, if the counterparty was not aware of any signs of insolvency.

Ordinary transactions, as a general rule, have immunity from contestation on the basis of undervalue and preference (Art. 61.2(1) and Art. 61.3 of the Bankruptcy Law). These provisions, on the one hand, are aimed at encouraging counterparties to enter into legal relations with debtors under moratorium, but on the other hand can be grounds for significant abuse on the debtor's part.

B. **Claims, that have arisen during the moratorium, are deemed as current**, which guarantees their priority satisfaction, in relation to the claims that arose before the introduction of the moratorium.

C. **The priority of claims, from compensatory financing of controlling persons, is not subordinated**, which is aimed at encouraging business' beneficiaries to rescue their companies.

5. Is a creditor entitled to defend against a deliberately-unenforceable restructuring installment plan?

One of the main amendments of the Bankruptcy Law is the possibility, for a debtor under moratorium, to apply a judicial installment plan, which we described in detail earlier in *newsletter "Moratorium on bankruptcy proceedings"*.

In accordance with these provisions, the debtor, subject to the moratorium, may apply for a court order, introducing the debt restructuring plan for up to three years, which is binding for all creditors.

However, the Supreme Court of the Russian Federation noted that creditors have the right to present evidence to the court that the debtor has no chance to restore its solvency, nor pay off all claims of the remaining creditors. In such a case, the court is entitled to dismiss an application for an installment (restructuring) plan.

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If you have any questions, please, do not hesitate to contact ALRUD partners



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