

Resolution of the Cabinet of Ministers of Ukraine No. 711 dated 24 May 2006 is aimed at improving the current situation. It broadens the powers of the inspector and introduces a number of new methods of control:

- the inspector is now entitled to control not only the legitimacy of the production and distribution of IP objects, but also the legitimacy of use of such objects; and
- the inspector may now conduct scheduled and unscheduled inspections during which he is entitled to seize objects of intellectual property or any material data mediums which contain these objects for a term of up to 30 days.

The inspector has a right to access every original document confirming the legitimacy of use of the intellectual property object as well as the right to access the premises where the documents are placed or stored.

14. BANKRUPTCY ISSUES

14.1 General

Ukraine's first *Law on Bankruptcy* was adopted on 14 May 1992. On 30 June 1999, this Law was significantly amended and restated, and now exists as the *Law "On Re-establishing the Solvency of Debtors or the Recognition of Debtors' Bankruptcy"* (the *Bankruptcy Law*). The Bankruptcy Law came into effect on 1 January 2000.

The *Bankruptcy Law* and certain other Ukrainian legislation establish a number of fundamental principles, which must be borne in mind when doing deals with potential Ukrainian debtors (Debtors).

14.2 Debtors Exempt from Bankruptcy

Under the applicable Ukrainian legislation, the following Debtors have absolute or limited immunity from bankruptcy procedures:

- (1) state enterprises, which fall under the category "*kazenne pidpryyemstvo*;"
- (2) municipal enterprises, which were exempted from the application of the *Bankruptcy Law* by the relevant decision of the local self-governing body;

- (3) mining companies, in which the state holds at least 25 per cent of the shares, until 1 January 2010;
- (4) enterprises of the fuel and energy sector of Ukraine, which have been included into the register of enterprises undergoing a debt recovery procedure; and
- (5) former companies of the State Joint Stock Company “Ukrudprom”, which have been privatized in accordance with the Law of Ukraine “*On Specific Features of Privatisation of Enterprises of the State Joint Stock Company “Ukrudprom”*” dated 9 April 2004. A moratorium, effective until May 2009, is introduced, *inter alia*, on the institution of property administration procedure (an initial bankruptcy proceedings stage) against any of the former State Joint Stock Company “Ukrudprom” companies.

14.3 Specifics of Bankruptcy Proceedings for Certain Categories of Debtors

Bankruptcy proceedings for certain categories of Debtors have important specific features, as compared with the generally applicable bankruptcy regime. Such categories of Debtors include banks, insurance companies, securities traders, issuers or managing companies of the mortgage certificates, managers of the utility (construction financing) funds, managers of real property operation funds, city-forming (giant) enterprises, enterprises with dangerous production facilities (*e.g.*, chemical, coal, nuclear, or metal producers, which have been recognized as dangerous manufacturers by a decision of the Cabinet of Ministers of Ukraine), agricultural producers, farms, private (individual) entrepreneurs, missing debtors and the debtors liquidated by their owners. Specific features of the bankruptcy proceedings for such enterprises include special terms and conditions of the bankruptcy proceedings, a special list of priorities for the satisfaction of creditors’ claims, extension of the term of the bankruptcy hearings, special sale procedures, and restrictions on the attachment of the Debtor’s assets.

14.4 Initiation of Bankruptcy Proceedings

A bankruptcy petition may be brought to a Ukrainian commercial court (“*hospodarsky sud*”) at the place of the Debtor by any creditor (other than a fully-secured creditor), the Debtor itself, the State Tax Administration and certain other state agencies

acting as the creditors. A creditor may be any individual or business entity, which possesses an incontestable claim against the Debtor in an amount of not less than 300 individual monthly minimum salaries (starting from 1 January 2009 - UAH605, which amounts to US\$78.57; from 1 April 2009 - UAH625, which amounts to US\$81.17; from 1 July 2009 - UAH630, which amounts to US\$81.82; from 1 October 2009 - UAH650, which amounts to US\$84.42; from 1 December 2009 - UAH669, which amounts to US\$86.88), and whose claim was not satisfied within three months after the expiration of the established term for its initial satisfaction.

