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Welcome address

Tomáš Richter

Session One:
Topics in Corporate Preventive Restructuring

Chair: Jennifer Gant

INSOL EUROPE 40 YEARS 1981-2021

The Emerging New Landscape of European Restructuring and Insolvency

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Implementation of the 2019/1023 Directive in French Pre-insolvency and Insolvency Law: The Debtor-Creditor Juggle

Sarah Pople

1

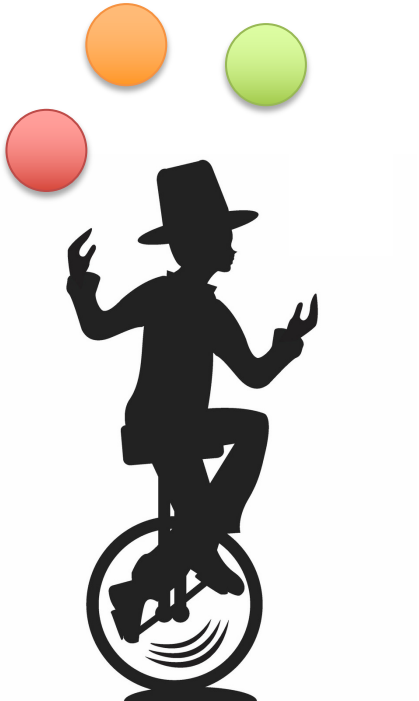
Safeguarding new creditor security given in preventive framework

2

More weight for secured/priority creditors (CPA)

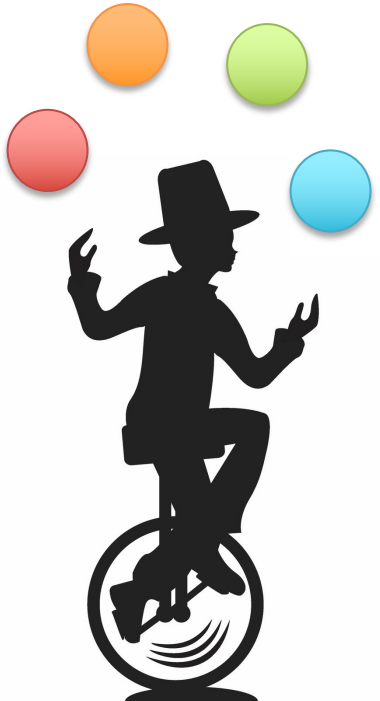
3

Moderating progressivity of debt heavy plans



4

Force the hand of a minority of recalcitrant creditors



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The Relatively Absolute Priority Rule in the Czech Preventive Restructuring Bill

Tomáš Richter

- Context: the Czech absolute priority rule in effect in reorganizations since 2008 (§ 348, 349 IA 182/2006)
- The proposed „relatively absolute“ priority rule in the draft Czech Implementation Bill
- The ups and downs
- The missing parts

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The Role of Shareholders in the Restructuring Plans in the Spanish Project of Implementation of the 2019/1023 Directive

José Carlos González Vázquez

Summary

1. The Problem: The Shareholder Hold-out.
2. The current Spanish “Solution” (since 2014).
3. The Different Alternatives allowed by the Directive.
4. The Option adopted by the Spanish Project.
5. Some Doubts and Proposals for Improvement.

1. The Problem: The Shareholder Hold-Out

- The well-known **risk of extortion by the debtor or the shareholders to obtain a "bigger piece of the pie"** in the restructured company because the have (almost) nothing to lose if they file for bankruptcy (Limited Liability Companies).
- "Member States should ensure that **they cannot unreasonably prevent the adoption of restructuring plans** that would bring the debtor back to viability" (recital 57).

1. The Problem: The Shareholder Hold-Out

- But, **we cannot forget** the opposite problem (also present in the Restructuring negotiations): **The risk of expropiation** of shareholders **by the company's creditors**.
- The shareholder is something more than a creditor (even residual one): **is owner** of the enterprise, has political rights (control power), and also **the right to recieve the restructuring surplus** after paying all the company's creditors.

