



THE SUPREME COURT HAS CLARIFIED CERTAIN ISSUES RELATING TO THE BANKRUPTCY OF INDIVIDUALS

FOA: heads and employees of companies' legal, finance and litigation departments.

Pepeliaev Group advises: On 13 October 2015, the Russian Supreme Court adopted its Plenum's Resolution No. 45 "On certain issues relating to procedures being brought into effect to be used in insolvency (bankruptcy) proceedings involving individuals". This clarifies how specific provisions of Federal Law No. 127-FZ "On insolvency (bankruptcy)" should be implemented. The provisions in question came into force on 1 October 2015 and regulate the bankruptcy of individuals.

Please find below an outline of the most important clarifications mentioned above.

The Russian Supreme Court has indicated which requirements should be complied with for a bankruptcy lawsuit involving a debtor (an individual) to be initiated.

The Russian Supreme Court explained that, for bankruptcy lawsuits involving individuals to be initiated, consideration is also to be given to the claims of creditors and an authorised body, which arose before 1 October 2015.

The provisions of the Law on the bankruptcy of individuals equally apply to individuals who enjoy the status of an individual entrepreneur.

From 1 October 2015 on, the provisions which regulate the bankruptcy of individuals apply to individual entrepreneurs, irrespective of whether or not there has been any connection between their entrepreneurial activities and the fact that certain requirements were not complied with, resulting in the bankruptcy lawsuit being initiated. If an individual enjoys the status of an individual entrepreneur, only one bankruptcy lawsuit may be initiated and considered.

Aspects of confirming the place of residence of a bankrupt individual.

As the Russian Supreme Court has explained, since bankruptcy proceedings are considered by a commercial ('arbitration') court at the relevant individual's location, the debtor's place of residence may be confirmed with documents certifying the debtor's registration, or with an excerpt from the Unified State Register of Individual Entrepreneurs, in line with article 20(1) of the Russian Civil Code, article 2(4) and article 3(2) of Law of the Russian Federation No. 5242-1 "On the right of citizens of the Russian Federation to move freely and choose their place of temporary and permanent residence within the Russian Federation" dated 25 June 1993, and article 5(2) and article 6 of Federal Law No. 129-FZ "On the state registration of legal entities and individual entrepreneurs" dated 8 August 2001.

To verify the information relating to the individual's place of residence as indicated in the bankruptcy petition against the debtor, the court may, when preparing the case file for the proceedings, request information concerning the debtor's place of residence from the relevant registration bodies.

If there is no information about the individual's place of residence or if such individual is staying outside the Russian Federation, this is not an obstacle to a bankruptcy lawsuit being initiated at the most recent known place where the individual resided in the Russian Federation.

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To prevent a bad-faith debtor (individual) or such debtor's creditors from initiating several bankruptcy lawsuits, or to avoid a bankruptcy lawsuit being initiated other than at the place of such individual's residence, we recommend that measures be taken to identify the most recent place of residence of the individual, and check whether commercial ('arbitration') courts of other regions are considering any bankruptcy cases involving the same individual.

A court declares an individual's bankruptcy petition groundless if on the next day after the petition had been filed, the applicant's claim was not confirmed by an effective court decision, and at the same time there is a dispute regarding the law.

Whether or not there is a dispute regarding the law may be evidenced by any objections, both oral as well as written, raised by the individual debtor against a claim of a bankruptcy creditor or an authorised body, if such objections concern the existence of any debts, the amounts of them and the timeframe for performing the obligation.

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To oppose a debtor's unlawful actions, namely, the debtor's unsubstantiated objections to a bankruptcy creditor's indisputable claims, it would be reasonable to provide the court with evidence that the debtor's actions amount to an abuse of the debtor's rights and are obviously aimed at putting off the start of the bankruptcy proceedings.

Grounds for not applying to a debtor (an individual) the rule providing that the debtor may be exempted from its liabilities.

The possibility for a court to refuse to exempt an individual from performing his/her obligations represents one of the crucial guarantees that the creditors' rights will be protected against bad-faith debtors' actions. The Russian Supreme Court has explained that one of the possible grounds for a debtor not to be exempted arises where the debtor is not complying with his/her duty to provide a response to the bankruptcy petition and documents provided for by legislation, and where the debtor provides inaccurate or incomplete information.

