Business Reorganisation Assessment

Azerbaijan

European Bank
for Reconstruction and Development

Special thanks to:

Dentons
Omni Law Firm

Part A

General Information

Macro Data

10.101	+2.3%	US$ 4,880	Azerbaijani manat – AZN	20%	3.5%	5.8%
Population (million)[1]	GDP growth rate[1]	GDP per capita[1]	Currency	Corporate tax rate[2]	Inflation rate[1]	Unemployment rate[1]

Insolvency Legislation

The Law No. 326-IQ **On Insolvency and Bankruptcy** (the Insolvency Law), adopted on 13 June 1997 and last amended on 30 December 2020, is the main legislation governing insolvency in Azerbaijan. The Insolvency Law applies to all commercial organisations (except banks) and non-profit organisations, as well as to entrepreneurs.

The Resolution No. 416 on the approval of the "Content of the debtor's reorganisation plan" dated 26 September 2018 and the Decree of the President of the Republic Of Azerbaijan No. 604 "On application of the Law of the Republic of Azerbaijan on insolvency and bankruptcy" dated 23 June 1997 are other relevant secondary legislative acts.

Insolvency Data

There is no publicly-available register related to insolvency proceedings in Azerbaijan and no publicly-available court system recording the number or type of insolvency proceedings. However, any applicant, whether debtor or creditor, must publish an announcement of the insolvency hearing on the official website of the Ministry of Economy. The list of announcements is available **here**. Publication must also take place in an official periodical five working days before the date of the start of the insolvency hearing. Therefore, some data may be accessed on an unconsolidated basis.

The official periodical is usually the newspaper published by the State Tax Service **(www.vergiler.az)**, in which announcements may be searched by the name of a particular legal entity or the taxpayer registration number.

The Office of the Supreme Court of the Republic of Azerbaijan has confirmed that in 2019 there were 18 bankruptcy cases before the administrative-economic courts, which were distributed as follows:

Court	Cases
Baku Administrative Economic Court No. 1	8
Baku Administrative Economic Court No. 2	8
Shirvan Administrative Economic Court	1
Sumgayit Administrative Economic Court	1

Out of the 18 cases, five cases were considered on their merits and final court judgements were adopted, of which only one application for reorganisation was satisfied, while four applications were rejected. Furthermore, four applications for reorganisation were stayed without further consideration and nine applications were returned.

[1] **Population, GDP growth Rate, GDP per Capita, Inflation Rate and Unemployment rate, retrieve from "IMF – Source as of July 2021:** www.imf.org/en/Countries/AZE

[2] **PWC – Source as of July 2021:** www.taxsummaries.pwc.com/azerbaijan/corporate/taxes-on-corporate-income

Company Information

The company law framework in Azerbaijan is governed by the Civil Code of the Republic of Azerbaijan.[3] The company register is managed by the State Tax Service under the Ministry of Economy of the Republic of Azerbaijan and is freely available at no charge **here**. Companies may be searched either by their official name or their taxpayer registration number.

Insolvency Courts, Regulatory Authorities and Practitioners

Insolvency (bankruptcy) court cases are dealt with by commercial courts. The territorial jurisdiction of the court is established based on the debtor's legal seat of operations in respect of legal entities or place of residence in respect of entrepreneurs.

The Ministry of Economy publishes announcements of insolvency hearings of commercial and non-commercial organisations and the Cabinet of Ministers is the general rulemaking body in relation to any rules to be promulgated under the Insolvency Law.

The State Service for Property Issues under the Ministry of Economy (SSPM) is involved in any insolvency proceedings related to state-owned enterprises. For instance, the SSPM's decision must be provided when the debtor applies to the court. Where creditors initiate insolvency proceedings against a state-owned enterprise, they must send a copy of the insolvency petition to the SSPM. Finally, while appointing the insolvency practitioner (known as the bankruptcy administrator) to a state-owned debtor, the court shall take into account the opinion of the SSPM. The SSPM also has other functions as prescribed in the Insolvency Law.

