

ClientAlert

Disputes Resolution

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Accrual and Payment of Interest on Creditors' Claims in Insolvency: The Plenary Session of the Russian Supreme Commercial Court Made the Clarifications



This issue considers the most important provisions of the resolution adopted at the Plenary Session of the Supreme Commercial Court of the Russian Federation (the "SCC") No. 88, dated 6 December 2013, "On Accrual and Payment of Interest on Creditors' Claims in Insolvency" (the "Resolution")¹. The Resolution resolves a number of important practical issues and creates new regulations governing, in particular:

- the introduction of uniformly accruing moratorium interest on the amount of outstanding indebtedness in lieu of any contractual interest and penalties payable to any creditors once the supervision stage is introduced in respect of a debtor;
- the arrangement of payment of interest upon termination of the insolvency proceedings;
- homogenisation of the position of creditors asserting claims at different stages of the insolvency proceedings; and
- the discounting of debt related to the claims which have not yet matured as on the date of their record in the register of creditors by the amount of interest due for future periods.

The provisions of the Resolution also intend to restrain wilful abuses of the insolvency process.

Procedure for Accrual of Interest Where Insolvency Proceedings Are Initiated against a Debtor

The Resolution establishes that, from the time the supervision stage is introduced, the contractual interest and sanctions shall not accrue in respect of any claims arising prior to the initiation of insolvency proceedings².

Instead, uniform interest (the "moratorium interest") shall accrue in respect of all claims (whether included in the register of creditors or not) at the refinancing rate set forth by the Central Bank of Russia as of the date the supervision stage is introduced³. This approach emulates the provisions of the Insolvency Law which stipulate the accrual of moratorium interest during financial rehabilitation⁴, external administration⁵ and receivership⁶.

¹ The Resolution was published on the SCC website on 27 December 2013: http://arbitr.ru/as/pract/post_plenum/102002.html.

² Para. 4 of the Resolution.

³ As of the date of this report (17 April 2014), the refinancing rate of the Central Bank of Russia amounts to 8.25% per annum.

⁴ Article 81(2) of the Federal Law On Insolvency (Bankruptcy) No. 127-FZ, dated 26 October 2002, (the "Insolvency Law").

⁵ Paragraph 4, Article 95(2) of the Insolvency Law.

⁶ Article 126(2.1) of the Insolvency Law.

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Key features of moratorium interest include:

- moratorium interest shall only accrue on the principal amount of the debt excluding interest⁷;
- it shall be collected by the insolvency administrator;
- it shall not be included on the register of creditors' claims nor shall it be counted in determining the number of votes held by a creditor at the creditors' meetings⁸;
- it shall be payable together with the principal debt prior to the payment of any penalties⁹; and
- it shall be part of the interest under the pledgor's claim, i.e. it may be repaid prior to the claims of other creditors, out of the value of the pledged property¹⁰.

Therefore, any contractual interest and penalties will only accrue until the supervision stage; once this stage is introduced the sums due will be replaced by moratorium interest¹¹.

Repayment of Interest upon Termination of Insolvency Proceedings

The Resolution also clarifies the extent to which moratorium interest must be paid if the insolvency proceedings are terminated.

If the indebtedness is repaid in full in the course of financial rehabilitation or external administration, the creditors shall not be entitled upon termination of the proceedings to claim that the debtor further pay the difference between the interest due under the agreement and the moratorium interest¹².

As a general rule, if the debt repayment schedule adopted in the course of financial rehabilitation (the "schedule") or the external administration plan (the "plan") provides that the claims recorded on the register shall be repaid in part (e.g., without any repayment of the moratorium interest), then, following the termination of the insolvency proceedings connected with the claims subject to the terms and conditions of the schedule or plan, the creditors may bring adversarial proceedings demanding that the debtor pay the remaining unpaid moratorium interest.

However, the plan or schedule may specify alternative arrangements which may, in particular, include prohibitions on demands for further payment of the moratorium interest or demands for additional payment of contractual interest¹³.

