

Client Alert on Proposed Amendments to the Law on Banks

April 12, 2017

On April 7, 2017, the Azerbaijani Parliament passed in the first reading a Draft Law “On Introducing Amendments to the Law “*On Banks*” (the “**Draft Law**”).

The Draft Law, once adopted and signed into law, will introduce significant changes to the cornerstone of banking legislation in the country, completely rewriting sections of the law dealing with the appointment of temporary administration and the financial rehabilitation of troubled banks. The Draft Law comes at the time when liquidations in bankruptcy of several small and mid-sized Azerbaijani banks are currently underway, in relation to one of which (Bank Standard) the newly established regulator, the Financial Markets Supervisory Authority (the “Regulator” or “FIMSA”) attempted, unsuccessfully, to introduce a financial rehabilitation program.

We summarize the major aspects of the Draft Law below:

Disposition of an Insolvent Bank

A new section is proposed to be introduced to the Law on Banks, entitled “Disposition of an Insolvent Bank”, which would deal with various matters related to the appointment of a temporary administrator by FIMSA for an initial period of nine months, which could be extended for a further three months. This section sets forth in detail events that would warrant the appointment of a temporary administrator by FIMSA, the principles under which the temporary administrator would manage the insolvent bank and the powers of the administrator, as well as the possible outcomes for troubled banks. These include the following:

- merger of an insolvent bank into a healthy bank;
- transfer of assets and liabilities of an insolvent bank (fully or partially) to an acquiring bank;
- establishment of a bridge bank, the transfer of healthy assets and liabilities of an insolvent bank (fully or partially) to the bridge bank, and the sale of the bridge bank to investors;
- sale of an insolvent bank to investors;
- liquidation of an insolvent bank.

Voluntary debt restructuring of bank obligations

Another important novelty in the Draft Law is a previously unavailable framework that would allow banks to force a voluntary debt restructuring of the bank’s obligations vis-à-vis its creditors, except for claims of depositors that are eligible for deposit insurance.

According to the Draft Law, the process of voluntary debt restructuring begins with a resolution of the Supervisory Board of the bank if a bank is not able to comply, or there is a risk of the inability on the part of the bank to comply,

with the demands of its creditors due to the absence or lack of funds or the impossibility to use funds for other reasons. FIMSA will then have up to 20 calendar days to review the resolution of the Supervisory Board and to enter into a written agreement with the bank.

The bank then would prepare a draft restructuring plan to be submitted to FIMSA for its approval, after which the bank would file an application with a court asking for approval of the commencement of the voluntary restructuring of the bank's obligations. The bank would be required to publish notices in the local and international press about the court decision, as well as inform its creditors of the obligations which are subject to restructuring.

From the effective date of the court decision on the voluntary restructuring of the bank's obligations, the bank would be entitled:

- to suspend performance of sale and purchase, exchange and gift agreements, or any other agreements providing for the disposal of any assets of the bank, and to suspend the conclusion of agreements creating any risks for the bank, including, loan, credit and guarantee agreements or agreements providing any kind of financing;
- to suspend, in full or in part, the performance of the obligations that are subject to restructuring.

The above-mentioned restrictions would apply for 180 calendar days, a term that could be extended for up to 90 calendar days upon application of the bank, as acknowledged by FIMSA.

The bank would be able to introduce changes to the draft restructuring plan in the course of the voluntary debt restructuring of the bank's obligations, in which case such amendments must be submitted to the Regulator for approval 30 calendar days prior to the creditors' meeting. Once approved by the Regulator, the final draft of the restructuring plan would be presented for creditors' approval during a creditors' meeting. The restructuring plan would be approved by creditors holding at least two-thirds of the total bank obligations which are subject to restructuring, and will be binding for all creditors, claims of which have been included into the restructuring plan. Once approved by the creditors, the restructuring plan would be presented to the court for final approval.

ADIF to be appointed to all bank liquidations

The Draft Law seems to codify the established practice of appointing the Azerbaijan Deposit Insurance Fund ("ADIF") as the liquidator and the bankruptcy liquidator of local banks. It also envisages that the Regulator will oversee the activities of the liquidator of a bank.

Potential personal liability of bank administrators

Finally, in addition to other sweeping powers that a liquidator of a bank would have, the Draft Law introduces the authority to investigate the circumstances that lead to the bank's liquidation and to inform the relevant authorities of the results of its investigation, including the names of any potential suspects, as well as to apply to a court seeking compensation for damages suffered by the bank as a result of the actions or inaction of such suspects. The current language of the Draft Law is rather broad and could be interpreted to include bank administrators (members of the management and supervisory boards of the bank, heads of its branches, etc.) and possibly even shareholders of the bank.

Note: This Client Alert is based on the Draft Law dated April 7, 2017, retrieved from the official website of the Parliament of Azerbaijan. As of the date of this Client Alert, we understand that the Draft Law has passed only the first reading, so its text may be subject to further revision.

Law stated as of April 11, 2017.

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