In principle, there are two ways in which a creditor may participate in bankruptcy proceedings: a creditor may either bring the bankruptcy petition itself or, if another party has already initiated the bankruptcy proceedings, it may join such proceedings by way of filing a participation petition.

Once the bankruptcy proceedings have been triggered, any creditor (except a fully-secured creditor) may within 1 month from the formal publication in one of the state official newspapers (“Golos Ukrainy” or “Uriadovy Kurier”) of the commencement of the bankruptcy proceedings against the Debtor, may submit a participation petition substantiating its claims against the Debtor. Claims submitted after the expiration of the period established for their submission will not be considered and their debts will be deemed extinguished.

A creditor, whose claims are fully-secured by collateral, is deemed to be a secured creditor, and as a matter of law, may not initiate bankruptcy proceedings. If a secured creditor considers that its claims are not fully-secured, or if the collateral has been lost/absent, then it can initiate bankruptcy proceedings/participate as a creditor with respect to the unsecured part of its claims or of all its claims.

14.5 Stages of Bankruptcy Proceedings

Under Article 4 of the Bankruptcy Law, the judicial bankruptcy proceedings in Ukraine include the following stages:

- (1) special proceedings for the disposal of the Debtor’s assets (the assets management proceedings);
- (2) amicable settlement;
- (3) solvency renewal (sanation) proceedings; and
- (4) liquidation proceedings.

Under the assets management proceedings, the Ukrainian commercial court will appoint a bankruptcy trustee (*rozporядnyk mayna*), who will supervise and approve the disposal of the Debtor's assets. The court may impose a moratorium on the discharge of any of the claims of the Debtor's creditors, which have arisen before the date of the initiation of the bankruptcy proceedings. This moratorium may last until the completion of the liquidation of the Debtor.

A bankruptcy trustee is an individual, who is registered as a private entrepreneur, and is licensed to act as the manager of the Debtor's assets, the solvency renewal trustee and the liquidator at the respective stage of the bankruptcy proceedings.

In the assets management proceedings, which may last about three months from the day of commencement of the bankruptcy proceedings, the bankruptcy trustee identifies the creditors, prepares the Register of the Creditors and the Amounts Claimed from the Debtor for further approval by the court, organizes the general meeting of the Debtor's creditors, which in turn, appoints the creditors' committee (the "Committee").

Upon election of the Committee, the committee is entitled to initiate the solvency renewal proceedings and/or the liquidation proceedings against the Debtor, to agree on the terms and conditions of the solvency renewal plan and to apply to the court for its approval, to provide the court with the candidates for the appointment of the solvency renewal trustee and the liquidator, as well as to apply for their replacement, to agree on the terms and conditions of the amicable agreement and to apply to the court for its approval, and to decide on other practical issues of the bankruptcy proceedings.

The creditors participating in the General Meeting of the Creditors or in the meetings of the Committee have the votes in the amount which is determined on the pro rata basis of their respective claims, and they make their decisions by the majority of the votes.

The solvency renewal proceedings may be introduced by the court as the next stage of the bankruptcy proceedings for the period of twelve months on the basis of the relevant request made by the Committee. The period of the solvency renewal proceedings may be extended by the court for the additional six months period upon request of the Committee, the solvency renewal trustee or the investors.

By the ruling on the introduction of the solvency renewal proceedings the court appoints the solvency renewal trustee, who will act as the head of the Debtor. For the period of the solvency renewal proceedings the other managing bodies of the Debtor are not able to exercise their statutory powers.

The solvency renewal trustee ought to prepare the solvency renewal plan and provide it to the Committee for approval within three months from the day of the court ruling on appointment of the trustee. If the Debtor is the state owned company with the share of the state not less than 50%, the solvency renewal plan is subject to approval by the state authority supervising the disposal of this property.