2. The current Spanish "Solution"

- The shareholders **have the right to participate** in the Restructuring Agreement (RA) **when their rights are affected**.
- So, **the approval of the SGM is necessary when the RA includes matters of its competence** (reduction or increase of legal capital, merger, spin-off, sale of essential assets, etc.).

2. The current Spanish "Solution"

- But **in 2014**, the Spanish Insolvency Act (IA) was **reformed to facilite** the adoption of increase of capital by conversion of company's debts (**Debt-Equity-Swap**), with several measures (arts. 634 and 668 IA):
  - **Reduction of the mayorities** for the adoption of the resolution in the SGM (legal ordinary majorities).
  - Establishing that all the Company's debts will be **considered "liquid, due and payable"** (to comply wiht art. 301 Spanish Company Act).

2. The current Spanish "Solution"

- **"Incentives"** to participate in the Debt-Equity-Swap (**for creditors**):
  - The new shareholders (previously creditors) **will not be considered "specially related to the debtor"** in case of consecutive bankrupty (it would mean "subordinated" creditors). Art. 283.2 first paragrah IA.
  - The express consent of the creditors is needed for the conversión, but those creditors that do not give it **will suffer a reduction equal to the nominal amount that would have received in the debt-equity-swap** (art. 625.2 IA).

2. The current Spanish "Solution"

- **"Incentives" for the debtor and the shareholders** to approve the Debt-Equity-Swap (the "star" and most controversial measure):
  - The consecutive Bankruptcy **will be considered "guilty"** if:
    - **Directors did not propose** the adoption to the shareholders, **without reasonable cause** (art. 700 IA).
    - **Shareholders have refused, without reasonable cause**, to adopt the Debt-Equity-Swap resolution (or an issue of securities or convertible instrument), or have voted against the proposal (art. 701 IA).

2. The current Spanish "Solution"

- **Valuation**:
  - **Lack of solid legal justification** (Company Law).
  - Lack of consistency with the porpuse of Bankruptcy qualification.
  - There is no legal duty to colaborate in the entreprise rescue and viability.
  - Lack of consistency with the right to freedom of enteprise and property rights (option to liquidate it/file for bankruptcy) and. Unconstitutional?
  - **Many technical deficiencies** that hinder its application.
  - **Practical irrelevance** (never applied) and ex post effects.
  - **Lack of provision for other SGM resolution** (reduction of capital, sale of esencial assets, etc.)

3. The Different Alternatives allowed by the Directive

- A Harmonization that hardly harmonizes:
  - Option A: applying arts. 9-11 Directive (especially, **Cross-class Cram-down**), ensuring that equity holders are not allowed to unreasonably prevent or create obstacles to the implementation of a restructuring plan.
  - Option B: **ensure by other means that** those equity holders **are not allowed to unreasonably prevent or create obstacles** to the adoption and confirmation of a restructuring plan (art. 12.1 Directive).

3. The Different Alternatives allowed by the Directive

- In any case, SM are **allowed to adapt what it means to unreasonably prevent or create obstacles** to take into account:
  - whether the debtor is an **SME or a large enterprise**;
  - the proposed restructuring **measures touching upon the rights** of equity holders;
  - the **type of equity** holder;
  - whether the debtor is a **legal or a natural person**; or
  - whether partners in a company have **limited or unlimited liability**.

3. The Different Alternatives allowed by the Directive

- "Equity holders of SMEs that are not mere investors, but are the owners of the enterprise and contribute to the enterprise in other ways, such as managerial expertise, might not have an incentive to restructure under such conditions. For this reason**, the cross-class cram-down should remain optional for debtors that are SMEs"** (Recital 58).

- Equity Holders are able "to **provide** non-monetary restructuring assistance by drawing on, for example, their **experience, reputation or business contacts**" (Recital 59), and so, may have right to retain a "piece of the pie".

