

Transposition of the Preventive Restructuring Directive into Ukrainian Law

Oleksiy Kononov comments on the alternative bills proposing the adoption of the Directive in Ukraine¹



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On 9 November 2023, the Parliamentary Economic Development Committee recommended the adoption of the Bill implementing the EU Preventive Restructuring Directive 2019/1023 (“Bill #10143”)² at the first reading. The next day, the Cabinet of Ministers of Ukraine presented its own (alternative) bill on the same subject (“Bill #10228”).³

The imminent transposition of Directive 2019/1023 (“Directive”) into Ukrainian law is driven by several factors:

- (1) The attainment of candidate status by Ukraine for EU membership in June 2022 mandates compliance with the Directive as part of the EU *acquis*;⁴
- (2) Fulfilling conditions for micro-financial assistance in 2023, crucial during wartime, necessitates legislation aligning with Directive principles to enhance corporate bankruptcy and insolvency regimes, allowing for full debt discharge;⁵
- (3) Transposition is integral to the Roadmap for Capacity-Building Activities designed to facilitate the implementation of the Code of Ukraine on Bankruptcy Procedures adopted by the Ministry of Justice in September 2023;⁶ and
- (4) The European Commission’s November 2023 emphasis on the imperative of enhancing Ukraine’s bankruptcy legislation further underscores the urgency for the transposition of the Directive.⁷

It is important to keep in mind that the conditions for providing micro-financial assistance for 2023 required Ukraine to implement the Directive by the end of 2023, and it appears that the country failed to meet that deadline. Given the complexity of preventive restructuring and Ukraine’s unique situation of having to transpose the Directive during wartime, the failure to meet the deadline is not surprising. What remains clear is that the transposition of the Directive will occur sooner or later, and the bills tabled in Parliament provide a certain idea of how the Ukrainian restructuring procedure may ultimately look.

Existing restructuring framework and problems

Preventive restructuring is not a new concept for Ukraine. Article 5 of the Bankruptcy Code (“BCU”)⁸ outlines procedures for the so-called “pre-trial rehabilitation”. Pre-trial rehabilitation in many respects resembles the English scheme of arrangement,⁹ and involves the development of a rehabilitation plan, its prior approval by creditors, and further sanctioning of the plan by the respective commercial court. In essence, the existing procedure is essentially compelling creditors to adhere to a rehabilitation plan developed by the debtor under the strict supervision of the court.

According to the drafters of Bill #10143, the existing regulations do not provide clarity for their practical application, contain numerous contradictions with other provisions of the Code,

and lack clear guarantees for debtors and creditors, which could have ensured the debtor’s rehabilitation before initiating bankruptcy procedures.¹⁰ Consequently, the existing pre-trial rehabilitation remains unpopular, with only 14 pre-trial rehabilitation plans approved by the courts between 2019 and late 2023.¹¹

Different approaches to smaller businesses

Bill #10143 is more radical compared to Bill #10228. It suggests a drastic revision of the BCU by introducing an entirely new section on preventive restructuring, with specific options available for micro and small enterprises, which are the most vulnerable to insolvency. Bill #10228 essentially transposes the minimum requirements of the Directive and offers no special solutions to micro and small enterprises.

Early warning tools; Internet portal

Both bills propose detailed obligations for company management to inform equity holders about impending bankruptcy risks, with preventive restructuring as a recommended measure. Bill #10143 requires auditors, accountants, and lawyers to alert debtor management of insolvency indicators. However, neither bill specifies consequences for failing to notify equity holders or the debtor. It is unclear if executive agencies and municipal authorities will solely monitor state and municipal enterprises or have broader notification powers.



The conditions for providing micro-financial assistance for 2023 required Ukraine to implement the Directive by the end of 2023



Without clarity, these rules may remain moot in practice.

