5. Internationales Symposium Restrukturierung

Jahreskonferenz 2016





Restructuring Reform with Pre-Insolvency Proceedings – Where is the European Union heading to?

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EU Insolvency Law: where do we stand? (i)

- Early period till 2002: ad hoc, e.g.
 - Dir. 77/187 Safeguarding Employees' Rights in case of Transfer of Undertakings
 - Dir. 90/314 re Insolvency of Tour Operator
- 2002 EU Insolvency Regulation 1346/2000 Conflict of law system in x-border insolvency matters:
 - The requirement of fulfilling international jurisdiction ('COMI', 'establishment')
 - The principle of applying the *lex concursus* of the MS in which insolvency proceedings have been opened, to the rest of the EU (except Denmark)
 - The principle of automatic recognition of certain insolvency (related) judgments in other EU MSs, and
 - The duty for cross-border cooperation between insolvency office holders ('liquidators') when two or more insolvency proceedings in MSs are pending
- June 2017 EIR Recast

http://bobwessels.nl/2015/09/2015-09-doc14-short-note-on-eir-recast/

EU Insolvency Law: where do we stand? (ii)

- EIR Basis in Art. 81 TFEU (promoting judicial cooperation)
 - Hardly contains 'harmonisation'

Recital 11:

'(11) This Regulation acknowledges the fact that as a result of widely differing substantive laws it is not practical to introduce insolvency proceedings with universal scope in the entire Community. The application without exception of the law of the State of opening of proceedings would, against this background, frequently lead to difficulties. This applies, for example, to the widely differing laws on security interests to be found in the Community. Furthermore, the preferential rights enjoyed by some creditors in the insolvency proceedings are, in some cases, completely different ...'

EU Insolvency Law: where do we stand? (iii)

Guide to Enactment and Interpretation UNCITRAL Model Law on Cross-Border Insolvency (2013, nr. 5):

All national insolvency systems having so many differences, these '... hamper the rescue of financially troubled businesses, are not conducive to a fair and efficient administration of cross-border insolvencies, impede the protection of the assets of the insolvent debtor against dissipation and hinder maximization of the value of those assets. Moreover, the absence of predictability in the handling of cross-border insolvency cases impedes capital flow and is a disincentive to cross-border investment ...'

EU Insolvency Law: where do we stand? (iv)

- Since 2011 in EU: Third phase: harmonisation
- Late 2011 EP asked EC for legislative proposals
 - "... relating to an EU corporate insolvency framework, following the detailed recommendations set out in the Annex hereto, in order to ensure a level playing field, based on a profound analysis of all viable alternatives."
- 12 December 2012 (next to proposal for Recast EIR) EC policy 'A new approach to business failure and insolvency' aiming to harmonise certain matters of insolvency and company laws
- July 2013 Consultation
- March 2014 EC's Recommendation
- September 2015 Interim assessment: disappointing results
- 2016 Group of experts on restructuring and insolvency law http://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupDetail&groupID=3362
- 26 October 2016 EU 'Instrument' announced

Legislative Landscape in EU 2012

In a 2012 study Univ. of Heidelberg prof. Andreas Pieckenbrock compared insolvency laws of England, Italy, France, Belgium, Germany and Austria, concluding that there are several common tendencies in the approach to rescue:

- **1.Early recourse** Sometimes there is an earlier moment of starting a rescue process, for instance in the French *Sauvegarde*: the debtor must encounter problems that he can not solve, which is earlier than the traditional moment that the debtor can not pay its financial obligations when they are due
- **2.Debtor in possession** The board is not fully replaced by the insolvency administrator; in certain proceedings the board stays in control of the business
- **3.Stay** In these countries one finds a moratorium or a stay either automatic like in the Sauvegarde or at request (for instance the concordato preventivo or réorganisation judiciare)
- **4.Protecting fresh money** There are special provisions to protect fresh money available for the company while trying to work itself out of its misery
- **5.Debt for equity swap** Possibilities of a debt for equity swap, i.e. the conversion of a creditors claim into shares in the capital of the company
- **6.Reorg. plans** with mechanism to bind disapproving creditors ('cram-down')

Main Objects of EC's Recommendation (i)

Two main objects of EC's Recommendation of 12 March 2014:

1.To '... ensure that viable enterprises in financial difficulties, wherever they are located in the Union, have access to national insolvency frameworks which enable them to restructure at an early stage with a view to preventing their insolvency, and therefore maximise the total value to creditors, employees, owners and the economy as a whole. The Recommendation also aims at giving honest bankrupt entrepreneurs a second chance across the Union.' (recital (1))