The insolvency practitioner profession is not regulated in Azerbaijan and insolvency practitioners are not required to have a special authorisation to act (whether in the form of a licence or registration). There is no public register of practising insolvency practitioners.

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[3] The Azerbaijani version of the Civil Code of the Republic of Azerbaijan is available at **e-qanun.az/framework/46944**

Part B

Business Reorganisation

Are there any incentives for extrajudicial voluntary agreements (workouts)?

No, there are no particular incentives for workouts. However, insolvency (bankruptcy) proceedings without any court involvement may be initiated by the debtor (Chapter III) and these may end up with reorganisation (sanation). Additionally, if insolvency (bankruptcy) proceedings have been initiated, the debtor may together with the insolvency practitioner propose an amicable settlement with creditors at the first or at any subsequent meetings of creditors (Chapter VII).

What is the nature and purpose of the reorganisation procedure?

Under the Insolvency Law, there is one court-supervised reorganisation procedure: reorganisation (sanation) (sağlamlaşdırma). This can be conducted within court-supervised main insolvency (bankruptcy) proceedings (iflas prosesinə məhkəmə vasitəsilə başlanması) and within insolvency (bankruptcy) proceedings without court involvement (iflas prosesinə məhkəmənin iştiraki olmadan borclu müəssisə tərəfindən başlanması). However, in insolvency (bankruptcy) proceedings without court involvement the reorganisation plan must still be confirmed by the court (Article 41-1.3). **Click here** for an overview of the procedure.

The aim of the reorganisation (sanation) procedure is to restore the solvency of the debtor by means of financial assistance from the debtor's owner, creditors and other legal entities and individuals, and to prevent the debtor's liquidation (Article 40). However, the debtor and creditors may also conclude an amicable settlement agreement (barışıq sazişi) at the first creditors' meeting or any subsequent meeting within insolvency (bankruptcy) proceedings. This is also available in the out-of-court procedure.

The amicable settlement agreement needs to be approved by the court in order to become effective and may include measures such as sale or transfer of the whole or part of the debtor's property, including shares, establishment of a new legal entity as a result of the agreement, deferment of payment, and reorganisation of the capital structure of the debtor.

The Insolvency Law, as explained above, also allows for out-of-court insolvency (bankruptcy) proceedings. In this case, a creditors' meeting is convened, and an insolvency practitioner (known as an administrator) is appointed. The law does not, however, provide many details about the out-of-court procedure, which is mainly creditor-led.

Who can commence the process and what entry conditions apply?

Reorganisation (sanation) procedure

This procedure is only available within main insolvency (bankruptcy) proceedings. Such proceedings may be initiated by the debtor or its creditors. The court considers the application for bankruptcy within one month from the date of receipt and makes a decision to declare the debtor insolvent and commence the procedure or to refuse the application (Articles 10 (1) and 11).

The debtor is insolvent if it declares itself insolvent, or a court or the creditors determine that: the debtor has failed to fulfil certain obligations within two consecutive months from the date when they fell due; the debtor has not fully complied with tax obligations and other government payments for 10 consecutive months from the date of their accrual; or the debtor has not fulfilled its obligations with other creditors in accordance with the prescribed expiry dates of such contracts (Article 3).

After the initiation of the proceedings, the debtor and its creditors have the right to request the court to consider reorganisation as an option (Article 40). The request must include certain documentation including, among other matters, proof that the solvency of the debtor can be restored and information on the amount of the debtor's obligations (Article 41). The application may also include the reorganisation plan, where this has already been adopted by the creditors' meeting. Otherwise, the debtor has two months to prepare a reorganisation plan and propose it to creditors for the adoption (Article 41.1).

Settlement agreement

The debtor or the insolvency practitioner can propose a settlement with creditors which may contain the measures stated above. The settlement may be proposed within the court-supervised insolvency (bankruptcy) proceedings as well as during the out-of-court insolvency (bankruptcy) proceedings but would need to be approved by the court in both cases (Articles 35 and 37).