4. The Option adopted by the Spanish Project

- When the restructuring plan contains measures that require **the consent/resolution of the partners/shareholders** of the debtor, **the legal regime established for the type of company will apply** (art. 631.1 Spanish Project (SP)).
- So, shareholders are not considered as a more class of creditors (2/3 votes in favor, ¾ if they are secured creditors)

4. The Option adopted by the Spanish Project

- But **with especial rules** to speed up and facilite the agreement, in case of SA and SRL (art. 631.2 SP):
  - **Just 10 days between the call and the meeting** of the SGM (If Listed, 21).
  - The SGM can be held after the file for confirmation of the Restructuring Plan (RP), and can be called by the Judge.
  - If the **SGM is not called, or is not held, or does not approve the RP within the following 10/21 days, it will be considered that they reject the RP.**
  - The **agenda will be limited** to the approval or rejection of the RP.
  - The resolution will be **adopted with the legal ordinary quorum and majority** (not apply legal or bylaws supermajorities).
  - This resolution will be **challenged exclusively by the procedure to challenge the decision on the confirmation** of the RP by dissenting affected parties.
  - Company's debt will be **considered liquid, due and payable in case of Debt-equity-swap** (art. 632 SP).

4. The Option adopted by the Spanish Project

- Possibility of **confirmation of the RP without shareholder approval** (cross-class cram-down), when (art. 639 SP):
  - It has been **aproved by majority of classes (one of the privileged creditors) or, at least a class of creditors that is "in the money"** (report of a restructuring expert about the Enterprise value as going concern).
  - The company is **in inminent (3 months) or current insolvency** (not in case of "probability of insolvency" -2 years-) (art. 640.2 SP).
  - The **company is not allowed to file for bankruptcy** (opposition of restructuring expert of more than 50% of affected credits). (art. 637 SP).

4. The Option of the Spanish Project

- **Exception to the Absolute Priority Rule** (APR): "when it is **essencial to ensure the viability of the company** and the credits of the affected creditors are **not unjustifiably harmed**" (art. 655.3 SP), for example, shareholders "to provide non-monetary restructuring assistance by drawing on, for example, their experience, reputation or business contacts" (Recital 59).
- In case of **SME, it is possible cross-class cram-down applying RPR**: It is enough that the dissident class receive more favorable treatment that any other of lower rank (art. 682.4 SP).

4. The Option of the Spanish Project

- Exceptions to confirmation of the RP without shareholder approval:
  - **No** in case of **SME** (less tan 50 workers; les tahn 10MM incomes) (art. 682.1 y 2 SP).
  - **No** when any partners or **shareholders are liable for company debts** (art. 640.2 SP).

5. Some Doubts and Proposals for Improvement

- Doubts:
  - What happens with the **SHA? Also "deactivated"?**
  - What about **special rules in the company´s bylaw**? For example, requiring previous SGM authorization to iniciate the negociation of a RP or its approval in any case
  - What about **instructions by the SGM to the directors?**

5. Some Doubts and Proposals for Improvement

- Proposals:
  - To **restore preemptive rights** in Debt-Equity-Swap.
  - To **respect,if it is the case, the supermajorities established in the bylaws.**
  - To establish a legal **option in favor of the shareholders on the shares acquired by the creditors** (Price = fase value of their credits converted), in orther to avoid their expropiation by the flucrum class of creditors.

Coffee break

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Session Two:
Fresh Start and other Topics Related to Individual Debtors

Chair: Line Herman Langkjær

Natural Person Ltd.: Towards a Unified Discharge Regime for Entrepreneurs and Consumers

Gauthier Vandenbossche

Overview

- **Natural person ltd. : towards a unified discharge regime for entrepreneurs and consumers**
  - Introduction
  - 1. Directive 2019/1023: discharge of debt for *entrepreneurs*
  - 2. Typology of insolvency procedures
    - 2.1 Typology of procedures
    - 2.2 Typology of debtors
  - 3. The case for a unified discharge regime for natural persons
    - 3.1 Reason 1 – Problems of delineation
    - 3.2 Reason 2 – Entrepreneurs and consumers face the same concerns in an insolvency situation
  - 4. Conclusion

Introduction

- Insolvency and over-indebtedness
  - Social + Economic (initiative ↓ - productive capacity ↓ - productivity ↓)

- **Personal** insolvency procedures (incl. discharge of debts)
  - Fresh start / second chance
  - Entrepreneurs / non-entrepreneurs (*i.e.* consumers)

- Should EU-MS run separate systems of discharge of debts for entrepreneurs and non-entrepreneurs?