Main Objects of EC's Recommendation (ii)

- 2. In order to achieve these aims, the Commission deemed it necessary to:
 - encourage greater coherence between the national insolvency frameworks in order to reduce divergences and inefficiencies which hamper the early restructuring of viable companies in financial difficulties and the possibility of a second chance for honest entrepreneurs, and thereby lower the cost of restructuring for both debtors and creditors. Greater coherence and increased efficiency in those national insolvency rules would maximise the returns to all types of creditors and investors and encourage cross-border investment. Greater coherence would also facilitate the restructuring of groups of companies irrespective of where the members of the group are located in the Union.' (recital (11))

Creation of a Capital Markets Union (CMU)

In 2015 the Commission launched a plan for the establishment of a *Capital Markets Union (CMU)*. The Commission proposes a legislative initiative on business insolvency, including early restructuring and second chance, drawing on the experience of the Recommendation:

'The initiative will seek to address the most important barriers to the free flow of capital, building on national regimes that work well'.

This means that '(insolvency) laws' should be drafted in a way that it would be much more easy for investors to assess credit risk, particularly in cross-border investments.

Insolvency is put between brackets, as in certain MSs assessing credit risk relates to the creation and enforcement of security rights, including the transparency of systems of registration of assets.

Heart of the Recommendation's System

- 'Minimum standards' for 'preventive restructuring frameworks'
- Six Core Principles:
 - 1. Early recourse to framework for debtor in 'likelihood of insolvency'
 - 2. Minimised court involvement
 - 3. Debtor in possession
 - 4. Court-ordered stay
 - 5. Ability to bind dissenting creditors to a restructuring plan
 - 6. Protection for new finance

Rescue of Business in Insolvency Law



The European Law Institute (ELI) is an independent non-profit organisation established to initiate, conduct and facilitate research, make recommendations and provide practical guidance in the field of European legal development. Building on the wealth of diverse legal traditions, its mission is the quest for better law-making in Europe and the enhancement of European legal integration. By its endeavours, ELI seeks to contribute to the formation of a more vigorous European legal community, integrating the achievements of the various legal cultures, endorsing the value of comparative knowledge, and taking a genuinely pan-European perspective. As such its work covers all branches of the law: substantive and procedural; private and public.

ELI Project

Business Rescue in Insolvency Law

- Q1/2014 Q3/2017
- Aim: to design a set of norms and requirements that will enable the further development of coherent and functional rules for business rescue in the EU ('ELI Legislative Guide')



ELI Project Organisation

- 2 Reporters
- 25 National Correspondents (NCs)
- Advisory Committee of 10 (AC)
- Members Consultative Committee (MCC), some 30

Chair: prof. Tatjana Josipović (Uni of Zagreb)

ELI Members are still welcome to register for the MCC

Register via: <u>businessrescue@europeanlawinstitute.eu</u>

Headings Questionnaire (for NCs)

- 1. Governance and Supervision of a rescue in court and out-of-court
 - Conditions for out-of-court workouts, conditions for opening of such 'proceedings', conditions for opening formal pre-insolvency and insolvency proceedings
 - Role of a court, a supervisory judge or other state agency
 - Status, powers and supervision of insolvency practitioners; duties and liabilities of directors
 - How are unsuccessful rescue attempts in pre-/insolvency procedures terminated or converted into other procedures?
- 2. Financing a rescue, including critical vendors and other pressures on liquidity; the stay
- **3. Executory contracts**, including leases, IP-licensing contracts; termination and modification of contracts; transfer of contracts
- 4. Ranking of creditor claims; governance role of creditors
- **5.** Labour, benefit and pension issues
- **6. Avoidance powers**, including safe harbour for failed rescue efforts in a later bankruptcy, and avoidance powers in pre-insolvency procedures and out-of-court workouts
- 7. Sales of substantially all of the debtor's assets on a going-concern basis
- 8. Rescue plan issues: procedure and structure; distributional issues
- 9. Multiple enterprise/corporate group issues
- **10. Special arrangements for small and medium-sized enterprises** (SMEs) including natural persons (but not consumers)

Comparing ELI Project and Recommendation (i)

From the Questionnaire the following topics do not seem to be addressed in the Recommendation:

- 3 ('Executory contracts, including leases, IP-licensing contracts; termination and modification of contracts; transfer of contracts')
- 5 ('Labour, benefit and pension issues'),
- 6 ('Avoidance powers, including safe harbour for failed rescue efforts in a later bankruptcy, and avoidance powers in pre-insolvency procedures and out-of-court workouts'),
- 7 ('Sales of substantially all of the debtor's assets on a going-concern basis'),
- 9 ('Multiple enterprise/corporate group issues', although there are some references to groups in the recitals of the Recommendation), and
- 10 ('Special arrangements for small and medium-sized enterprises (SMEs) including natural persons (but not consumers)')

Comparing ELI Project and Recommendation (ii)

From the Questionnaire indeed partly are addressed:

- topic 1 ('Governance and Supervision of a rescue in court and out-of-court')
- 2 ('Financing a rescue, including critical vendors and other pressures on liquidity; the stay')
- 4 ('Ranking of creditor claims; governance role of creditors') and
- 8 ('Rescue plan issues: procedure and structure; distributional issues')
- Recommendation also covers consumer bankruptcies, a topic that falls outside the scope of the ELI study

International benchmarking

- International Inventory report
 (comparing soft law solutions, such as World Bank 2011 Principles for Effective Insolvency and Creditor/Debtor Regimes and UNCITRAL Legislative Guide)
- Reports of EC re Recommendation's 'implementation' (Sept. 2015)
- Certain EU MS's country analysis' + literature
- ABI's report on reform of US Chapter 11 Bankruptcy Act (published in December 2014)
 - See Final Report and Recommendations (241!)

https://abiworld.app.box.com/s/vvircv5xv83aavl4dp4h

Project Outcomes

- Inventory report on national insolvency laws, in particular rescuerelated tools, including empirical evidence and the underlying policy choices from 13 selected MSs
- 2. Inventory report on international recommendations from standardsetting organisations re 10 topics of Questionnaire
- 3. Legislative aide/guide, possibly model rules, based on transparent and reasoned policy choices and comprising a catalogue of identified good & best practice models which support and facilitate the rescue of business while striking a fair balance with creditors' interests and other recognized interests
- 4. (if justified) Legislative proposal (probably: Directive) addressed to the EU legislator, aiming at targeted harmonization of national insolvency laws in order to create a level playing field of balanced rescue solutions in Europe

General recommendations

Example

2. A Member States' restructuring and insolvency legislative framework should be based on an explicit policy that strongly favours the speedy, inexpensive, negotiated adjustment of a company's debts afforded by out-of-court procedures.

General recommendations (cont'd)

• 3 Member States should recognise that the success of any restructuring or insolvency system is very largely dependent upon those who administer it. That system can only function well when all stakeholders, including the general public, have confidence and respect in the courts and the way the roles of all parties involved are guaranteed and executed.

Actors in restructuring and insolvency proceedings

- court
- mediator
- supervisor
- independent intermediary
- expert
- insolvency practitioner
- debtor in possession
- turnaround manager
- corporate restructuring officer (CRO)

Need for solid insolvency systems

In each individual case the organisational structure should be assured, meaning

'... a country's insolvency governance system in an individual case (the allocation of functions between courts and IPs, including the legal and operational relationships between them, based on law and additional regulations) as well as a country's institutional system, merely related to the requirements to fulfil these actors' functions, including professional and ethical rules that apply to them.'

(2012 Report 'Harmonisation of Insolvency Law in EU' by Fletcher/Wessels)

Court



Court

A court / a judge has to fulfil a set of five criteria:

- 1. a general understanding of business management (so as not to assume managerial tasks),
- 2. understanding what it needs to effectively enforce the rights of both secured and unsecured creditors outside of insolvency proceedings,
- 3. preferably, be a specialists in commercial matters,
- 4. be impartial and independent, and
- 5. were practical, have specialized insolvency expertise.

Court

'Mutual trust' / 'sincere cooperation' between MSs assumes that European courts, dealing with civil law and commercial law matters, requirements (ii) (understanding what it needs to effectively enforce the rights of both secured and unsecured creditors outside of insolvency proceedings) and (iv) (be impartial and independent) are met

Query: what about the other three??

