

INSOLVENCY LAW AMENDED TO FURTHER PROTECT COLLATERAL ARRANGEMENTS AND CLOSE-OUT NETTING IN RUSSIA

On 27 December 2019 the Russian President signed into law the latest set of amendments (the "**Amendments**") to Federal Law No. 127-FZ On Insolvency (Bankruptcy) of 26 October 2002 (the "**Insolvency Law**"). The Amendments are intended to give greater protection, in the context of insolvency of a Russian counterparty, to collateral arrangements and close-out netting in respect of over-the-counter derivative, repurchase and certain other "financial" transactions documented under eligible master agreements. The Amendments took effect on 8 January 2020 and are summarised below.

IMPACT ON TRANSACTIONS AND COLLATERAL ARRANGEMENTS

The Amendments significantly limit the grounds for challenging as a "preferential transaction" (i) the execution of a transaction, including the making of a collateral arrangement, and (ii) the payments made / deliverables provided under such transaction, where:

- the relevant transaction/collateral arrangement in question was made at least one month before the court accepted the insolvency filing against Russian counterparty / temporary administration in relation to the Russian counterparty was introduced (where Russian counterparty is a financial institution); and
- the other party to the transaction/collateral arrangement had no knowledge that the Russian counterparty met the "insufficiency of assets" test (a debtor's liabilities exceeding the value of its assets) or the "inability to pay" test (a debtor's failure to meet its debts as they fall due, on account of having insufficient funds).

That said, as far as collateral arrangements are concerned, it is likely that the above protections will be available only to title transfer collateral arrangements. For example, in terms of ISDA documentation, it would be the 1995 ISDA Credit Support Annex (Transfer-English Law) and the ISDA 2016

Credit Support Annex for Variation Margin (VM) (Title Transfer-English Law) that are likely to benefit from these protections.

IMPACT ON CLOSE-OUT NETTING

New Eligibility Requirements for Master Agreements

According to the Amendments, early termination and close-out netting cannot be challenged as a preferential transaction, provided that the relevant master agreement was executed at least one month before the court accepted the insolvency filing against Russian counterparty / temporary administration was introduced in relation to the Russian counterparty that is a financial institution.

The Amendments require that the net termination amount be calculated within the time limit set out in the master agreement. However the Amendments are silent as to whether or not, in the context of insolvency of a Russian counterparty, close-out netting is possible under a master agreement that does not contain such a time limit or does not define it in precise terms¹.

Netting Across Different Master Agreements Is Allowed

The Amendments allow close-out netting under more than one master agreement between the same parties, unless one of the master agreements came to be in place between the parties as a result of a succession (assignment) that occurred during one of the suspect periods established by the Insolvency Law (the standard suspect period is one month prior to the date the court accepted the insolvency filing in relation to the Russian counterparty / one month prior to the date the Russian counterparty's banking licence was revoked; if the parties to the master agreement are related parties or if one of the parties knew at the time of the succession (assignment) that the other party had "insufficiency of assets" or "inability to pay", then extended suspect periods apply).

Impact of Challenging a Transaction on the Net Termination Amount

The Amendments make it clear that if a particular transaction documented under a master agreement or a payment / delivery under such an agreement is successfully challenged after early termination and close-out netting have already occurred, this does not invalidate the entire close-out netting; rather, the net termination amount must be adjusted "*in accordance with the procedure set out in the master agreement*". This wording can be interpreted to mean that in order for a master agreement to be eligible for close-out netting in the context of insolvency of a Russian counterparty, the agreement must explicitly specify such adjustment procedure.

¹ For example, according to Section 6(d)(i) of the 1992/2002 ISDA Master Agreement, the time limit is drafted as "[o]n or as soon as reasonably practicable following the occurrence of an Early Termination Date...".

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