The solvency renewal plan may include corporate restructuring of the Debtor, sale of its assets, recovery of the receivables, debt restructuring, restructuring of assets, sale or cancellation of the debt and the other means of renewal of the Debtor's solvency.

Upon approval of the solvency renewal plan by the Committee, the solvency renewal trustee ought to submit it to the court for the consideration and the final approval. If the solvency renewal trustee fails to provide the solvency renewal plan to the court for approval within six months from the day of commencement of the solvency renewal proceedings, the court may recognize the Debtor as the bankrupt and introduce the liquidation proceedings as the final stage of the bankruptcy proceedings.

The court may also introduce the liquidation proceedings with the relevant ruling, if the Debtor has failed to restore its solvency in accordance with the solvency renewal plan, on the basis of the Committee's request.

It should be noted that the Committee may ask the court for introduction of the liquidation proceedings after the assets management proceedings omitting the solvency renewal proceedings.

By the ruling on the introduction of the liquidation proceedings the court appoints the liquidator, who will act as the head of the Debtor. For the period of the liquidation proceedings the other managing bodies of the Debtor are not able to exercise their statutory powers.

In the liquidation proceedings the liquidator ought to determine the liquidation value of the Debtor's assets, to sell these assets and to pay off the debt to the creditors in accordance with the priority list for the satisfaction of the creditors' claims as established by the law.

Upon completion of the liquidation proceedings, the liquidator prepares the report, as well as the liquidation balance sheet of the Debtor, and provides them to the court for the consideration and approval. Based on the results of the liquidation proceedings the court may approve the report and the liquidation balance sheet of the Debtor, dissolve the debtor and terminate the bankruptcy proceedings.

According to the Bankruptcy Law, the term of liquidation proceedings amounts to twelve months from the day of commencement, but it may be extended by the court for the additional six months period.

At any stage of the bankruptcy proceedings the creditors and the Debtor may enter into an amicable agreement with a view to restructuring and/or cancellation of the debt. The first priority debt, except the debt secured by a pledge (mortgage), cannot be cancelled or restructured, and the debt arising from the mandatory pension and social security contributions cannot be cancelled by the amicable agreement.

The parties of the amicable agreement may agree on the transfer of the debt to third parties or the transfer of the Debtor's assets or the corporate rights in the Debtor to its creditors in exchange for the cancellation of the debt.

The amicable agreement is subject to approval by the court and becomes effective from the day of the relevant court decision. By the ruling on approval of the amicable agreement the court terminates the bankruptcy proceedings.

It should be noted that the amicable agreement may be invalidated by the court on the legal grounds provided by the Civil Law of Ukraine. In case of invalidation of the amicable agreement, the court may reinstate the bankruptcy proceedings against the Debtor.

The creditors may apply to the court for the termination of the amicable agreement in case of non-performance of this agreement by the Debtor with regard to not less than one third of the total amount of the debt. The termination of the amicable agreement for the specific creditor or creditors will not result in the termination of the agreement for the rest of the creditors, and reinstatement of the bankruptcy proceedings.

14.6 Priority of Claims

Amounts received from the sale of the bankrupt's assets will be used to pay the claims of its creditors and others in the following order:

(1) *Claims of the First Priority:*

- claims of creditors secured by a pledge (mortgage) of the bankrupt's assets (up to the value of the relevant collateral);
- the payment of termination allowance to the bankrupt's employees, and repayment of any loan received by the bankrupt for the purpose of the payment of such termination allowances;
- claims of the Individual Deposit Guarantee Fund for the amounts paid by the Fund to the creditors of the insolvent bank;
- claims of the creditors under insurance agreements; and
- expenditures associated with the conduct of the bankruptcy proceedings and the expenses of the liquidators;