References to Articles are to Articles of the Insolvency Law, unless specified otherwise. For an explanation of technical terms, please see the **Glossary of the Main Assessment Report**

Is there any court involvement?

Yes, insolvency proceedings are supervised and administrated by the competent court but there is also an option for creditor-led out-of-court insolvency proceedings supported by insolvency practitioner. The court is nevertheless involved in any approval of a reorganisation (sanation) agreement concluded out of court. A settlement agreement needs to be approved by the court.

Are there any hybrid reorganisation procedures?

Yes, the out-of-court insolvency procedure may be considered as a hybrid procedure, since an agreement is reached without the court's involvement and is then submitted for judicial confirmation. Out-of-court proceedings may result in either an agreement on insolvent liquidation or reorganisation (sanation).

Does the debtor remain in possession of and continue to manage its business?

No, as from the date of the court decision on the beginning of any reorganisation (sanation) procedure, whether under the in-court or out-of-court procedure, management and shareholder bodies of the debtor are prohibited from using and disposing of property belonging to the debtor (Article 41-2). On appointment of the provisional insolvency practitioner (known as the administrator), the authority of the debtor's management terminates (Article 33).

Prior to this, on initiation of the bankruptcy proceedings (but before the debtor has been declared insolvent), the debtor may also not dispose of any of its assets without the permission of the court or the insolvency practitioner. However, if the insolvency practitioner has not been appointed, the debtor may continue to carry out certain activities without any specific permission that relate to the payment of wages and current expenses, and the disposal of perishable assets (Article 17 (2)).

Is there a need to appoint an insolvency practitioner?

Yes, a provisional insolvency practitioner (the administrator) is appointed for the management of the debtor at the outset of the main insolvency (bankruptcy) proceedings while the court considers the possibility of sanation. The appointment of a provisional insolvency practitioner of property is a temporary measure and has the following objectives: to provide that assets of the debtor are not alienated illegally before the insolvency of the debtor is announced; and to carry out preliminary financial analysis of the debtor's status (Article 32). The provisional insolvency practitioner has the same powers as the permanent insolvency practitioner (Article 33).

The term of the provisional insolvency practitioner terminates on appointment of the permanent insolvency practitioner. This occurs once the insolvency case has been examined by the court (Article 11). Chapter V of the Insolvency Law sets forth a number of procedural rules to be followed and requirements to be completed by the insolvency practitioner, such as: publication of the insolvency notice at least twice with at least seven days' break; affixing the "undergoing bankruptcy proceedings" mark on all documents in the debtor's name; periodic reporting to the court and creditors; authorisation to act on behalf of the debtor, enter into and terminate agreements etc.; and authorisation to sell the debtor's assets (up to five per cent of the debtor's total assets) without convocation of the creditors' meeting.

Is there any applicable stay or moratorium?

Yes, irrespective of the form of commencement of the insolvency (bankruptcy) proceedings, a moratorium on enforcement actions and disposal of assets takes effect from the declaration of the debtor insolvent (Article 18 (2)). No earlier protection is envisaged.

From the moment the debtor has been declared insolvent: all court proceedings and other actions aimed at collecting sums owed by the debtor are terminated; claims against the debtor may be presented only within the framework of insolvency (bankruptcy) proceedings under the Insolvency Law; and provided there is no contradiction to legislation, execution of court decisions concerning the debtor's property adopted earlier is suspended.

The initiation of the reorganisation (sanation) procedure results in a further moratorium in which: the founders (shareholders) and other governing bodies of the debtor are prohibited from using and disposing of any property of the debtor and commencing insolvency (bankruptcy) proceedings against the debtor and execution of court decisions by such persons is suspended. Withdrawal of moneys from the debtor's bank accounts by creditors is also prohibited, as well as any foreclosure on the debtor's property (Article 41-2 part 1).

However, if there are circumstances that may lead to the destruction of the collateral (mortgage) of secured creditors or if collateral (mortgage) is not included in the reorganisation plan, then on the basis of the debtor's or the creditor's application, the court may decide to lift relevant restrictions listed above.

