INSOL Europe/LexisPSL joint project on the implementation analysis of the Directive (EU) 2019/1023 in the EU Member States

Estonia

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Restructuring & Insolvency analysis: This article looks at how Estonia has implemented Directive (EU) 2019/1023 as part of the Joint Project between INSOL Europe and LexisPSL to track implementation.

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INSOL Europe/LexisNexis research on implementation of the EU Directive

LexisPSL are working with INSOL Europe on a joint project to obtain articles from the INSOL Europe membership and Country Coordinators showing how EU Member States have implemented Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (the EU Directive).

A consolidated table appears at Practice Note: INSOL Europe/LexisPSL Joint Project on EU Harmonisation Directive 2019/1023: consolidated table.

As always, you should contact local lawyers in the relevant jurisdiction to check the current measures in force and the impact of any particular circumstances or nuances of your case.

Question 1: When did/will the new restructuring law come into force? What is/are the name of the new proceedings which comply with the EU Directive?

In July 2022, multiple amendments to several Estonian legal acts came into force in order to allow compliance with the EU Directive.

A draft law was drawn up during an extensive revision of Estonian insolvency laws, adopting the EU Directive.

In relation to natural persons, the Debt Restructuring and Debt Protection Act (RT I, 06.12.2010, 1) was abolished and the new Natural Person's Insolvency Act (RT I, 20.06.2022, 1) came into force. The purpose of the new Act is to enable a natural person suffering payment difficulties to reorganise their debts or discharge their obligations through bankruptcy proceedings, while also ensuring the protection of creditors.

In order to transpose the Directive's provisions on the restructuring procedure of legal entities, amendments were made to the Reorganisation Act, the Bankruptcy Act and the Commercial Code (RT I, 20.06.2022, 1) in Estonia.

In relation to legal entities, the name of the proceedings was and still is: '*saneerimismenetlus'*, and for natural persons was and still is: '*kohustustest vabastamise menetlus'*.

Question 2: Is court approval automatically required? Is court involvement possible during the course of the proceedings? (for e.g. to rule on short notice on conflicts regarding classes of creditors with voting rights, etc…)

The court still plays important role in both restructuring proceedings, for both natural persons and for legal entities. For natural persons debt counselling is prescribed too.

Restructuring proceedings ('*saneerimismenetlus'*) for legal entities begin with the debtor's or creditor's application submission to the county court (first level court instance) in Estonia. The court shall open the proceedings within seven to fourteen calendar days (which can be extended at the court's discretion) if the applica-

tion is submitted by the debtor and the court needs additional information before deciding whether to open restructuring proceedings.

While deciding whether to open restructuring proceedings, the court may demand the debtor to confirm (under oath in court) that the information submitted to the court about assets, debts and economic or professional activities is correct to the best of its knowledge. If the debtor refuses to take the oath, the court may refrain from opening restructuring proceedings.

However, once the proceedings are open, the restructuring advisor and the court shall be involved during these proceedings.

For instance, if the creditor whose claim is to be restructured by the restructuring plan does not agree with the data specified in the debt list, they can submit a written statement to the restructuring advisor, stating the extent to which they do not agree with said claim, while submitting circumstantial evidence. If the statement is not submitted by the due date, the creditor is deemed to have accepted the amount of the claim.

The restructuring advisor will check the legality of the claim of a creditor who disagrees with the claim to commence proceedings, by evaluating the proof and legality of the claim to be restructured and informing the court about a claim that does not actually exist, the size of which is unclear, or the legality or proof of which cannot be assessed. If the restructuring advisor does not agree with the statement of the creditor, they shall immediately forward the statement (together with the evidence they have found) to the court and give reasons why they do not agree with the creditor's statement. The restructuring advisor therefore needs to prove their claims. Based on the submitted statements and evidence, the court then decides the size of the creditor's main and secondary claim and the existence and scope of the guarantees within two weeks from the receipt of the creditor's application to the restructuring advisor.

Before determining the claim, the court may hear evidence from the debtor, the restructuring advisor and the creditor whose claim it concerns. A debtor may file an appeal against a court order determining the amount of the creditor's main and secondary claim.

Question 3: What are the entry criteria (ie must insolvency be proved)? Could you please define the entry criteria under your national legislation?

Paragraph 8 of the Reorganisation Act stipulates that the court shall open restructuring proceedings if the restructuring application meets the requirements set forth in the Code of Civil Procedure (formal criteria) and Reorganisation Act, and if the debtor or creditor has proven that:

- the debtor is not permanently insolvent, but the occurrence of insolvency in the future is likely
- the debtor needs restructuring
- sustainable continuing management of the debtor is likely to be possible after restructuring

However, the restructuring proceedings shall not be opened if:

- the court has already appointed a temporary bankruptcy administrator on the basis of the bankruptcy petition filed against the debtor
- a court order has been issued on the compulsory winding up of the debtor or additional liquidation is taking place
- less than two years have passed since the end of the restructuring proceedings against the debtor
- the conditions and required proofs are not met

If, when deciding to open restructuring proceedings, the court finds that the debtor is permanently insolvent, the court shall propose to the debtor that bankruptcy proceedings be carried out against it. If the debtor agrees, the restructuring application is treated as a bankruptcy application. In such a case, the court rejects the reorganisation application and settles the bankruptcy application instead.

