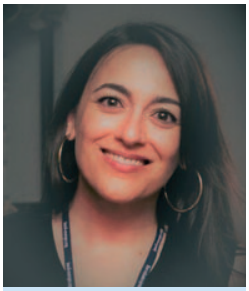
# A closer look at:

# The European Commission Proposal for a Directive harmonising certain aspects of insolvency law



EMMANUELLE INACIO
*INSOL Europe*
*Chief Technical Officer*

> *The objective of this proposal is to reduce differences in substantial insolvency laws and hence address the issue of more inefficient insolvency laws in some Member States*

**Although the Directive on Restructuring and Insolvency adopted on 20 June 2019[1] has not been transposed in all Member States yet, the European Commission already published on 7 December 2022 the proposal for a Directive harmonising certain aspects of insolvency law.[2]**

The objective of this proposal is to reduce differences in substantial insolvency laws and hence address the issue of more inefficient insolvency laws in some Member States, increasing the predictability of insolvency proceedings in general and lowering obstacles to the free movement of capital. By harmonising targeted aspects of insolvency laws, the proposal aims, in particular, to reduce information and learning costs for cross-border investors thus expanding the choice of funding available to companies across the Union. Indeed, this proposal is part of the new EU's Capital Markets Union action plan announced in 2020, which is a key plan designed to further financial and economic integration in the European Union.[3]

The Directive on Restructuring and Insolvency adopted on 20 June 2019 is an instrument of targeted harmonisation, which focused on two specific types of procedure: pre-insolvency procedures; and debt discharge procedures for failed entrepreneurs. On the one hand, the minimum harmonisation standards of the Directive on Restructuring and Insolvency only apply to businesses that are not yet insolvent, i.e. when there is only a likelihood of insolvency, and pursue the very aim of avoiding insolvency proceedings for businesses that can still be returned to viability. On the other hand, the minimum standards on the second chance for failed entrepreneurs do not address the way insolvency proceedings are conducted but relate to the discharge of debts for insolvent entrepreneurs.

As for the proposal for a Directive harmonising certain aspects of insolvency law, it sets out minimum requirements in targeted areas of national formal insolvency proceedings, i.e. the situation where a business becomes insolvent and has to undergo insolvency proceedings, which have a significant impact on the efficiency and length of such proceedings, especially on cross-border insolvency proceedings. This proposal targets the three key dimensions of insolvency law: (i) the recovery of assets from the liquidated insolvency estate; (ii) the efficiency of proceedings; and (iii) the predictable and fair distribution of recovered value among creditors.

## Targeted areas of substantial insolvency law

In order to protect the value of the insolvency estate for creditors, a minimum set of harmonised conditions for exercising **avoidance actions**[4] are first introduced.

The proposal then improves the possibilities of insolvency practitioners to identify and **trace assets** belonging to the insolvency estate for the maximisation of the value of that estate through targeted rules on the access to various registries containing relevant information on assets that belong or should belong to the insolvency estate, including those from other Member States.[5]

Member States will have to include in their insolvency regime a **pre-pack proceeding** composed of a 'preparation phase' followed by a 'liquidation phase' in order to maximise the recovery value of the business at an early stage.[6]

To avoid potential asset value losses for creditors, **an obligation of the directors to promptly submit a request for the opening of insolvency proceedings**[7] is imposed no later than three months after the directors became aware or can reasonably be expected to have been aware that the legal entity is insolvent.

Provisions for **liquidating insolvent micro-enterprises** are also introduced[8] to strengthen procedural efficiency. The cost of ordinary insolvency procedures for these companies is prohibitively high and the possibility to benefit from a debt discharge would enable them to unblock entrepreneurship capital for new projects. Although the provisions of this Directive concerning simplified winding-up proceedings only apply to micro-enterprises, it should be possible for Member States to extend their application also to small and medium-sized enterprises that are not micro-enterprises.[9]

To ensure a fair and predictable distribution of

recovered values among creditors, the proposal introduces requirements for improving the representation of creditors' interests in the proceedings through **creditors' committees**.[10]

Finally, to ensure an enhanced **transparency of the key features of national insolvency proceedings** and help especially cross-border creditors to estimate what would happen if their investments got involved in insolvency proceedings, the proposal provides for an easy access to that information in a pre-defined, comparable and user-friendly format.[11]

## Impacts

If a new EU Directive designed to harmonise substantive insolvency law is most welcome, certain aspects of insolvency law are conspicuously absent from the proposal as – to cite just one example – a harmonised definition of insolvency. Admittedly, the proposal focuses only on aspects of insolvency law facilitating cross-border investment. However, this lack of harmonised definition might lead to practical divergences when implementing the obligation for a director to submit a request for the opening of insolvency proceedings where a legal entity becomes insolvent.[12] Moreover, the proposal provides that a micro-enterprise shall be deemed insolvent for the purposes of simplified winding-up proceedings when it is generally unable to pay its debts as they mature[13] while this insolvency test is not shared by all Member States.

The proposal sets out only minimum harmonisation requirements in targeted areas of substantive insolvency law. However, their transposition is not without problems, especially as regards simplified winding-up proceedings for micro-enterprises. Indeed, an insolvency practitioner will only be appointed if (a) the debtor, a creditor or a group of creditors requests such an appointment and (b) the costs of the intervention of the insolvency practitioner can be funded by the insolvency estate or by the party that requested the appointment.[14]

In practice, the appointment of an insolvency practitioner will never occur if this provision is finally adopted. The problem is that most of the insolvency proceedings in Member States where insolvency practitioners are appointed are winding-up proceedings of micro-enterprises which could harm this profession... Moreover, this provision is inconsistent with the ones strengthening the tracing of assets belonging to the insolvency estate since only an insolvency practitioner can request the courts to access bank account registries or access registries relating to the debtor's assets. Thus, access to this information would not be possible in the context of simplified winding-up proceedings for micro-enterprises… How to protect the value of the insolvency estate for creditors in this case?

## INSOL Europe EU Study Group

As the proposal for a Directive harmonising certain aspects of insolvency law is now open for feedback for a minimum period of 8 weeks,[15] the INSOL Europe EU Study Group composed of Barry Cahir, Florian Bruder, Adrian Théry and Robert Hänel will collect information via the INSOL Europe Council members and Country Coordinators on the positive and negative effects of this proposal in all Members States to contribute to the future discussions before its adoption by the European Parliament and the Council. ■

> ***The proposal sets out only minimum harmonisation requirements in targeted areas of substantive insolvency law***

**Footnotes:**

1 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 (Directive on restructuring and insolvency), OJ L 172, 26.6.2019, p. 18.
2 Proposal for a Directive of the European Parliament and of the Council harmonising certain aspects of insolvency law, 7 December 2022, COM/2022/702 final
3 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, A Capital Markets Union for people and businesses-new action plan, 24 September 2020, COM/2020/590 final
4 Proposal for a Directive harmonising certain aspects of insolvency law, Title II, Art. 4-12.
5 *Ibid.*, Title III, Art. 13-18.
6 *Ibid.*, Title IV, Art. 19-35.
7 *Ibid.*, Title V, Art. 36&37
8 *Ibid.*, Title VI, Art. 38-57
9 *Ibid.*, Recital 35.
10 *Ibid.*, Title VII, Art. 58-67.
11 *Ibid.*, Title VIII, Art. 68.
12 *Ibid.*, Art. 36.
13 *Ibid.*, Art. 38, 2.
14 *Ibid.*, Art. 39.
15 See more information in the Technical Column, p. 42 of this edition