These rules also seem to apply where the insolvency proceedings are terminated in connection with the entry into a settlement agreement.

Restraining Insolvency Proceedings Commenced in Bad Faith

A particular provision of the Resolution is aimed at preventing abuses by creditors¹⁴. It refers to instances where the debtor or its affiliated creditor files an insolvency petition so as to benefit improperly the debtor through insolvency procedures. Examples of such benefits might include any decrease in interest rates due to any accrual of moratorium interest, stay of enforcement proceedings or release from attachment. In such situations, if the debtor is solvent, then, taking into consideration the interests of creditors, the court may terminate the insolvency proceedings¹⁵. The debtor may then be obliged to pay the contractual (not moratorium) interest and penalties for the period of the insolvency proceedings.

Unification of the Creditors' Position

Prior to the adoption of the Resolution, interest and penalties with respect to the creditors' claims continued to accrue at the stage of supervision if the creditor did not apply for the registration of the claims on the creditors' register. If the creditor did so apply, then¹⁶ the amounts of claims were determined as of the claim's filing date and subsequently were not revised. The effect of this was that, at the stage of supervision, no interest or penalties accrued.

Hence, the creditor had to make a choice: it could submit an application for the inclusion of the claims in the creditors' register at the stage of supervision in order to participate in the first creditors' meeting and control the insolvency proceedings; alternatively, it could file a claim for registration at later stages of the insolvency proceedings while accruing interest and penalties during the supervision stage.

Pursuant to the introduction of the uniform moratorium interest at the supervision stage, the SCC has eliminated the aforementioned choice and made the position of both creditor groups identical. This is intended to encourage creditors to file their claims during the supervision proceedings and to facilitate the fulfilment of the rehabilitative function of the insolvency proceedings.

7 Para. 7 of the Resolution.

8 Para. 4 of the Resolution.

9 Para. 7 of the Resolution.

10 Para. 8 of the Resolution.

11 Para. 4 of the Resolution.

12 Para. 7 of the Resolution.

13 Ibid.

14 Para. 10 of the Resolution.

15 Paragraph 1, part 1, Article 150 of the Commercial Procedure Code of the Russian Federation.

16 By virtue of Article 71 of the Insolvency Law

Calculation of the Indebtedness to be Included on the Register in respect of the Unmatured Claims

The Resolution also clarifies the position in relation to the interest due under creditors' claims to be included on the register which have not yet matured as of the date of the insolvency proceedings.

The SCC sought to avoid situations where claims in the creditors' register include the interest for interest periods that have not yet occurred as on the date of the claims' registration.

This situation would occur if the amount of the principal debt determined by the parties to the obligation actually included the interest for the use of a loan (including a commercial loan). This might occur by way of increasing the common price of similar goods or the amount of a promissory note as compared with a loan issued by way of its acquisition¹⁷.

In this event, the court may reduce the amount of the claim to be registered in the creditors' register by the amount of the interest to be accrued between the commencement of the supervision stage and the maturity date of the obligation. This will occur at the average rate for short-term, working capital loans offered by credit institutions to business entities at the location of the debtor at the time the supervision stage is introduced.

In the event that the creditors' register includes the claims under a facility agreement providing for the priority repayment of the interest for the entire term of the facility utilisation, the amount of the outstanding principal debt shall be recalculated based on the amount of the interest accrued as on the date the supervision is introduced. Accordingly, in order to include the claims in the creditors' register, it will be deemed that a part of the principal debt has been repaid first, rather than the interest for interest periods that have not yet occurred.

Application of Certain Provisions of the Resolution

The provisions regulating the discounting of claims, the determination of and the procedure for accrual of moratorium interest in the course of supervision proceedings shall apply if the first insolvency proceeding was initiated after the Resolution publication (after 27 December 2013).

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¹⁷ Para. 3 of the Resolution.