Question 4: Can foreign companies use the process?

The Reorganisation Act does not contain provisions on international jurisdiction for preventive restructuring proceedings and it therefore seems to have some legal uncertainty. Legal entities registered in Estonia are

definitely eligible for preventive restructuring. Paragraph 5 of the Reorganisation Act states that in restructuring proceedings, the provisions governing jurisdiction in the Bankruptcy Act apply to the filing of the application. The Bankruptcy Act refers to the first instance (county) courts. General rules stipulated in the Code of Civil Procedure apply.

Question 5: Does the debtor (ie company's management) remain in possession or is an insolvency practitioner (or any other professional, in that case could you please specify) automatically appointed?

The debtor (company's management) remains in possession, but a restructuring advisor shall be automatically appointed by the court when restructuring proceedings are opened. In most cases, this person has been selected by the debtor (as co-operation is necessary) and the costs of these restructuring proceedings (including advisor's fee) will be governed by the debtor.

After opening the restructuring proceedings, the restructuring advisor prepares a restructuring plan in co-operation with the debtor. When preparing a restructuring plan, the debtor has a duty of co-operation and assistance towards the restructuring advisor. (§ 20 of the Reorganisation Act).

Question 6: Is there any moratorium on claims to protect the debtor during the process? What is the minimum and maximum length of the stay?

Yes, but the term of the initial stay may be no longer than four months from the opening of the restructuring proceedings. However, the stay can be extended at the request of the debtor, creditor or restructuring adviser, or the stay can be re-applied if justified in the particular circumstances, especially if significant progress has been made in the restructuring proceedings and the continuation of the stay is necessary for successful restructuring and does not disproportionately harm the interests and rights of any person affected by the stay. In total, the deadline, including extensions and renewals, cannot be longer than twelve months from the opening of the restructuring proceedings (§ 11(6) of the Reorganisation Act).

Question 7: Are creditors placed into classes for voting purposes? How are 'affected creditors' defined under your legislation?

In general, it depends on the specific restructuring plan and how creditors are handled therein.

An affected person is defined in § 20 (3') of the Reorganisation Act as a creditor whose claim is to be reorganised by the restructuring plan, and as a partner or shareholder whose interests are directly affected by the restructuring plan.

According to § 21 of the Reorganisation Act the restructuring plan must include, among other things:

- the list of the company's assets and liabilities on the date of submission of the restructuring plan, a description of the economic condition of the company and an analysis of the reasons that have led to the need for the company's restructuring
- property value in the case of bankruptcy proceedings, if the bankruptcy proceedings were carried out at the time of submission of the restructuring plan, also taking into account the change in the value of money over time, and the property value, if the restructuring plan is executed, also showing the values of the pledged items in both cases
- identification data of the entrepreneur/company
- details of the person appointed as restructuring advisor
- a description of the forecasted economic condition of the company after restructuring, and reasons why the restructuring plan has reasonable prospects of preventing the company's bankruptcy and ensuring its viability, including the preconditions for the success of the plan
- the deadline for execution of the restructuring plan
- the persons affected by the restructuring plan and the amounts of their claims or the content of interests covered by the restructuring plan
- groups of affected persons formed for the adoption of the restructuring plan, grounds and justifications for the formation of groups

- description and analysis of the appropriateness of the restructuring measure to be implemented, including the description and justification of the transformation of the creditor's claim
- the satisfaction rate of each creditor's claim on the basis of the restructuring plan compared to the satisfaction rate of the claim in bankruptcy proceedings, if the bankruptcy proceedings were conducted at the time of the submission of the restructuring plan, also taking into account the change in the value of money over time
- creditors who are not affected by the restructuring plan and the reasons for this
- a description of the situation of the employees at the time of submission of the restructuring plan and the impact of the restructuring plan on the company's employees
- the conditions of the restructuring plan, including in particular the procedure for informing and consulting employee representatives, the company's estimated cash flows, new financing expected within the restructuring plan, its amount, sources and conditions, and the reasons why new financing is necessary for the implementation of the plan

If the restructuring plan concerns persons with different legal status, the plan must stipulate that the affected persons are treated as separate groups. Separate groups are formed as follows:

- creditors with claims secured by a pledge
- creditors with unsecured claims
- creditors whose claim would be satisfied in a lower rank according to § 153 (4') of the Bankruptcy Act (thus, claims submitted not on time)
- partners or shareholders of the legal entity, if the plan provides for the replacement of the obligation with a part or share of a legal entity as a measure for restructuring the claim

In addition to the groups of affected persons provided for, other groups of affected persons may be formed. One group can be formed by affected persons who have the same interests, which are based on verifiable criteria and are similar. Separate groups are formed from the company's close creditors. The persons specified in subsection 2 of § 117 of the Bankruptcy Act are considered close relatives.