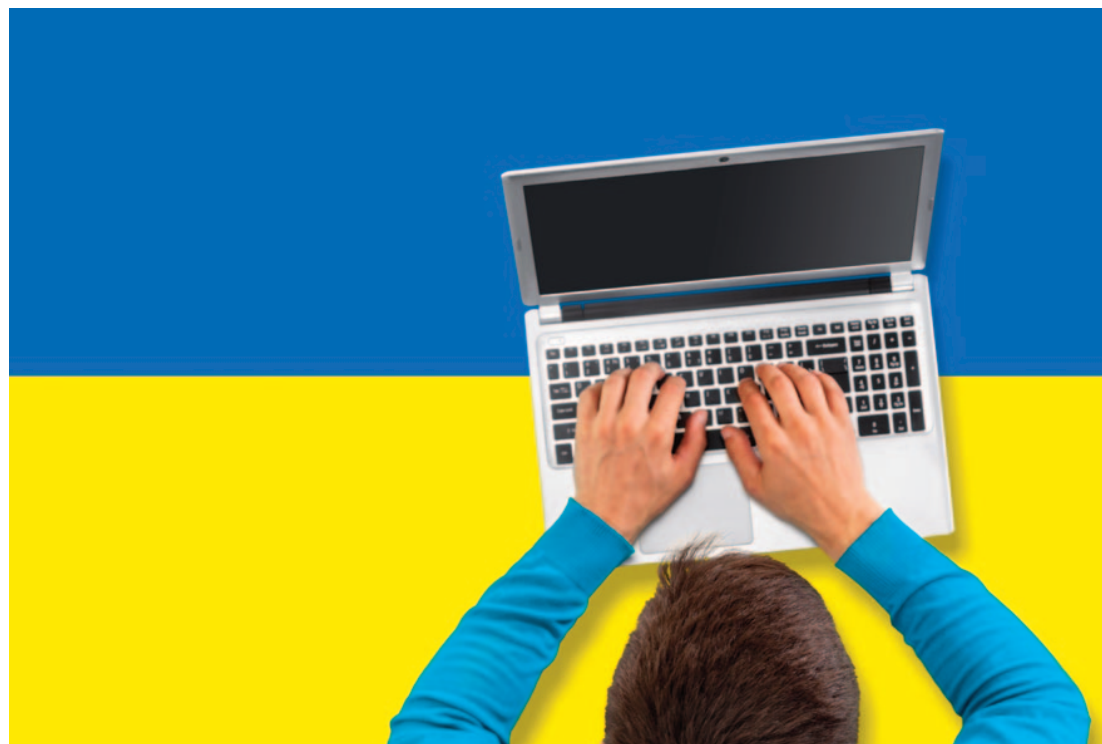
Another important and undoubtedly very useful novelty suggested by both bills is the extended authority of the Ministry of Justice on matters related to preventive restructuring. In particular, the ministry will be responsible for the development and maintenance of a dedicated web portal focused on preventing insolvency. This portal will offer information on early warning tools provided by public authorities, details about preventive restructuring measures and procedures, and comprehensive guidance.

The introduction of the web portal is promising: it will provide much-needed assistance to debtors with limited resources and may become a new milestone for Ukrainian authorities in developing new digital tools for those in financial distress.

However, the launch of such a portal entails expenditure¹² that is hard to come by, given the state budget has been heavily exhausted by the ongoing war. This problem may not only delay the launch of the portal but also the adoption of either of the two bills into law.

Restructuring plans

Both bills retain the option to employ procedures resembling the existing pre-trial rehabilitation in cases where the debtor already possesses a restructuring plan approved by creditors before applying to court. However, instead of mandating the submission of a plan pre-approved by creditors to the commercial court to initiate pre-trial rehabilitation, both bills propose that debtors can present a draft restructuring plan which can be meticulously negotiated with creditors and amended after the initiation of preventive restructuring. Both bills provide detailed requirements for creditors' voting on the proposed plan and debtor's reporting obligations, which would certainly eliminate problems of the lack of transparency inherent in the existing pre-trial rehabilitation.