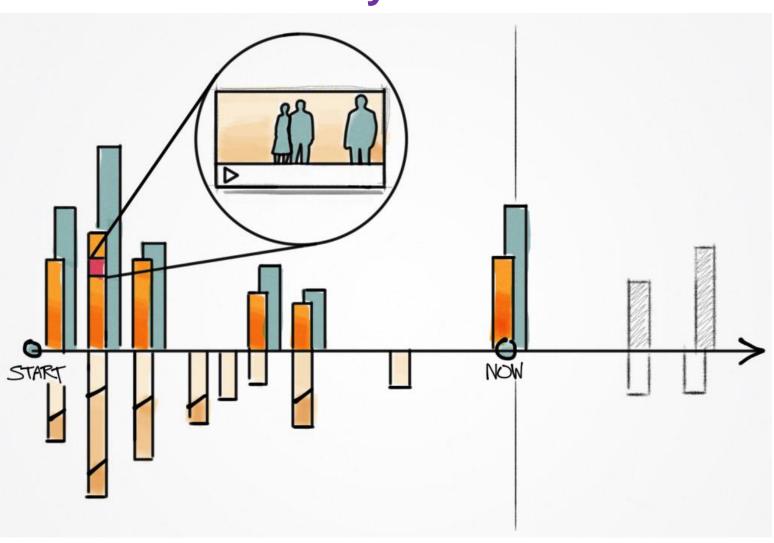
- (i) a general understanding of business management,
- (iii) preferably, be a specialists in commercial matters, and
- (v) were practical, have specialized insolvency expertise

June 2016 - Nordic-Baltic Insolvency Network Recommendation XI ('Administration of insolvency proceedings'), 13 and 14:

'The court's qualifications and role in the management'

- 13. Insolvency proceedings, as well as other cases and matters with strong insolvency law implications, should be handled by insolvency courts, commercial courts with special qualifications in the area of insolvency law, or by a division of a court or certain judges who are specialised in or equipped with special qualifications in insolvency law
- 14. If the qualification requirements in the previous section's conditions cannot be met, the insolvency law should not give the court a central or an active role in the management of liquidation or reorganisation proceedings. In particular, the court in that event should not make decisions regarding business matters.'

The way ahead?



Thoughts

- 1. greater efforts in training of national and other EU judges
- 2. develop Professional Insolvency Standard by the judges themselves (NL example)
- 3. give a pre-vision on an uncertain matter (London Financial List)
- 4. introduce court specialization (Loi Macron, France)
- 5. a system of challenge based on the argument that the judge is not (sufficiently) competent to act in a certain case?
- 6. outsourcing to mediator / supervisor
- 7. create specific EU debt restructuring court(s) ??

Recommendations regarding Courts and its Judges (Cont'd)

- 6 In achieving the objective of Recommendation 5 Member States and courts should recognise that the performance of restructuring and insolvency tasks by courts and its judges requires the continuous strengthening of judicial independence, and the appearance of such independence.
- 7 In achieving the objective of Recommendation 5 the European Commission, Member State and courts should actively develop methods to effectively improve judges' performances by either (i) concentration of courts with jurisdiction to decide in matters of restructuring and insolvency, (ii) selecting certain matters in which court can be addressed to provide their view in certain matters of market uncertainties, (iii) developing specific education beyond the boundaries of general legal competence, (iv) developing and applying professional insolvency standards to assess performance, or by a combination of these.
- 8 Given their inherent complexities and specific procedural requirements in cross-border cases, either within the EU or in relation to third states, Member States should consider allocating jurisdiction to one or a selected number of courts in its jurisdiction.

Practitioners



IOH - IP



World bank 2011 Principle D8 ('Competence and Integrity of Insolvency Representative')

'The system should ensure that:

- Criteria as to who may be an insolvency representative should be objective, clearly established and publicly available;
- Insolvency representatives be competent to undertake the work to which they are appointed and to exercise the powers given to them;
- Insolvency representatives act with integrity, impartiality and independence; and
- Insolvency representatives, where acting as managers, be held to director and officer standards of accountability, and be subject to removal for incompetence, negligence, fraud or other wrongful conduct'

Quilt



IPs – A European quilt

Who may be appointed to act as an insolvency practitioner?

How are they appointed?

What powers do they have in each relevant procedure?

What duties do they owe, and to whom? What sanctions apply for breach of duty, and do they include any risk of personal liability?

What reporting obligations do they come under?

How are they remunerated?