Question 8: What is the voting threshold to approve the restructuring?

According to § 24 of the Reorganisation Act, if groups of affected persons have not been formed the plan has been adopted if creditors who hold at least two thirds of all votes voted in favour of it.

If the affected persons are divided into groups on the basis of the restructuring plan, the plan has been adopted if the persons affected by the plan, who hold at least two-thirds of the votes represented in the group, voted in each group.

A creditor whose claim is not reshaped by the plan, or a partner or shareholder whose interests are not affected by the plan, may not participate in voting, and the amount of their claim or participation is not taken into account when calculating the ratios.

The restructuring plan is adopted by the affected persons by voting at a meeting or without holding a meeting. The number of votes of the creditor is proportional to the size of their main claim. The number of votes of a partner or shareholder is proportional to the size of their share of the share capital or share capital with shares in accordance with the provisions of the Commercial Code.

Question 9: Can shareholders be bound?

It depends on the proposed and approved restructuring plan. The test of creditors' interests establishes that no creditor with a dissenting opinion should be in a worse position under the restructuring plan than it would be in the event of bankruptcy proceedings (and the application of the stages of satisfaction provided for in the Bankruptcy Act). When compiling comparative data on the bankruptcy proceedings, it is based on the fact that the bankruptcy proceedings are carried out at the time of submission of the restructuring plan, taking into account the change in the value of money over time.

If the claim is restructured by replacing the obligation with a part or share of a legal entity, the increase or decrease of the share or share capital is decided in accordance with the proceedings provided for in the Reorganisation Act. A shareholders' general meeting is not convened to increase or decrease the share or

share capital. The decision to increase and decrease the share or share capital is replaced by the court's regulation on the approval of the restructuring plan, including in the event that the partners or shareholders voted against the restructuring plan.

The conditions stipulated in § 192', 197', 342 or 357 of the Commercial Code must be stated in the regulation handled by the court. If it is necessary to change the company's articles of association in connection with the change of share or share capital, the court's regulation also replaces the decision to change the articles of association. Members and shareholders of legal entities do not have preferential rights to subscribe for new shares (§ 22(4) of the Reorganisation Act).

Question 10: How are secured creditors treated?

It depends on the proposed and approved restructuring plan. The test of creditors' interests establishes that no creditor with a dissenting opinion should be in a worse position under the restructuring plan than it would be in the event of bankruptcy proceedings (and the application of the stages of satisfaction provided for in the Bankruptcy Act). When compiling comparative data on the bankruptcy proceedings, it is based on the fact that the bankruptcy proceeding is carried out as of the submission of the restructuring plan, taking into account the change in the value of money over time.

If the creditor's claim is partly secured by a pledge and partly not, it belongs to the group of creditors with claims secured by a pledge to the extent of the part secured by a pledge, and to the group of creditors with claims not secured by a pledge to the extent of the part not secured by a pledge (§ 21 (4) of the Reorganisation Act).

Question 11: How are employees treated?

Claims of employees cannot be restructured. The stay on employees' claims is not applicable.

The employer (debtor), regardless of the provisions of § 22 subsection 2 of Reorganisation Act, is obliged to inform and consult with persons who have claims arising on the basis of an employment relationship. In particular, the debtor is obliged to inform the employees' representatives of the following:

- the deterioration of the economic situation of the entrepreneur (employer) and the probability of insolvency
- restructuring proceedings that may affect the rights of employees
- the restructuring plan submitted to the court for approval

It must be noted that Estonia has a different regime for employees' claims in the case of the employer's economic difficulties or permanent insolvency as there is an Unemployment Fund *(Eesti Töötukassa)* established by the government from which employees' claims will be satisfied in any case.

Question 12: Can certain (holdout) creditors be crammed down? Is the absolute priority rule applied?

Certain (holdout) creditors can be crammed down (see Question 8). However, the affected person who voted against the restructuring plan can submit a reasoned request to the court, in which they can ask the court not to approve the restructuring plan by explaining what constitutes a significant violation of their rights. The application shall be submitted to the court within fourteen days (§ 29 and the following section of the Reorganisation Act below).