Unlike existing pre-trial rehabilitation procedures, debtors will be able to initiate preventive restructuring without presenting a plan to the court. Instead, a preventive restructuring trustee, chosen from arbitration managers, will be mandatory to assist in plan development. Bill #10143 allows micro and small enterprises to submit a concise 'concept of preventive restructuring' as an option. These changes offer advantages by granting debtors with limited resources more flexibility but also increase costs due to mandatory trustee involvement, posing potential financial challenges for micro and small businesses.

Stay and protective measures

Prohibiting affected creditors from initiating insolvency procedures against the debtor is perhaps the most important novelty proposed by both bills in accordance with the Directive. The existing pre-trial rehabilitation chronically suffers from compelling debtors to hide their plans until the final stages to prevent creditors from

instigating bankruptcy proceedings, thereby undermining preventive measures against insolvency.¹³ The stay will also entail the suspension of financial sanctions against the debtor; suspension of the statute of limitations for affected creditors' claims, and restrictions on foreclosure on the debtor's assets.

In addition to that, both bills provide for the possibility for a court to apply protective measures, such as prohibiting enforced collection from the debtor based on enforcement documents, except during the stage of distributing proceeds, introduction of a moratorium on satisfying creditors' claims, and restrictions on certain transactions by the debtor. It is worth noting that, according to Bill #10143, protective measures can be requested only by the debtor, while under Bill #10228, both the debtor and creditors can petition the court to apply such measures. Under both bills, the application of protective measures cannot exceed the period of six months.

Bill #10143 includes safeguards against potential abuses by debtors seeking to



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prolong insolvency. Protective measures are only instituted, if the debtor provides a substantiated plan for preventive restructuring, presents comprehensive financial information, and non-implementation of protective measures would hinder restructuring or lead to insolvency.

Classes of affected creditors

Currently, under the BCU, categorizing creditors into classes for pre-trial rehabilitation plans is optional. Both bills seek to make this mandatory in line with the Directive, with Bill #10143 being more detailed. It requires division into secured creditors, unsecured creditors, unsecured creditors interested in the debtor (such as a parent company, affiliated companies, debtor's managers and executive officers, relatives etc.), and equity holders. Additional classes may be created based on factors like obligation deadlines, claim amounts, and creditor types, with criteria outlined in the preventive restructuring plan.

A class of employees must be established, if the proposed restructuring involves employee claims. The preventive restructuring plan cannot allocate different proportions for satisfying claims within a single class. Any creditors within that class facing a worsened position must unanimously consent in writing to the change. Under both bills, affected creditors may contest the formation of classes in court.

Unfortunately, neither of the two bills incorporates an opt-out provision available in the Directive, which would allow debtors representing micro and small businesses to forego dividing creditors into classes.

Plan approval; cross-class cram down

Both bills stipulate that a proposed restructuring plan is deemed approved by the secured creditors' class if it garners support from creditors entitled to vote, possessing at least two-thirds of the votes from the total secured

claims included in the plan within this class. For unsecured creditors, the plan requires more than 50% of the votes from the total unsecured claims included in each class for approval.

Alongside the stay provision, cross-class cramdown will undoubtedly be a significant addition to Ukrainian insolvency law. Both bills adopt Directive provisions, which mandate the respective court to cram down the plan on dissenting creditors if:

- no grounds exist for rejecting it;
- the plan is approved by a majority of affected parties'; voting classes, with at least one being secured creditors or senior to ordinary unsecured creditors, or by a class other than equity-holders;
- dissenting creditor classes are treated equally or better than similar ranks, and more favourably than junior classes; and
- no class receives or retains more than their full claims or interests under the plan.

