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Rescue of Business in Insolvency Law

The European Law Institute

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REPORTERS' PREFACE

We are pleased to present our ELI Business Rescue Report. It contains 115 recommendations on a wide variety of themes affected by the rescue of financially distressed businesses: the legal rules for professions and courts, contract law, treatment and ranking of creditors' claims, labour law, laws relating to transaction avoidance and corporate law, all focused on business rescue, including specifying specific rules for MSMEs (Micro, Small and Medium sized businesses).

These recommendations flow from our analysis of a selection of national laws with regard to restructuring and insolvency, a considerable volume of work that has been carried out in this field by organisations such as the United Nations Committee on International Trade Law (UNCITRAL) and the World Bank, and our own study and research of a vast amount of recent legal literature. For convenience of reference, the complete texts of our recommendations are set out in the front of this Report. Thereafter we provide, divided in ten chapters, our detailed analysis and references per chapter, pertaining to the recommendations.

In this preface, we explain our working method over the last four years. After having received approval of our proposal by the ELI Council in September 2013, we made a start with this study on 'Rescue of Business in Insolvency Law'. As the project title indicates, it surveys the legal rules and practices relevant for the rescue of financially distressed businesses and the application of such rules in practice. The ultimate aim of our study is to design a framework that will enable the further development of coherent and functional rules for business rescue in Europe. The ELI Business Rescue Project ran over a period of three and a half year, with as outcomes: (i) a report containing inventory reports on national insolvency regimes in Europe, as well as an inventory of international recommendations from standard-setting non-governmental organisations; and (ii) the present ELI Business Rescue Report. It states the law as it is on 28 February 2017.

Since the global financial crisis, insolvency law has been at the forefront of law reform initiatives in Europe and beyond. The specific topic of business rescue appears to rank top on the insolvency law related agenda of the EU institutions. The economic recession in Europe has faced a rapid growth of insolvencies, clearly highlighting the importance of effective business rescue. More recent the downfall of oil prices and for instance the problems retail markets face, are other causes for ongoing harm for businesses. In an introductory overview in the report, we provide further background to the developing legal background of business rescue, including the initiatives taken since 2011 by European institutions, particularly the European Commission, resulting in its Proposal for a Restructuring Directive in November 2016. We further also set out our working method over the last three years.

Crucial for our work has been our cooperation with National Correspondents who provided detailed insights into the national insolvency regimes of EU Member States by preparing inventory as well as normative reports. They did so on the basis of a detailed Questionnaire, which is to be found in Annex 1, and a set of normative questions, to be found in Annex 2. In this way, the reporters obtained detailed information of each selected jurisdiction on their rescue-related restructuring and insolvency laws. In addition, we considered it to be both appropriate and necessary to take account of the considerable volume of work that has already been carried out in the field of restructuring in recent years by a number of international non-governmental organisations. Selecting, analysing and identifying core values and principles in the area of business rescue therefore has been an integral part of our work.

The project also draws from the expertise of the Members Consultative Committee consisting of ELI Members and an Advisory Committee, with renowned experts from very different fields of law that took an interest in the project and its outcomes. The names of the National Correspondents and the members of the Advisory Committee, in all some forty persons, are listed in Acknowledgments.

In recent years, many Member States have introduced laws regarding business restructuring or amended existing laws to create systems ensuring the survival of economically efficient, but financially viable businesses. International non-governmental organisations have produced principles, guidelines and statements of best practices, all aiming for well-functioning restructuring and insolvency systems. The European Commission introduced by way of a Recommendation in March 2014 its new policy to prevent business failures and insolvency leading to recent proposals on preventive restructuring frameworks and second chance for entrepreneurs. The result of all these rather uncoordinated streams of rules is a delta with a bewildering variety of technical terms and expressions used in the various texts, so one can't see the wood for the trees. Therefore, we developed a Glossary of Terms and Expressions (following the text of the full set of recommendations at the beginning of the Report), with the aim of promoting the development of a uniform European legal terminology in matters relating to restructuring and insolvency. The Glossary containing around 160 of those terms serves the homogeneity of workout, pre-insolvency (restructuring) and insolvency processes and should assist insolvency practitioners, courts and legislators in their work. The Glossary partly finds its basis in a Glossary, included in 'Transnational Insolvency: Global Principles for Cooperation in International Insolvency Cases', Report to the American Law Institute (March 30, 2012).