In addition, according to § 36 of the Reorganisation Act, the court may approve a restructuring plan that was not accepted by the groups of affected persons, if the following conditions are met:

- the conditions set forth in § 28 (5) of Reorganisation Act have been complied with, with the exception of the condition of affirmative votes specified in § 24 (4) referred to therein
- the restructuring plan has been approved by at least one group of affected persons, with the exception of the group specified in § 21 (2) point 4 of the Act or another group which, as a result of the evaluation of the value of the enterprise based on the restructuring plan, would not receive payments or retain interests, or who do not have a reasonable expectation of receiving

payments or maintain interests if the order of satisfaction provided for in the Bankruptcy Act is applied
- the restructuring plan ensures that groups of affected creditors who remain in disagreement are treated at least as favourably as any group of the same rank and more favourably than any group of a lower rank
- on the basis of the restructuring plan, no group of affected persons may receive more than their total claim against the debtor

The court may even deviate from these provisions if it is absolutely necessary for successful restructuring. When approving the restructuring plan, the court shall assess the creditor's request not to approve the restructuring plan. If the creditor who voted against the restructuring plan has submitted a request not to approve the plan on the basis specified in § 29'' (1) or (2) of this Act, the court shall assess the value of the company's assets to verify the validity of the creditor's request. Otherwise, the court will not assess the value of the company's property on its own initiative.

The court decides whether or not to approve the restructuring plan within thirty days. The court may hold a hearing to decide on the approval of the restructuring plan.

Question 13: Can onerous contracts be disclaimed? Are there any restrictions on ipso facto clauses?

As a general rule, § 6 of the Reorganisation Act stipulates that an agreement according to which the creditor may refuse to perform the contract, speed up the performance of the contract, terminate the contract or change the contract in any other way to the detriment of the debtor due to the submission of a restructuring application, the initiation of restructuring proceedings, the approval of the restructuring plan, the submission of a request to stay, or the suspension of such measures, is void.

With the restructuring plan, it is possible to restructure proprietary claims against the debtor (see § 22 of the Reorganisation Act). Transformation of a claim includes, among other things:

- extension of the deadline for fulfilling the obligation
- fulfillment of the financial claim by instalments
- reduction of the debt amount
- replacement of an obligation with a part or share of a legal entity

The restructuring plan may demand that the credit agreement or other duration agreement concluded by the company before the restructuring application is submitted. This can result in proprietary obligations for the company that become enforceable after the restructuring application is submitted, ending when the restructuring plan is approved. The termination of the contract has the same consequences as the extraordinary termination of the contract due to a circumstance arising from the company. The obligations of the company arising as a result of the termination of the contract can be reshaped with a restructuring plan (see § 22' of the Reorganisation Act).

If it is planned to restructure the obligations arising from the lease agreement, the restructuring plan may stipulate that if the lease is necessary for the continuation of the company's activities and the carrying out of the restructuring proceedings, instead of terminating the lease agreement, the resulting proprietary obligations of the company may be restructured, which become enforceable within one year from the approval of the restructuring plan. These obligations can only be restructured in such a way that the deadline for the fulfilment of obligations is extended by one year from the date of approval of the restructuring plan (§ 22' of the Reorganisation Act).

Question 14: Will the new procedure be listed in Annex A of the EU Recast Regulation on Insolvency 2015/848? If not, how will it be recognised in other countries?

As for natural persons, proceedings called '*kohustustest vabastamise menetlus'* as part of the bankruptcy proceedings ('*pankrotimenetlus'*) was and is listed in Annex A of the EU Recast Regulation on Insolvency.

As for legal entities, restructuring proceedings '*saneerimismenetlus*' and the appointed restructuring advisor ('*saneerimisnıustaja*') should be listed in Annex A and B soon as the Ministry of Justice has made contact with the EU Commission in this regard.

Question 15: Are new money or other arrangements granted any protection/priority (eg DIP finance)?

It depends on the proposed and approved restructuring plan. No specific provisions on that topic are stipulated in the Reorganisation Act apart from the fact that DIP finance is one option and needs to be regulated in the restructuring plan.

Question 16: How long should the process take (roughly)?

It will depend on what has been agreed in the restructuring plan. No maximum deadline is prescribed by law.

Question 17: How much is the process likely to cost (roughly)?

Taking into account the fact that Estonia has the highest inflation rate at the moment in the EU, it is difficult to say. A minimum rough budget should not be less than EUR 30,000 on average.

The debtor under restructuring shall bear the costs of the restructuring proceedings. The procedural costs of the creditors shall be borne by them. The court may leave the creditors' procedural costs to be borne by the undertaking, if the undertaking knowingly submitted an unjustified restructuring application or caused the creditors procedural costs in another way by knowingly providing incorrect data or by knowingly submitting an unjustified request or objection. The debtor shall not be granted procedural aid from the state to cover procedural costs. An appeal may be filed against the ruling on procedural costs (see § 4 of Reorganisation Act).