Absolute Priority Rule Dilemmas in the Case of Slovenia

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The paper explores the implications of the Absolute Priority Rule (APR) in corporate bankruptcy law, focusing on its application in the context of Slovenia. The APR stipulates that in bankruptcy proceedings, all creditors must be fully satisfied before shareholders can retain any positions in the reorganized debtor or receive any liquidation payments. Senior creditors must also be satisfied before junior creditors can collect outstanding claims. This rule plays a pivotal role in various bankruptcy scenarios, including bankruptcy liquidation, financial reorganization of insolvent firms, and pre-insolvency (formal) procedures.

The paper discusses exemptions from the APR, which serve as incentives for the prompt initiation of bankruptcy procedures. Different approaches for various sizes of firms in need of restructuring are explored. While creditors have the right to be paid from the debtor's assets, exemptions from the APR are considered a necessary compromise to ensure equitable outcomes, reduce moral hazard, and deter pre-insolvency disposal of assets.

The study acknowledges that deviations from the APR can have both positive ex ante effects and negative ex post effects, making it challenging to measure their overall impact. The economic reality in the United States tends to favour deviations due to negotiation dynamics, with pre-packaged bankruptcy plans gaining importance.

Additionally, the paper provides insights into different comparative approaches to the APR rule, examining its application in countries like the United States, Germany, and England. Special attention is given to "contractual exemptions," where a majority within the class of creditors can agree to deviations.

The paper then shifts its focus to the case of Slovenia, highlighting the country's institutional background in insolvency proceedings. In Slovenia, insolvent firms can opt for reorganization or liquidation, with creditors unable to force the debtor into liquidation. Reorganization proceedings are typically initiated by the debtor, and any insolvency filing triggers the automatic stay rule. Conventional reorganization plans often involve reducing or postponing the repayment of debt held by ordinary unsecured creditors, while equity holder positions remain unaffected.

The paper discusses key reforms in Slovenia, including those in 2011 and 2014. The 2011 reform introduced minimum payment requirements for debtors in reorganization plans. In 2014, mandatory APR rules were established, along with mandatory debt-to-equity conversion. The reform also allowed for splitting the undersecured portion of secured claims and provided the possibility of postponing payments and lowering interest rates for secured creditors. Creditor-initiated insolvency reorganizations were made possible as well.

In conclusion, the paper emphasizes that the debate surrounding the pros and cons of the APR rule is ongoing. Different countries continue to have varying interpretations of how to implement the APR rule, and the European Union Directive on restructuring and insolvency has raised further questions and interests in this regard. The paper cautions against the incorrect adoption of the APR rule, as it can have adverse consequences for a country's insolvency law.