1. Directive 2019/1023: discharge of debt for *entrepreneurs*

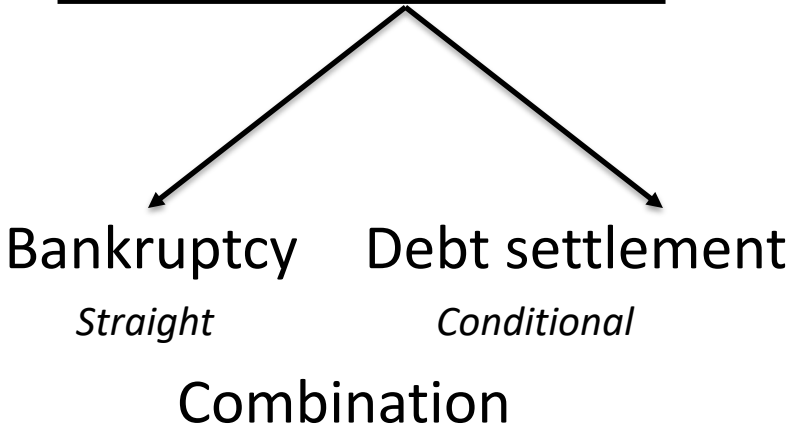
- Directive (EU) 2019/1023
  - *"This Directive lays down rules on: procedures leading to a discharge of debt incurred by insolvent **entrepreneurs**"*
- Optional extension to non-entrepreneurs
  - *"Member States **may** extend the application of the procedures referred to in point (b) of paragraph 1 to insolvent natural persons who are **not** entrepreneurs."*
  - *"For those reasons, although this Directive does not include binding rules on consumer over-indebtedness, it would be advisable for Member States to apply also to consumers, **at the earliest opportunity**, the provisions of this Directive concerning discharge of debt."*

1. Directive 2019/1023: discharge of debt for *entrepreneurs*

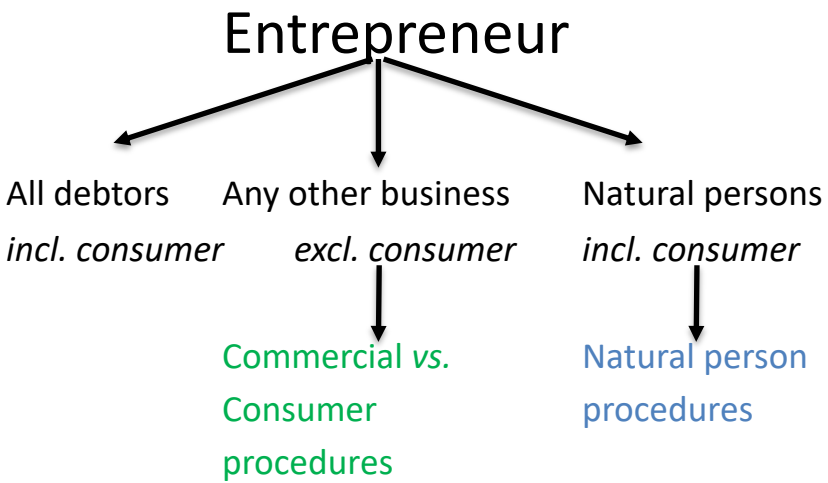
- Impact Assessment:
  - *"However, it needs to be taken into account that Member States would be obliged to regulate a discharge period for entrepreneurs in line with the minimum requirements of a Directive. In those circumstances* ***even non-binding provisions*** *on the extension of that regulation to consumers could* ***have tangible impact*** *on the ground over and above the 2014 Recommendation,* ***particularly in view of the fact that many Member States have common rules for entrepreneurs and consumers*** *and that in practice very often the consumer and business debts of an entrepreneur can hardly be distinguished."*

