

Client Alert

National Bank of Ukraine Introduces New Regulation on Foreign Currency Loans from Non-Residents and Establishes New Maximum Interest Rates

Foreign lenders financing Ukrainian entities will now need to take into account two recent enactments from the National Bank of Ukraine ("NBU") that may impact their transactions, and, in particular, the applicable interest rates. The first of these, the "Regulation on the Procedure for Residents to Obtain Credits, Loans in Foreign Currency from Non-Residents and the Extending of Foreign Currency Loans by Residents to Non-Residents," approved by NBU Resolution No. 270 on June 17, 2004 ("Resolution 270"), came into effect on August 16, 2004, and the second, NBU Resolution No. 363 "On Establishing Interest Rates for Foreign Borrowings of Residents," dated August 3, 2004 ("Resolution 363"), comes into effect on September 3, 2004.

Resolution 270, which replaces the previous regulations on the registration of foreign currency loans contained in NBU Resolution No. 602, dated December 22, 1999 ("Resolution 602"), leaves, in great measure, the prior rules concerning such loans intact and consolidates into one regulation concepts relevant to such loans that were contained in other letters and instructions issued by the NBU. In addition, Resolution 270 introduces a procedure for licensing Ukrainian lenders seeking to provide foreign currency loans to foreign borrowers. Most noteworthy, however, is that Resolution 270 introduces certain new concepts concerning the interest rate and other fees and charges that may be assessed by a foreign lender in connection with foreign currency loans, while Resolution 363 establishes new maximum interest rates that may be charged. In this client alert, we focus on the provisions concerning interest rates.

Maximum Interest Rate

At the outset, we note that the requirement of a Ukrainian borrower to register a loan in foreign currency from a foreign lender applies to all such loans, with the exception of loans guaranteed by the Cabinet of Ministers of Ukraine and trade credits (such as those extended by a seller of goods). Similar to the prior NBU regulations contained in Resolution 602, Resolution 270 provides that the NBU will not register a loan agreement if the interest rate exceeds the respective maximum interest rate for foreign currency loans established by the NBU. For loans in most freely convertible (hard) currencies (e.g., U.S. Dollars, Euros) the NBU will establish the maximum interest rate based on the cost of Ukraine's own sovereign borrowings on foreign financial markets. In establishing the interest rate, the NBU will consider the profitability of Ukrainian bonds issued by the Ministry of Finance (presumably Ukraine's Eurobonds), taking into account the median spread for sovereign (government) borrowings and private borrowings on international financial markets, as well as the ratings of Ukrainian companies by international rating agencies. As for loans in most currencies with limited convertibility (i.e., soft currencies), the maximum interest rate will be tied to the

weighted average interest rate at which Ukrainian banks normally extend their loans on the Ukrainian loan market.

In furtherance of the foregoing, the NBU issued Resolution 363 which sets out the maximum interest rates for both hard and soft currency loans. Previously, the applicable rates for such loans were, respectively, 11% and 19%. As of September 3, 2004, the maximum interest rate for soft currency loans will be 20% per annum. As for hard currency loans, the following maximum interest rates will apply:

- (i) for fixed rate loans:
 - with a maturity of up to 1 year - 9.8% per annum;
 - with a maturity from 1 to 3 years - 10% per annum; and
 - with a maturity over 3 years - 11%;
- (ii) for floating rate loans: 3-month USD LIBOR plus 750 basis points.

Although Resolution 270 does not contain any express exceptions to the maximum interest rate, it provides that the NBU may, on a case-by-case basis, permit a Ukrainian borrower to deviate from the maximum interest rates if the borrower is financing a project that is strategically important for the Ukrainian economy.

The new maximum interest rates will not (except as noted below) affect the interest rates on loans registered prior to the effective date of the Resolution 363 (i.e., September 3, 2004). As a general matter, the interest rate specified in a loan registration certificate will continue to apply to the loan throughout the entire term, regardless of whether the NBU subsequently increases or decreases the maximum interest rate. If, however, the registration certificate needs to be amended as a result of an increase in the principal amount of the loan or an extension of the validity of the certificate (e.g., in connection with an extension of the final repayment date), the NBU will not register the amendment if the interest rate under the agreement exceeds the maximum interest rate in effect at the time of the amendment. In such cases, the lender will be required to charge the lower interest rate to any increased principal or for any extension of the loan term.

Expansion of Applicability of Maximum Interest Rate

As noted above, the NBU will not register a loan in foreign currency if the interest rate exceeds the maximum interest rates described above. Resolution 270 has, however, expanded the applicability of the maximum interest rate concept beyond the nominal interest rate charged by a lender for the loan, as was previously contemplated by Resolution 602. Under the new regulation, the NBU will now review whether the interest rate for the "use of the loan" does not exceed the maximum interest rate, with the former including not only the nominal interest rate applicable to the loan, but also all commissions, penalties (e.g., default interest) and other charges stipulated in the loan agreement.