Is there any protection for essential contracts and to prevent termination of contracts by third parties?

Yes, with respect to essential contracts only. There are no protections to prevent termination of contracts by third parties due to the debtor entering into insolvency (bankruptcy) proceedings, including reorganisation (sanation) proceedings, but the insolvency practitioner can take any necessary measures to ensure uninterrupted supplies under the following essential contracts: water, electric power, fuel and other services required for the economic activity of the debtor (Article 20.4).

Is new financing protected by law?

Yes, the insolvency practitioner has the right to carry out the existing economic activity of debtor, and for this purpose to conclude deals on behalf of the debtor, including contracts, agreements and compositions, as well as loan (credit) agreements or to continue implementation of concluded deals (Article 20).

All costs and expenditures of the bankruptcy process (including fees and expenses of the administrator and also claims resulting from liabilities accepted or continued by the insolvency practitioner after of the declaration of bankruptcy) are paid in the first place (Article 53).

Does the law recognise separate classes of creditors for voting purposes?

Reorganisation (sanation) procedure

Yes. The Insolvency Law foresees the following six classes of creditors' claims in decreasing order of priority: secured creditors secured by mortgage or other collateral; creditors for compensation claims related to harm caused to life or health as well as creditors for alimony claims; creditors for claims of severance pay and wages to persons working under an employment contract and on payments under an author's contract; creditors of payments to the state budget, an extra-budgetary state fund on compulsory state social insurance contributions, unemployment insurance contributions and budgets of municipalities as well as unsecured debts (including interest) of credit institutions; other unsecured creditors (including unsecured creditors under contracts for the provision of goods and services); and founders (shareholders) of the debtor which is a legal entity (Article 41-1).

Under the Insolvency Law, creditors are first organised into groups for intra-group voting purposes. These creditor groups (i.e., secured creditors (the first rank) and unsecured creditors (the second, third, fourth, and fifth ranks)) then vote at the creditors' meeting on the reorganisation plan through their representatives (Articles 41-1.4, 41-1.5, and 41-1.9). Different voting thresholds apply to groups of secured creditors and unsecured creditors (as described below). However the sixth rank (shareholders) do not vote on the plan, as voting of affiliated persons is not taken into account.

Settlement agreement

A creditors' meeting is convened for the approval of the settlement agreement (Article 36 (5) paragraph 2). The decisions made in the creditors' meeting do not require the creditors to be divided into classes. A general meeting decision can only be adopted if a majority by number of creditors participating or represented at the meeting vote in favour and such creditors represent a majority of the total amount of all unsecured debts of the debtor held by creditors participating or represented at the meeting.

What are the majorities required to approve a reorganisation plan?

Reorganisation (sanation) procedure

The reorganisation plan must be approved by each group of secured and unsecured creditors. Creditors representing more than two-thirds by value of all creditor claims in each group must attend the voting. Within each group of creditors, only creditors whose rights are affected because of the adoption of the reorganisation plan participate in the voting.

The reorganisation plan is adopted if the following vote favour of the plan: secured creditors representing more than two-thirds of the claims in each group; and unsecured creditors with more than 50 per cent of the amount of claims in each group.

In both cases, the claims of creditors which are affiliated persons are not taken into account for the purpose of voting. The definition of affiliated persons is very broad and includes management, directors, relatives as well as shareholders of the company/debtor (whether legal entities or individuals) holding (whether directly or indirectly) at least 10 per cent of the shares in the company/debtor.

Each group of creditors must participate in voting in the general meeting of creditors, which takes place through a representative after the voting in the internal groups. If a group of creditors consists of one creditor, this creditor must personally participate in the voting. The decision of the creditors' meeting is made by a simple majority of votes of the representatives of groups of creditors. One member of each group is considered as one vote. If the votes are equal, the vote of the chairman of the meeting is considered decisive. The chairman is elected by the meeting of creditors (Article 41-1.9). After a positive vote, the debtor must submit the reorganisation plan for approval to the court within three days following its adoption by the creditors.