2. Typology of insolvency procedures

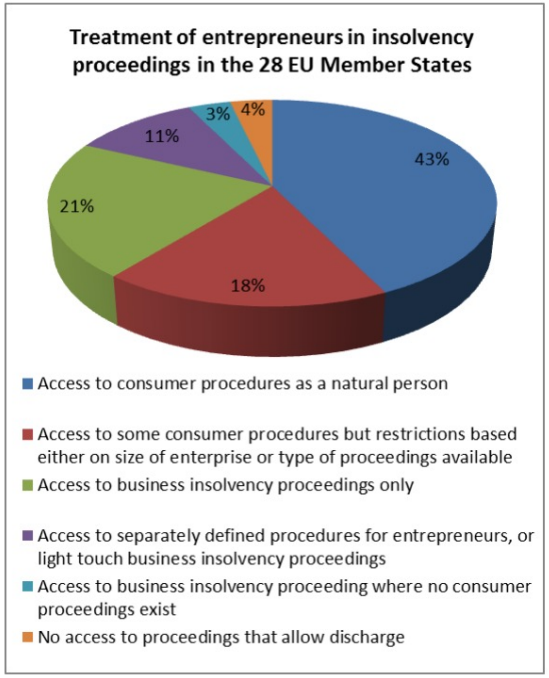
- Typology of procedures



- Typology of debtors



2. Typology of insolvency procedures



Source: EUROPEAN COMMISSION (DIRECTORATE-GENERAL FOR JUSTICE AND CONSUMERS) and UNIVERSITY OF LEEDS (G. McCORMACK, A. KEAY, S. BROWN and J. DAHLGREEN), Study on a new approach to business failure and insolvency: Comparative legal analysis of the Member States' relevant provisions and practices, January 2016, No. JUST/2014/JCOO/PR/CIVI/0075, https://op.europa.eu/s/uVEI, 287.

- <u>Typology of debtors</u>

Entrepreneur

All debtors *incl. consumer*

Any other business *excl. consumer*

Natural persons *incl. consumer*

Commercial *vs.* Consumer procedures

Natural person procedures

3. The case for a unified discharge regime for natural persons

- Reason 1 – Problems of delineation
  - Defining the concept of 'entrepreneur'
    - Company directors
    - Changing labour markets
  - Business and private debts
- Reason 2 – Same concerns
  - Similar issues
  - NINA and LILA debtors
  - Risk-taking
  - Economic and social concerns
    - Economic rationale
      - Economic rehabilitation
    - Humanitarian rationale
      - Human rights

Conclusion

- There is not any public policy rationale for consumers and entrepreneurs to be treated differently.

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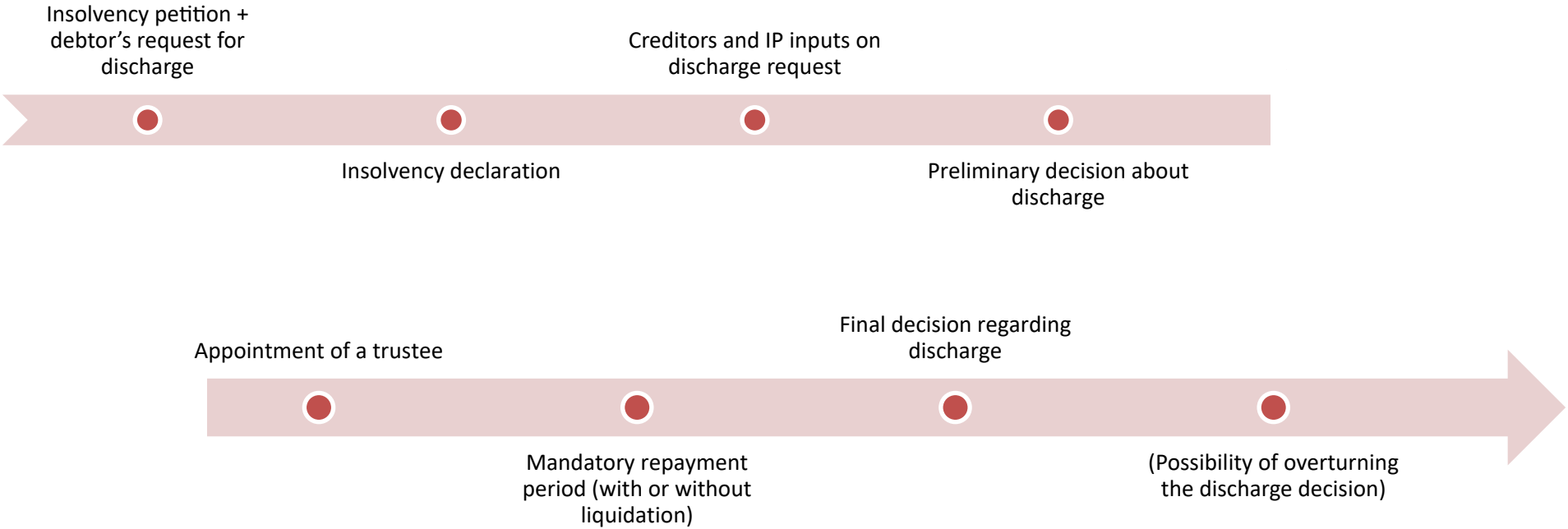
Portuguese Transposition of the Directive (EU) 2019/1023 – Where it Fell Short Regarding Personal Insolvency