• For instance: is the remuneration based on an hourly rate, a fixed rate, a percentage of realisations from the debtor's estate or a combination of the foregoing? Is this a general rate or can it be adjusted based on, for example, the experience of the insolvency practitioner and the complexity of the case? Is remuneration affected by the outcome of the procedure (for example, through payment of a 'bonus' for maximisation of recoveries or rescue of the debtor's business)? Does a tariff system exist limiting the maximum amount of remuneration that can be charged by an insolvency practitioner?



EBRD IOH Principles 2007

- Principle 1: qualification and licensing
- Principle 2: appointment in an insolvency case
- Principle 3: review of an office holder appointment
- Principle 4: removal, resignation and death of an office holder
- Principle 5: replacement of an office holder
- Principle 6: standards of professional and commercial conduct
- Principle 7: reporting and supervision
- Principle 8: regulatory and disciplinary functions
- Principle 9: remunerations and expenses
- Principle 10: release of office holder
- Principle 11: insurance and bonding
- Principle 12: code of ethics.

Nordic-Baltic Qualification requirements for liquidation trustees and reorganisation administrators

General requirements

- '4. The same requirement for insight, experience and suitability for handling the proceedings in question should apply to a liquidation trustee as to a reorganisation administrator. In most jurisdictions this would normally be a lawyer, but the network does not consider whether requirements for certain formal qualifications, a specific title, certification or license should be made in addition to the general suitability requirement.
- 5. The same requirement for independence and impartiality in relation to both the debtor and the creditors should apply for both categories. The trustee or administrator should be obligated to declare if there exists any threats to independence or any conflict of interest.'

Same requirements trustees/administrators

- insight, experience and suitability (XI:4)
- independence and impartiality in relation to both the debtor and the creditors (XI:5)
- appointment by the court (XI:7)
- regime for dismissal (XI:9)
- liability rules (XI:12)
- 'The trustee and administrator's liability for damages
- 12. A trustee and an administrator should have a duty to compensate for damage that he or she intentionally or negligently caused with regard to either the estate, a creditor or the debtor whilst performing his or her duties.

According to the first paragraph there should also be liability against third parties provided the trustee or the administrator has disregarded a written or unwritten insolvency law rule laid down for the protection of third parties.

EBRD 2014

On all aspects of the insolvency practitioners professions' deontology there are some similarities, but many times there are differences and diversities in a large proportion of its details.

These aspects concern what EBRD in its 2014 report has called '... seven core elements (benchmarks) for the development and performance of the IOH profession', these being (i) licensing and registration, (ii) regulation, supervision and discipline, (iii) qualification and training, (iv) appointment system, (v) work standards and ethics, (vi) legal powers and duties, and (vii) remuneration

The way ahead?



Recommendations on IPs

• 17 In achieving the objective of Recommendation 1 the European Commission or Member States should recognise that the performance of restructuring and insolvency tasks requires the recognition of an independent position of professionals in restructuring en insolvency in its laws, laying down clear and transparent rules for performing their tasks. Being regulated as a lawyer or an accountant is in itself not sufficient that the standards of performance necessary for a fit and proper exercise of the restructuring and insolvency tasks required for a job are met

Recommendations on IPs (Cont'd)

18 In support of recommendation 3 and in line with Recommendation 4 the European Commission or Member States should set professional and ethical standards for insolvency practitioners and should ensure that the relevant professional bodies are consulted and involved in the creation of such standards and that they take into account best practices for appropriately regulated professional parties as set out in principles and guidelines on regulation of the restructuring and insolvency profession developed or adopted by European and international non-governmental organisations active in the area of restructuring and insolvency. In any event these standards should relate to licensing and registration, regulation, supervision and discipline, qualification and training, appointment system, work standards during administration, legal powers and duties, remuneration, reporting and communication and ethical working standards (including rules on conflict of interests and a complaint procedure).

EU Instrument in the oven

Brussels, 14.9.2016 COM(2016) 601 final

Communication of EC re **Capital Markets Union** - Accelerating Reform 2) Accelerating delivery of the next phase of CMU actions

The Commission will present shortly a proposal on business restructuring and second chance, key elements of an appropriate insolvency framework. Allowing honest entrepreneurs to benefit from a second chance after overcoming bankruptcy is crucial for ensuring a dynamic business environment and promoting innovation.

The Commission is also conducting a benchmarking review of loan enforcement (including insolvency) regimes to establish a detailed and reliable picture of the outcomes that banks experience when faced with defaulting loans in terms of delays, costs and value-recovery. The review will assist Member States seeking to increase the efficiency and transparency of their regimes.