

Legal Regulation of Insolvency (Bankruptcy) in Ukrainian Legislation

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Principles of Legislative Regulation of Bankruptcy



Ukrainian legislation that regulates insolvency (bankruptcy) of business entities can be ranked as follows:

- The *Commercial Code of Ukraine* containing some general principles on insolvency;
- The *Restoration of Solvency of a Debtor or Recognition of Bankruptcy Act of Ukraine*, approved on 30 June 1999. This specialized legal instrument contains both an interpretation of the main terms and detailed regulation of bankruptcy procedures, including the order and conditions of their initiation and the powers of participants, purposes, content and procedure;
- The *Code of Commercial Procedure of Ukraine* that regulates judicial proceedings in cases on insolvency;
- The *Criminal Code of Ukraine* that recognizes sham bankruptcy, intentional bankruptcy, and concealment of financial insolvency as crimes;
- A number of regulatory documents of authorized state bodies that help to run detailed regulation of legal relations arising during insolvency procedures.

Key Provisions

In Ukraine, the purpose of legal regulation of insolvency is to ensure the most effective satisfaction of legal requirements of creditors by a debtor that cannot satisfy such requirements. At the same time, regarding the two main ways that are implied in such cases in general practice — restoration of solvency of a debtor through measures of reorganization, management, investment, and technical, financial, and economic changes on one hand, and on the other hand recognition of a debtor to be bankrupt, with subsequent liquidation — Ukrainian legislation favors restoration of solvency. Among the legal procedures of bankruptcy, liquidation of a debtor is an extreme measure, and can only be applied when measures on restoration of solvency do not provide the required result.

It should be mentioned that legal proceedings on bankruptcy cases with the participation of creditors who are non-residents is generally regulated by the *Restoration of Solvency of a Debtor or Recognition of Bankruptcy Act*



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of Ukraine. Exceptions can be stipulated by international agreements to which Ukraine is a party.

The following entities participate in legal relations that arise in connection with insolvency of a business entity:

Debtor — a business entity that is unable to meet liabilities to creditors, including obligations on payment of taxes and other mandatory payments in the course of three months after the due date of payment. A debtor himself can initiate a bankruptcy case, and in some instances, initiation is the duty of a debtor.

Creditors — both legal entities and individuals that have claims confirmed by documents on liabilities, including demands of workers of the debtor about payment of arrears, and also tax and other state bodies that supervise payment of taxes and other mandatory payments. Creditors can include persons whose claims to the debtor arise before the legal proceedings on bankruptcy (competitive creditors), and after such proceedings begin (current creditors). After a court approves a register of claims, creditors establish a committee that is authorized to cooperate with the court and the arbitration manager.

Arbitration Manager — the key person in a case of insolvency, during legal proceedings has influence on the efficiency of legal proceedings of bankruptcy and, ultimately, the efficiency of satisfaction of creditors' claims. According to the requirements of legislation, an obligatory provision for arbitration managers is a higher legal or economic education, or possession of special knowledge. The work of an arbitration manager is subject to licensing by an authorized state body. Depending on the legal procedure applied during consideration of a bankruptcy case, an arbitration manager carries out the functions of an administrator of the debtor's property, a rehabilitation manager, or a liquidator. He or she analyzes and introduces the registered creditors' claims, fully supervises the activity and property of a debtor during litigation and, in procedures regarding rehabilitation and liquidation, acts as the head of a debtor. An arbitration manager is appointed by a court in view of creditors' suggestions.

Court — bankruptcy cases are considered by specialized (commercial) courts of Ukraine at a location of the debtor. In courts of first instance, a judge considers bankruptcy cases individually. The judge makes a decision on initiation of a bankruptcy case upon applications by a debtor or creditors; introduces a moratorium on creditors' claims; starts judicial bankruptcy procedures; appoints an arbitration manager, an administrator of property, a rehabilitation manager, and a liquidator of a debtor; approves the register of creditors'

claims; forms an amicable agreement; and performs other functions in accordance with Ukrainian legislation.

The Ministry of Economy of Ukraine — in the capacity of an authorized state body on bankruptcy issues, it performs the organization and preparation of arbitration managers and licensing of their activity; suggests arbitration managers to courts; maintains a uniform database of enterprises that have bankruptcy cases initiated against them; and performs other functions stipulated by legislation.

Ukrainian legislation stipulates the following bankruptcy procedures:

The purpose of the **administration of a debtor's property** is securing the property claims of creditors. This procedure can start immediately after initiation of a bankruptcy case. An arbitration manager administers property and his powers include safety of the available property of a debtor; analysis of financial, investment and economic activities; consideration of claims declared by creditors; and introduction of the latter into the register. At this stage, the supervisory bodies of a debtor preserve some of their powers: in instances established by legislation their decisions should be coordinated with the property's administrator.

The decision on the **procedure of rehabilitation (restoration of solvency) of a debtor** and appointment of a rehabilitation manager is approved by a court upon a corresponding application by a committee of creditors. The term of rehabilitation procedures can vary from six to 18 months. Since the court's decision on rehabilitation, all the management rights of a debtor pass to a rehabilitation manager. Such a person receives the right to dispose of debtors, to conclude civil and labor agreements on behalf of a debtor, to conclude amicable agreements, and to file applications on recognizing agreements made by a debtor as void. However, the activity of a rehabilitation manager is supervised by a committee of creditors.

The recognition of a debtor to be bankrupt and the commencement of a **liquidation procedure** imply termination of the economic activities of a debtor and formation of a liquidation value, which include, with minor exceptions, assessing the assets of a bankrupt individual or entity that belong to him or it on the basis of property rights, and subsequent sale of that property in an open auction.

Finally, conclusion of an **amicable agreement** between a debtor and creditors concerns delay and/or payment by installment or writing-off of debts in a situation when satisfaction of creditors' claims is believed improbable. This allows the avoidance of further expenses for proceedings and also allows the debt to be included into gross expenses as bad debt.

As regards the sequence of satisfaction of creditor's, presumed by Ukrainian legislation, priority in this case granted to the secured claims, obligations of a bankrupt enterprise to workers and also taxes and mandatory payments.

A brief description of some of the most significant features of insolvency legal proceedings according to Ukrainian legislation is necessary:

- Litigation on bankruptcy can be initiated by a court when indisputable claims of a creditor (creditors) to a debtor exceed UAH 300 in minimum wages and were not satisfied by a debtor in the course of three months after the term established for repayment. To date the minimum amount of a debtor's debt that allows the initiation of a bankruptcy case totals UAH 71,100.

• Simultaneously with initiation of a bankruptcy case, a court introduces a moratorium on satisfying creditor's claims that applies to liabilities and obligations on payment of taxes and duties that were due prior to the date of the moratorium. The moratorium does not apply to payment of wages, alimony, or compensation of damage caused to the health and life of citizens or to a copyright.

• The powers of a debtor's management during the procedure for administration of property can be suspended upon petition by creditors and assigned to an arbitration manager in the event of failure to take measures to secure the property, curbing the actions of an arbitration manager, and other violations of legislation.

• Creditor's claims against the debtor that have occurred prior to the date of a bankruptcy case should be declared within 30 days from the date of an official publication on initiation of a bankruptcy case. Claims declared after the specified term, or not declared at all, shall not be considered and are recognized as paid.

• The term of consideration of a bankruptcy case is formally limited to seven months, after which a court should make a decision on the rehabilitation of a debtor, either recognizing that debtor as bankrupt and starting a liquidation procedure or terminating the case. Nevertheless, in practice such litigations can last more than two years.

PRO file

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