Ana Filipa Conceição, Catarina Frade and Fernanda Jesus

Portuguese debt discharge mechanism – *exoneração do passivo restante* – at a glance (2004 Bankruptcy Code - CIRE)



Some perceptions about debt discharge in Portugal

- Structural lack of information about personal insolvency proceedings
- Too late access to any formal proceedings from both debtor and creditors
- Discharge still preferred to court and pre-court debt restructuring mechanisms
- In early years (since 2004 CIRE), courts adopted a conservative approach towards discharge (favouring creditors' side) and were inconsistent regarding debtors' access to repayment period and the rules for disposable income
- Discharge grown on judges and other judicial actors over the years, especially since 2011, when Portugal was bailout and personal insolvencies burst

Some statistical data on insolvency proceedings

(source: Portuguese Ministry of Justice)

- Personal insolvency proceedings represent 3/4 of all insolvency proceedings, since 2011
- Credit recovery rate extremely low (below 10% of the amount claimed)
- 2021 data on discharge:
  - **7200** debtors discharged
  - **112** debtors were refused discharge at preliminary stage
  - **5106** debtors entered into repayment period
  - **887** debtors breached their duties during repayment period
  - **441** debtors were denied discharge at the end
  - **1** discharge decision was overturned

Law 9/2022 of January 11st (transposition of the Directive 2019/1023) (overview)

- Law 9/2022 will come into force on April 11, 2022, and the new provisions will apply to all pending insolvency proceedings
- News provisions of the law apply to all debtors, not only to entrepreneurs (article 1/4 of the Directive)
- Mandatory repayment period drops from 5 to 3 years (articles 235 and 237/b) of CIRE)
- In case of a breach of duties that may disturb or delay the repayment scheme, the debtor, his/her creditors, the trustee or the IP may ask the court for an extension of the repayment period up to 36 months (article 243 of CIRE following article 23 of the Directive)

Law 9/2022 of January 11st (transposition of the Directive 2019/1023) (overview)

- Other rules apart from the directive:
  - court may order a post-closing/supervening liquidation (no assets during proceedings – article 241-A of CIRE)
  - definitive court order regarding the classification and ranking of claims before granting payment to the creditors (article 241/1 d) CIRE);
  - new deadline for creditors to ask for the IP's supervision of the debtors' duties during the repayment period (article 242/3 CIRE);
  - reduction, from one year to six months, of period for creditors to require early termination of the repayment period due to the breach of duties by the debtor (article 243/3 CIRE);
  - the value of the claim, for purposes of appeal regarding this incident, will be the value of the dischargeable debts (article 248-A CIRE)

Where did Law 9/2022 fell short?

- *Overall, a missed opportunity for a new personal insolvency paradigm, based on straightforward discharge, and fewer and simpler procedures*
- *A sum of timid and insufficient measures to explore the Directive possibilities and to address the practical difficulties pointed out by judicial players*

Where did Law 9/2022 fell short?