If the circumstances in which a debtor (an individual) cannot be exempted from his/her liabilities are identified after the debtor's property has been sold, the court may reconsider this issue at the initiative of a bankruptcy creditor, an authorised body or a financial administrator.

The Russian Supreme Court has confirmed that none of the parties who have initiated a bankruptcy lawsuit may put forward a specific person to act as a court-appointed administrator.

The Resolution additionally explains the procedural implications of a petition filed to initiate a bankruptcy case if either no self-regulating organisation has been specified or a specific financial administrator has been appointed.

The costs incurred on persons whom the financial administrator has engaged to procure his/her work are borne by persons who have consented to the above persons being engaged.

The Russian Supreme Court has explained that if a bankruptcy creditor, an authorised body or a financial administrator has agreed that the services provided by the engaged persons should be paid for, then the costs incurred by such persons should not be covered at the debtor's expense. At the same time, where services are provided by a court-appointed administrator, whom the petitioning creditor involved in the bankruptcy proceedings and the fees for such services have been placed into the court's deposit account,

these may be repaid to the creditor in the form of current payments if it is identified that the amount of property owned by the debtor is enough for the fee to be paid to the financial administrator.

The court may restore the period for claims to be raised against a bankrupt individual.

If a bankruptcy creditor (an authorised body) fails to submit its claims within a bankruptcy lawsuit involving a debtor (an individual) within two months, the court may restore this period for a good reason. This period may be restored until the date on which the first meeting of the debtor's (the individual's) creditors is scheduled, which offers an opportunity to participate in this meeting.

If a claim is raised outside the above period or in the event of a refusal to restore such period in order to provide an opportunity to participate in the first meeting of the debtor's creditors, this is not a ground for a court to decline to consider this claim for the purpose of including it in the register. These claims, if included in the register of claims of the debtor's creditors, are settled in line with the general conditions for doing so. However, if a claim has been raised late during the process of selling a debtor's property, such claim may be only settled after the claims of the creditors included in the register are settled.

The period for filing claims associated with a bankruptcy case involving an individual starts on the date of the latest official notification.

The Russian Supreme Court has explained that, when determining the starting date of the period within which a claim may be filed in relation to an individual's bankruptcy case, the date of the latest official notification should be taken as a point of reference.

A court may approve a plan for restructuring debt only if this plan has been approved by the debtor.

A plan may be signed off without the debtor's approval only in exceptional cases, i.e. if proof is available that the debtor, in rejecting the plan, is committing an abuse of right (article 10 of the Russian Civil Code). A court does not approve a plan for restructuring debt if, economically speaking, such a plan is deliberately impracticable. However, a plan for restructuring debt may provide that the goal, i.e. to restore the debtor to solvency, will be considered as achieved if, after the plan has been implemented, the debtor has no arrears and can continue to meet its obligations which have not yet matured (without reference to article 213.11(2) (2) of the Bankruptcy Law). A plan for restructuring debt may be revoked by court.

To prevent the approval of a deliberately groundless restructuring plan that has been proposed by the debtor or any creditors, we recommend that you insist on an expert economic analysis being scheduled, or provide other proof that to implement this plan is impracticable.

The Supreme Court has explained how the provisions of the Bankruptcy Law should be applied in terms of the debtor's (individual's) property being sold.

The general rules of article 139(1.1) of the Bankruptcy Law set out how the procedure, conditions and terms of selling property are approved by the meeting (board) of creditors; these rules are applied only when bankruptcy cases are considered which involve individual entrepreneurs and individuals who have lost this status, and when property is sold which was intended for the commercial activities of such individuals.

Conclusions and recommendations

The Resolution has left unexplained a considerable number of contentious issues which have arisen in relation to the entry into force of the rules for procedures applied in bankruptcy lawsuits involving individuals. Foremost among these are the implications of violating the rules which restrict the right to dispose of the debtor's property. In this regard, it remains somewhat difficult to assess the risks associated with an individual counterparty's potential bankruptcy. This would require account to be taken of previous bankruptcy practice involving individuals and legal entities.

Help from your adviser

Pepeliaev Group's experts have an extensive track record of protecting any categories of persons involved in the procedures which are used in insolvency (bankruptcy) lawsuits, including those featuring individual entrepreneurs. Our lawyers are well placed to assess the risks associated with the institution of individual bankruptcy being introduced.

Legal alert

28 октября 2015 года

For any explanations or advice, please contact Yulia Litovtseva, Head of Bankruptcy and Anti-Crisis Protection of Business.

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