Settlement agreement

The settlement agreement must be approved at a meeting of creditors. A meeting of creditors is considered quorate provided that creditors, whose claims altogether represent not less than 50 per cent of total amount of creditors' claims, attend the meeting. (Article 48 (3)).

Decisions made at the meeting of creditors are valid when supported by: a simple majority of creditors attending the meeting, i.e. over 50 per cent by number; and a majority of creditors by value of claims in relation to unsecured claims.

Thus the settlement agreement needs to achieve the aforementioned majority of number of creditors and majority by value of unsecured claims. However, if one or more creditors attending the meeting vote in favour of taking certain measures with respect to the insolvency assets of the debtor, their decision is binding irrespective of whether the resolution was supported by the majority of creditors, provided that the consenting creditors hold at least 75 per cent of the total amount of claims.

Secured creditors secured by mortgage or other collateral, creditors for compensation claims related to harm caused to life or health as well as creditors for alimony claims; and creditors for claims of severance pay and wages to persons working under an employment contract and on payments under an author's contract, i.e. creditors of the first three ranks, must all expressly consent to the settlement agreement in order to be bound by its terms and cannot be subject to cram down (Article 38). A secured creditor has the right to vote at the meeting of creditors if it waives its security interest (Article 49). Furthermore, creditors which have voted against the proposed agreement, and which did not participate in the creditors' meeting, should be provided with equal rights to those who supported the settlement.

Who does the reorganisation plan bind?

Reorganisation (sanation) procedure

Subject to achieving the requisite majorities described above and court approval, the plan binds all secured and unsecured creditors, including any dissenting creditors within these groups (Article 41-2, paragraphs 6, 7, 10 and 11).

Settlement agreement

Subject to achieving the requisite quorum and majorities described above, and court approval, the agreement binds all unsecured creditors which received notification about the creditors' meeting, irrespective of whether they were present at the meeting and whether they approved the agreement (Article 37 (6)). Secured creditors secured by mortgage or other collateral, creditors for compensation claims related to harm caused to life or health as well as creditors for alimony claims; and creditors for claims of severance pay and wages to persons working under an employment contract and on payments under an author's contract i.e. creditors of the first three ranks, must all expressly consent to the settlement agreement in order to be bound by its terms.

What is the timeframe for the reorganisation procedure and any moratorium?

Reorganisation procedure

A reorganisation procedure shall not exceed 24 months (Article 41 (6) a)). The debtor must draw up a reorganisation plan within two months from the date of the decision on reorganisation between the debtor and the creditors.

The moratorium arises on the opening of the procedure and is in force for the duration of the procedure (Article 41-2).

Settlement agreement

There is no specific timeframe for reaching a settlement agreement. This option is available throughout the entire insolvency (bankruptcy) proceedings. As this is an option rather than a procedure, there is no associated moratorium.