(2) *Claims of the Second Priority:*

- liabilities to the bankrupt's employees (other than those included as the first and fifth priority claims listed hereby);
- liabilities arising from the infliction of harm to the life or health of an individual, by means of capitalization of the respective payments, *inter alia*, to the Employment Injuries and Occupational Diseases Insurance Social Fund regarding the employees, insured in this fund;
- liabilities relating to the mandatory pension and social security contributions; and
- claims of individuals arising from their property or funds having been deposited with the bankrupt (if the bankrupt is a trust company ("*dovirche tovarystvo*"), a bank or other "credit-financial institution," or any other business entity attracting the assets of individual depositors);

(3) *Claims of the Third Priority:*

- local and state taxes and other mandatory payments; and
- claims of the State Reserve Fund;

(4) *Claims of the Fourth Priority:*

claims of creditors not secured by a pledge (mortgage) of the bankrupt's assets (other than the claims of the fifth priority and the sixth priority), including claims which have arisen during the assets management proceedings or the solvency renewal proceedings;

(5) *Claims of the Fifth Priority:*

claims for the "repayment of the bankrupt's employees' contributions to the charter fund" of the bankrupt; and

(6) *Claims of the Sixth Priority:*

"all other claims."

Claims with a higher priority must be satisfied in full before any lower ranking claims may be paid. In the event that the cash proceeds from the sale of the property are insufficient to satisfy all claims with equal priority, then all claims with the same priority are to be satisfied pro-rata. Claims not paid due to the insufficiency of funds shall be deemed extinguished. Any assets remaining after the satisfaction of the claims of the creditors and the employees are to be distributed to the "owners" of the Debtor (*i.e.*, its shareholders or holders of its participatory interests), if the court decides to dissolve the Debtor. The court is not able to dissolve the Debtor, if the remaining assets of the Debtor exceed the amount of assets which is required by the law for the establishment of the relevant legal entity.

Note that Ukrainian legislation establishes a special order of priority of satisfaction of creditors' claims for certain categories of debtors (including banks).

14.7 Criminal Liability

Under the *Criminal Code of Ukraine*:

- (1) an intentional concealment by an individual-participant/shareholder or by an owner of a subject of entrepreneurial activity, as well as by an

- officer of a subject of entrepreneurial activity, of the sustainable financial insolvency of such subject by means of the filing of untrue information, if such activity has caused substantial material damages (US\$1,103.89) to a creditor or the state, is punishable with a monetary penalty from 2,000 to 3,000 monthly non-taxable incomes of individuals (currently UAH34,000 - 51,000, which amounts approximately to US\$4,415.58 - 6,623.38), or with imprisonment for a term of up to 2 years with the deprivation of the right to occupy certain positions or to conduct certain activities for a period up to 3 years;
- (2) the willful making of an untrue statement (verbal or in writing) by a company's official about its financial incapability to meet the claims of its creditors and its obligations to make budget contributions, if such activity has caused substantial material damages (US\$1,103.89) to a creditor or the state, is punishable with a monetary penalty from 750 to 2,000 monthly non-taxable incomes of individuals (currently UAH12,750 - 34,000, which amounts approximately to US\$1,655.84 - 4,415.58), or with imprisonment for a term of up to 3 years;
- (3) "letting bankruptcy," *i.e.*, the intentional activity, with mercantile motives or other personal interests, or in the interest of third parties, of the owner or corporate official of an enterprise, which has caused the sustainable financial incapability of such enterprise, if such activity has caused substantial material damages (US\$1,103.89), is punishable with a monetary penalty from 500 to 800 monthly non-taxable incomes of individuals (currently UAH8,500 - 13,600, which amounts approximately to US\$1,103.89 - 1,766.23), (with the deprivation of the right to conduct certain activities for a period of up to 3 years); and
- (4) an intentional concealment of property or information about the property, or about transfers of the property, of an insolvent company by its owners or corporate officials, which resulted in significant damages (US\$1,103.89), is punishable with a monetary penalty from 100 to 500 monthly non-taxable incomes of individuals (currently UAH1,700 - 8,500, which amounts approximately to US\$220.78 - 1,103.89), or with imprisonment for a term of up to 3 months with the deprivation of the right to occupy certain positions or to conduct certain activities for a period of up to 3 years.