Monitoring and conclusion of the procedure

Under both bills, either the debtor or the appointed preventive restructuring trustee must submit implementation reports to the court. Bill #10143 limits the preventive restructuring plan's implementation to a maximum of four years, whereas Bill #10228 does not impose such a restriction.

The restructuring procedure concludes upon the submission of a report detailing the fulfilment of the preventive restructuring plan to the court. Bill #10228 offers more avenues for affected parties to contest the conclusion and extend the procedure, while Bill #10143 emphasizes "successful" completion but lacks explicit provisions for objections by affected parties.

Summary

At present, it is uncertain which of the two bills introduced in

Parliament will prevail, with a possibility of legislators combining strengths from both for a more comprehensive approach to transposition. The efficiency of this process in Ukraine's unique circumstances remains uncertain. Challenges are acknowledged, and stakeholders anticipate the new preventive restructuring mechanism will not be fully operational immediately upon enactment. Nonetheless, both bills offer a solid foundation to address deficiencies in the existing pre-trial rehabilitation system, especially if focusing on aiding micro- and small enterprises. ■

Footnotes:

- This project has received funding through the MSCA4Ukraine project, which is funded by the European Union. Views and opinions expressed are however those of the author only and do not necessarily reflect those of the European Union. Neither the European Union nor the MSCA4Ukraine Consortium as a whole nor any individual member institutions of the MSCA4Ukraine Consortium can be held responsible for them.
- Bill #10143 of 12 October 2023 on amending of the Code of Ukraine on bankruptcy procedures and other legislative acts of Ukraine regarding the implementation of Directive 2019/1023 of the European Parliament and the Council of the European Union and the introduction of preventive restructuring procedures, available in Ukrainian at: <https://itd.rada.gov.ua/billInfo/Bills/pubFile/2025002>.
- Bill #10228 of 8 November 2023 on amending some legislative acts of Ukraine regarding the improvement of preventive procedures and prevention of bankruptcy (text presented on 10 November 2023), available in Ukrainian at: <https://itd.rada.gov.ua/billInfo/Bills/pubFile/2064509>.
- European Council, 'Meeting (23 and 24 June 2022) – Conclusions'; EUCO 24/22, para. 11; Commission, 'Staff working document Ukraine 2023 Report Accompanying the document Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions 2023 Communication on EU Enlargement policy'; SWD/2023/699 final, 28.
- Memorandum of Understanding between the European Union as Lender and Ukraine as Borrower of 16 January 2023 – Instrument for providing support to Ukraine for 2023 (micro-financial assistance+) of up to EUR 18 billion.
- See: <https://minjust.gov.ua/news/ministry/minyust-zavverd-dorozhnyu-kartu-u-serii-bankrutstva>.
- SWD/2023/699 final, 28.
- Code of Ukraine on Bankruptcy Procedures of 18 October 2018 (in force since 21 October 2019).
- Olha Stakheyeva-Bogoviyk, *New Bankruptcy Code of Ukraine: What to Expect* (2019) 76 *Euroforum* 26, available at: <https://www.insol-europe.org/download/documents/1585>.
- Explanatory note to Bill #10143, available in Ukrainian at: <https://itd.rada.gov.ua/billInfo/Bills/pubFile/2025003>.
- The number can be inaccurate and in fact lower due to the absence of data officially published by the Department of Bankruptcy, Ministry of Justice of Ukraine. Besides, it is not uncommon for the Supreme Court to quash decisions of trial courts approving pre-trial rehabilitation plans many months after the approvals by the trial court.
- The budget problem was emphasized by the respective parliamentary committee, for which see: <https://itd.rada.gov.ua/billInfo/Bills/pubFile/2128344>; <https://itd.rada.gov.ua/billInfo/Bills/pubFile/2120630>.
- Round table 'Preventive Restructuring according to Bill #10143'; Kyiv, Ukraine, 8 December 2023 (in Ukrainian), available at: <https://www.facebook.com/Pravojusticeukraine/videos/262958836778151>.