As a follow-up to the European Commission's Recommendation of March 2014, the Commission published late November 2016 its Proposal for a Restructuring Directive on (amongst others) preventive restructuring frameworks, just two months before the date of our planning to finalise the text of our Report so it could be subject to the process of discussion and approval within the European Law Institute. With the approval of the ELI Council we have not integrated specific rules of this proposal in the body of our texts. Leaving aside the fact that the first reactions to the Proposal for a Restructuring Directive (2016) have been rather mixed, the final text is far from being certain as it will be the result of several consultations with the European Parliament and the Council, which may take considerable time. In some cases, however, we thought it appropriate to include references to the proposal in our footnotes. Still, the theme of the Proposal Restructuring Directive (2016) of enhancing a rescue culture in Europe is the theme of our whole report and we have been fortunate that the staff of the Commission was involved in all stages of development of our recommendations as an observer, and that the reporters have had the chance to influence the process that lead to the proposal by attending stakeholder meetings in 2016 in Brussels.

Here we may also mention that in from 2014 to early 2017 four half day to one and a half day seminars were held, where ELI members, National Correspondents and invited judges debated and discussed various sections of the project as the work progressed. These meetings were held at the University of Zagreb (2014), the University of Vienna (2016), the University of Ferrara (2016) and the University of Leiden (2016). Moreover, certain parts of the draft text of the Report were exposed for comment at a number of seminars and meetings with academics, insolvency practitioners and judges in some eight countries. The feedback from all these gatherings, involving hundreds of experts from some 15 EU Member States, has been particularly instructive and the present text is based on the cumulative results of discussions in these meetings and suggestions communicated by individuals to the Reporters. We are very grateful for all the assistance received.

At the outset of the project, three reporters were appointed by the ELI to take responsibility for the project and to coordinate its outcomes, including the present ELI Business Rescue Report describing an appropriate legal enabling framework that supports the rescue of viable businesses in a situation of distress. Prof Dr em Bob Wessels (University of Leiden), Prof Dr Stephan Madaus (Martin Luther University Halle-Wittenberg) and Associate Prof Kristin van Zwieten (Oxford University). Due to reasons unrelated to the project since April 2016 Kristin van Zwieten stepped down from being a reporter for the project. During the whole period, the reporters were assisted by Gert-Jan Boon (University of Leiden), and the staff of the ELI Secretariat (in particular Alina Lengyel, Rosana Garciandía, Dadi Olafsson and Tomasz Dudek). We would like to thank all of them for their continuing support.

The reporters take individual as well as collective responsibility for the contents of the report as a whole and the resulting recommendations. We point out that Bob Wessels primarily worked on the Introduction and Chapter 1 (paragraphs 1.1), 2, 6, 7 and 9, whilst Stephan Madaus has worked on Chapter 1 (paragraph 1.2 and 1.3), 3, 4, 5, 8 and 10.

We believe that our recommendations are in line with international developments and other attempts of developing modes of restructuring and insolvency. We think we can fairly claim that our Business Rescue report provides the responses to the question posed in the study, the European Law Institute entrusted to us at the time of our appointment.

We recommend, amongst others, further strengthening of the professional and honest roles all parties involved (insolvency practitioners, turnaround managers, courts, company directors), the introduction of tools (such as a stay on enforcement actions of creditors and forms of available finance) and procedural safeguards to enable serious rescue efforts of viable businesses, whilst protecting justified interests. In relation to the necessities of a pursued rescue strategy we set norms for provision of information to all stakeholders, for the (non-)continuance of contracts and for the integrity of the process of negotiations between stakeholders (mainly creditors) of and voting on a restructuring plan, including – if necessary – a court's approval. To better reflect the demands of real business life, we recommend specific approaches for MSMEs (Micro, Small and Medium sized businesses) as well as for groups of companies, a collection of legally independent legal subjects, however financially or operationally functioning as one economic unit. We are therefore confident that the recommendations, and the report supporting these, form a framework that will enable the further development of coherent and functional rules for business rescue in

Europe. If the reports and the recommendations are formally approved by ELI, they can be commended for use by the European institutions active in this field, Member States, organisations and associations of turnaround managers, insolvency practitioners and judges, and other groups across Europe, in the meaning of the terms of our initial engagement.

As reporters, we have reached the completion of our joint labours and we wish to express our appreciation to ELI for the privilege of having served as reporters for this most timely and important project, and to all those who have provided input during its elaboration.
We cherish the hope that the outcome will make a significant contribution to the European architecture of restructuring and insolvency.