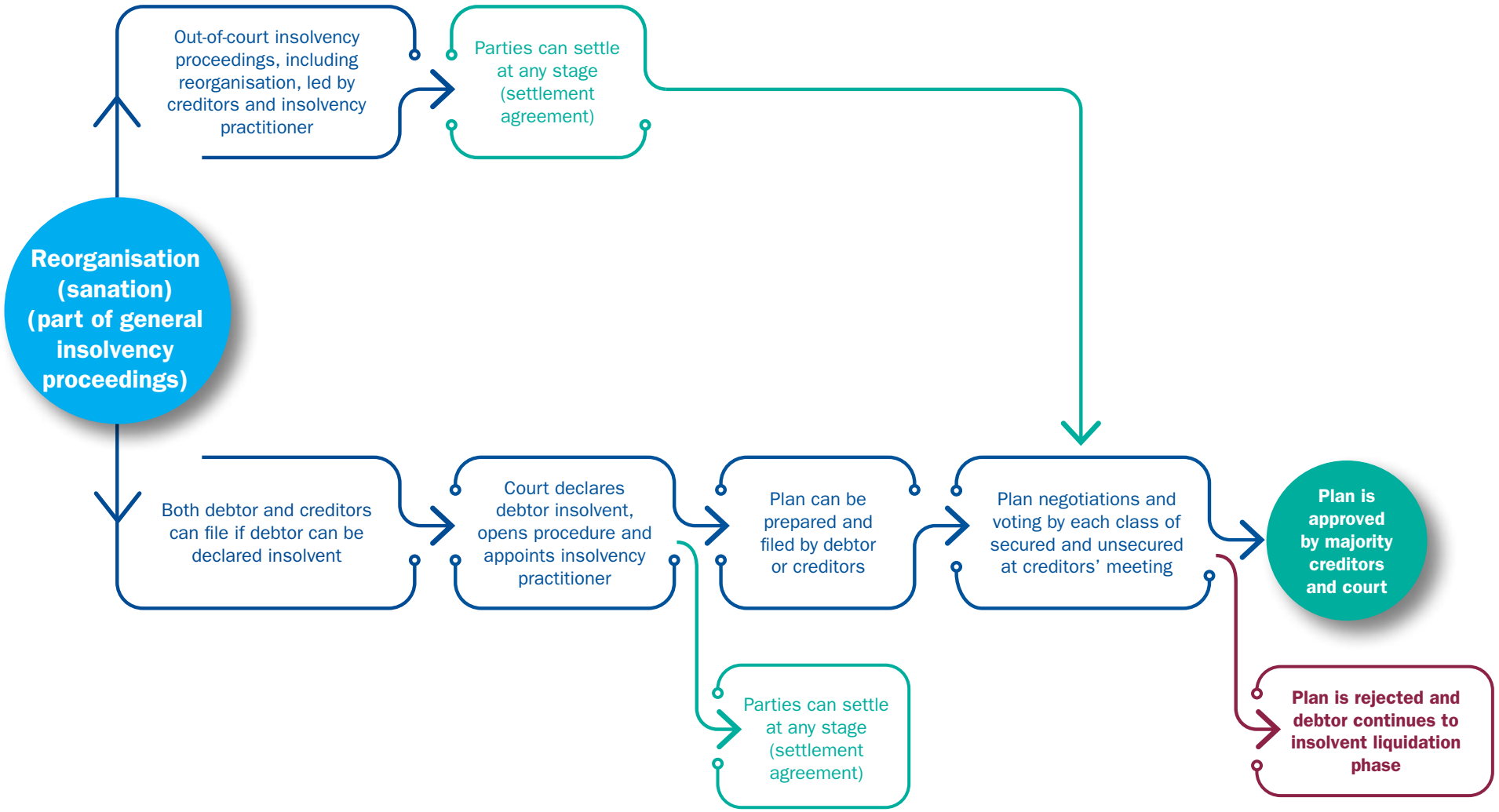
Has the UNCITRAL Model Law on Cross Border Insolvency been adopted?

No, the UNCITRAL Model Law has not been adopted and there are no cross border insolvency provisions in the Insolvency Law. In general, decisions of foreign courts can be recognised and enforced in Azerbaijan based only on relevant treaties ratified by Azerbaijan, or if the law so provides or based on the principle of reciprocity. In practice, the reciprocity principle is not widely practised in Azerbaijan. Azerbaijan does not have treaties on execution of court decisions with the United Kingdom or European Union member states.

Special features/observations:

- The Azerbaijani Insolvency Law contains provisions on regulation of out-of-court insolvency proceedings in which creditors should appoint an insolvency practitioner (administrator) at the first creditors' meeting to lead the process. The proceedings may be of either a reorganisation or liquidation nature.

Overview of Azerbaijani Business Reorganisation Procedures*



* This provides a high-level overview of business reorganisation procedures. See the commentary in this profile and the Insolvency Law for further details, including with respect to any applicable moratoria and creditor voting thresholds.

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