The NBU has not, however, explained what the term "other charges" includes or how it will apply this new requirement to calculate whether the interest rate for the "use of the loan" exceeds the NBU's maximum interest rate. It appears from the language of Resolution 270 that the term "other charges" may be interpreted to mean a variety of fees and charges that are customary for loans by Western lenders, such as commitment fees, arrangement fees, and the like. Given that the manner in which the NBU will determine whether the interest rate, commissions and other charges exceed the maximum interest rate is not yet clear, foreign lenders may need to consider the possibility that

certain payments contemplated by their agreements might not be permissible and/or that the NBU may simply refuse to register the loan agreement if it determines that the aggregate of the interest rate, commissions, penalties and other charges exceeds the maximum interest rates.

For example, certain customary charges and fees in loan agreements do not continually accrue throughout the term of the loan, but instead are one-time or contingent charges. If the NBU were to simply aggregate all such contemplated charges at the outset, rather than consider the nature of the charges, given current market practices in Ukraine for foreign currency loans the interest rate for the "use of the loan" for most loan agreements would likely be deemed in excess of the maximum interest rate. We anticipate that the NBU will reconsider the language of Resolution 270 and provide further clarification as to the application of the maximum interest rate to the interest rate for the "use of the loan."

We note further that Resolution 270 now provides that the NBU will not register loan agreements that provide for the payment of interest for the "use of the loan" before the loan proceeds are actually disbursed. Presumably, given the broad extension of the concept of interest to payments such as commissions and other charges, in drafting loan agreements foreign lenders may need to time the payments of any up-front commissions or other charges by a Ukrainian borrower to immediately follow (rather than precede) the first disbursement under the loan.

* * * * *

September 1, 2004

For Additional Information

This client alert can be found, together with other recent Chadbourne & Parke LLP client alerts, on our website at www.chadbourne.com/publications/sub_Publications.html. Our client alerts are for general informational purposes and should not be regarded as legal advice. If you have any questions regarding this alert, please contact any of the following:

Kyiv

Adam M. Mycyk	+380 (44) 230-2534	amycyk@chadbourne.com
Anna Y. Ryzhova	+380 (44) 230-2534	aryzhova@chadbourne.com

London

Lynne E. Gedanken	+44 (020) 7337-8022	lgedanken@chadbourne.com
Nabil L. Khodadad	+44 (020) 7337-8036	nkhodadad@chadbourne.com
Rubin Weston	+44 (020) 7337-8031	rweston@chadbourne.com

Chadbourne & Parke LLP

New York

30 Rockefeller Plaza
New York, New York 10112
Telephone: +1 (212) 408-5100
Facsimile: +1 (212) 541-5369

Washington, D.C.

1200 New Hampshire Avenue, N.W.
Washington, D.C. 20036
Telephone: +1 (202) 974-5600
Facsimile: +1 (202) 974-5602

Los Angeles

350 South Grand Avenue, Suite 3300
Los Angeles, CA 90071
Telephone: +1 (213) 892-1000
Facsimile: +1 (213) 622-9865

Houston

1100 Louisiana, Suite 3500
Houston, TX 77002
Telephone: +1 (713) 571-5900
Facsimile: +1 (713) 571-5970

London

Chadbourne & Parke
(a multinational partnership)
Regis House
45 King William Street
London EC4R 9AN
Telephone: +44 (0)20 7337-8000
Facsimile: +44 (0)20 7337-8001

Moscow

52/5 Kosmodamianskaya Naberezhnaya
Moscow 115054, Russian Federation
Telephone: +7 (095) 974-2424
Facsimile: +7 (095) 974-2425

Warsaw

(through a Polish partnership)
ul. Emilii Plater 53
00-113 Warsaw, Poland
Telephone: +48 (22) 520-5000
Facsimile: +48 (22) 520-5001

Kyiv

11 Mykhailivska Street, 4th Floor
Kyiv 01001, Ukraine
Telephone: +380 (44) 230-2534
Facsimile: +380 (44) 230-2535

Beijing

Beijing Kerry Centre
1 Guang Hua Road
Chao Yang District
Beijing 100020, China
Telephone: +86 (10) 8529-8892
Facsimile: +86 (10) 8529-8866

If you would like additional copies of this client alert, please contact Phillipa Yule, Director of Marketing and Creative Services, at +1 (212) 408-5240 or e-mail: pyule@chadbourne.com.