- Provision of more information to debtors (dedicated websites, debt counseling services; insolvency information services, financial education)
- Elimination of disperse and ineffective debt restructuring proceedings (sole pre-insolvency proceeding)
- Elimination of mandatory repayment period and immediate discharge (repayment plan would remain for those debtors who would like to keep their assets)
- Creation of incentives/rewards for debtors with a repayment plan (or in mandatory repayment period)
- Discharge extended to tax claims

Where did Law 9/2022 fell short?

- Provision of a different treatment for mortgage debts (in 2015, represented circa 80% of the total amount due in personal insolvencies)
- Possibility of a sole proceedings for companies and shareholders, whenever there is a high percentage of personal guarantees
- Reform of the trustee's tasks during the repayment period
- Elimination or cut in personal insolvency proceedings fees, when debtor fills for insolvency

Thank you for your attention!

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Reconsidering Fairness for Vulnerable and Involuntary Stakeholders in Insolvency and Restructuring

Jennifer Gant

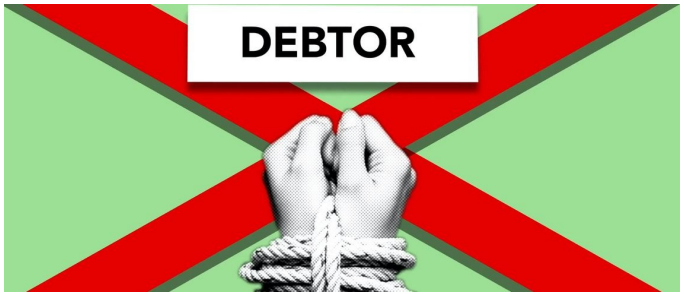
Introduction: Revelations of the Pandemic

The ability to respond to vulnerability demonstrates the relative resilience of an individual or an institution

Different insolvency stakeholders demonstrate different levels of resilience

Consumer Vulnerability in Bankruptcy

- Ondersma: make relief that is ***legally*** available ***actually*** available.
- Recognising that 'It is unjust and nonsensical to require impoverished debtors to undergo an expensive and burdensome process to obtain relief.'



Not an Entirely New Idea!

- Korobkin, 'Vulnerability, Survival, and the Problem of Small Business Bankruptcy' (1994) 23(1) Capital University Law Review 413

Challenging the Status Quo

Views on the resolution of financial distress have been changing

A potential turning point?

A new framework within which the balancing act between wealth maximisation and fairness can be viewed.

A New Theory Responding to Fairness

- Law and economics approaches are exclusionary
- A socio-legal perspective allows for an analysis of current legal structures directly linked with the social circumstances
- Martha Fineman: Vulnerability Theory

Is Equal Treatment Always Fair Treatment?

- Different social values of debts owed to different stakeholders
  - Employees
  - Tort creditors
  - Environmental damage

The Concept of Vulnerability in Corporate Insolvency

- Vunlerability describes:

'a universal, inevitable, enduring aspect of the human condition that must be at the heart of our concept of social and state responsibility.'

Fineman 2008

Social Implications of Corporate Insolvency

- Adjusting the theoretical lens through which we view non-economic features of corporate insolvency
- Focus on stakeholder vulnerability may uncover the weaknesses of institutions
- Redesign with greater fairness in mind

Conclusion

'…[as] law should recognise, respond to, and, perhaps, redirect unjustified inequality, the critical issue must be whether the balance of power struck by the law was warranted.'

Fineman 2017

Thank You

- Dr Jennifer L. L. Gant
- Jenniferl.l.gant@gmail.com

Picture Credits

1. Thomas Claes and Kristina Rehbein, 'Middle-income countries' debt trap' (IPS 2021) <https://www.ips-journal.eu/topics/economy-and-ecology/middle-income-countries-debt-trap-5607/>
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The Gabriel Moss Memorial Lecture

Cross Border Recognition of Corporate Restructuring Arrangements: Reflections on the Preventive Restructuring Directive 2019/1023, National Restructuring Frameworks and the EIR Recast 2015/848

Irene Lynch Fannon

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