Inside Story – Spanish Reforms

The government of Spain is preparing another bankruptcy act reform to give viability to small and medium companies, facing the international monetary fund reviews about Spanish bankruptcy proceeding. Agustín Bou of Jausas Legal in Spain reports on the new reforms.

The Real Decreto Ley 4/2014, of 7 March (published in BOE No 58 –Spanish gazette- of 03.08.2014) introduced important amendments to the Spanish Insolvency Act ("LC"), to ease the process of restructuring and refinancing in order to prevent companies that may be viable becoming insolvent as a result of excessive financial burden, although it appears that the regulation is intended primarily for medium and large companies.

Basically, the *Real Decreto Ley* 4/2014 ("RDL 4/2014") has modified three aspects: (i) The so called preconcurso* introducing the novelty of the stoppage of judicial executions on necessary assets for the continuity of the business or profession of the debtor, (ii) refinancing agreements, easing the process for their preparation and introducing the possibility of individual refinancing agreements, and (iii) the approval of refinancing agreements, collecting the possibility of extending its effects to all financial creditors, including those who voted against and creditors with security in rem, if the conditions provided by law.

However, the public creditors have been left out of the reform: the administrative charge proceedings are not paralysed with the *preconcurso* request and they are not subject to refinancing agreements nor even a court approval. These privileges of public creditors have received criticism from the International Monetary Fund itself, who reminded the Spanish Government that most of the debts of small and medium companies are to public creditors.

Moreover, this reform is intended to be applied to refinancing processes that are initiated from its entry in force, which took place on 9 March 2014, so it may not apply to companies that are already in insolvency, such as Pescanova and Madrid radial highways, or in cases where an agreement with grave difficulties of compliance has been approved, as happens with the real estate company Martinsa Fadesa.

Also, following the approval of the reform, the European Commission Recommendation of 12 March 2014 concerning a new approach to insolvency and business failure was published in the European Union Gazette, which urges European countries not only to establish a framework for the efficient restructuring of viable companies with financial difficulties (the goal that the RDL 4/2014 pursues), but also to provide the system with mechanisms that provide a second chance to frustrated

entrepreneurs, allowing total debt forgiveness except in cases of dishonest acting or in bad faith. However, the Spanish insolvency framework lacks efficient mechanisms to ensure this vital second chance.

In order to solve these loopholes, although the official excuse is the willingness to make improvements, the Government has decided to deal with the RDL 4/2014, and validated in the House of Representatives on 20 March 2014 (BOE No 74 of 03.26.2014), as a bill, which will also be used for improving the liquidation phase in the sense of providing for the assignment of contracts, permissions and licenses without the consent of the contracting parties in case of sale the production units.

However we believe that the sticking point will be the cutting of the privileges hold by the public creditors, after that the Ministries of Finance and Employment and Social Security have already expressed their opposition.

In summarising, since 2009 there have already been four main reforms of the Bankruptcy Act, but it seems that the Spanish legislator has not yet reached a formula that prevents the 95% of insolvent companies in Spain going into liquidation. Only time will tell if the next reform will be able to provide the ultimate solution to this alarming destruction of the Spanish network of businesses.

*allows the debtor to inform the Commercial Court at the start of negotiations to reach an agreement to refinance or a proposal for agreement. After making such a communication, the duty to initiate insolvency proceedings is not enforceable. But after three months from the filing date of the communication, whether or not an agreement to refinance or accessions necessary for a proposal for agreement have been reached, a declaration of bankruptcy must be applied for within one month if the state of insolvency persists.

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