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CHAPTER OVERVIEW

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LIST OF ABBREVIATIONS

A-G	Attorney General
ABI	American Bankruptcy Institute
ABI Journal	American Bankruptcy Institute Journal
AC	Advisory Committee (ELI Business rescue project)
ALI	American Law Institute
B.C.	US Bankruptcy Code
BB	Der Betriebsberater
BGH	Bundesgerichtshof
CJEU	Court of Justice of the European Union
Ch.D	Chancery Division
CMLR	Common Market Law Review
CoCo Guidelines (2007)	European Communication and Cooperation Guidelines for Cross-border Insolvency 2007
COMI	Centre of a debtor's main interests
Cong.	Congress
CR&I	Corporate Rescue and Insolvency
DIP	Debtor in possession
diss.	Dissertation
Doct. Th.	Doctoral Thesis
DZWIR	Deutsche Zeitschrift für Wirtschafts- und Insolvenzrecht
EBLR	European Business Law Review
EBOR	European Business Organisation Law Review
EBRD	European Bank for Reconstruction and Development
EBLR	European Business Law Review
EC	European Community
ECB	European Central Bank
ECFR	European Company and Financial Law Review
ECHR	European Court of Human Rights
ECJ	European Court of Justice
ECL	European Company Law
ECLI	European Case Law Identifier
EEA	European Economic Area
EESC	European Economic and Social Committee
EIR (2000) or European Insolvency Regulation (2000)	Council Regulation (EC) 1346/2000 of 29 May 2000 on insolvency proceedings, OJ L 160 of 30 June 2000
EIR (2015) or European Insolvency Regulation (2015)	Regulation (EU) 2015/848 of the European Parliament and the Council of 20 May 2015 on insolvency proceedings (recast)

ELI	European Law Institute
EP	European Parliament
ERPL	European Review of Private Law
et al.	and others (et alii)
etc.	et cetera
EU	European Union
Eur. Bus. L.R.	European Business Law Review
EuZW	Europäische Zeitschrift für Wirtschaftrecht
EWiR	Entscheidungen zum Wirtschaftsrecht
EZWiR	Europäische Zeitschrift für Wirtschaftsrecht
FIP	Tijdschrift Financiering, Zekerheden en Insolventiepraktijk
GRR	Global Restructuring Review
ICCLR	International Corporate and Commercial Law Review
ICR	International Corporate Rescue
IFLR	International Financial Law Review
IILR	International Insolvency Law Review
III	International Insolvency Institute
IIR	International Insolvency Review
INSOL Europe	International Federation of Insolvency Professionals International
Ins. Int.	Insolvency Intelligence
IOH	Insolvency Office Holder
JBL	Journal of Business Law
JOR	Jurisprudentie Onderneming & Recht
JudgeCo Guidelines	EU Cross-Border Insolvency Court-to-Court Cooperation Principles
Jur.	Jurisprudence of the European Court of Justice
KSI	Kölner Schrift zur Insolvenzordnung
KTS	Konkurs- Treuhand- und Schiedsgerichtswesen, Zeitschrift für Insolvenzrecht
MCC	Members' Consultative Committee (ELI Business rescue project)
MSMEs	Micro, Small and Medium sized businesses
NCs	National Correspondents Practice Guide (ELI Business rescue project)
NIBLeJ	Nottingham Insolvency and Business Law e-Journal

NZI	Neue Zeitschrift für das Recht der Insolvenz und Sanierung
OBLB	Oxford Business Law Blog (www.law.ox.ac.uk/oblb)
OECD	Organisation of Economic Cooperation and Development
OJ	Official Journal of the European Community
op. cit. (or: o.c)	opere citatio (the quoted/cited work)
p.	page
para.	Paragraph
RI	Rechtspraak Insolventierecht
RO	Rechtspraak Ondernemingsrecht
Riv. dir. int. priv. Proc	Rivista di diritto internazionale privato e processuale
TBH	Tijdschrift voor Belgisch Handelsrecht
TFEU	Treaty on the Functioning of the European Union
TOP	Tijdschrift Ondernemingsrechtpraktijk
TvI	Tijdschrift voor Insolventierecht
UK	United Kingdom
UNCITRAL	United Nations Committee on International Trade Law
UNCITRAL Model Law	UNCITRAL Model Law on Cross-Border Insolvency Proceedings
UNCITRAL Practice Guide	UNCITRAL Practice Guide on Cross-Border Insolvency Cooperation
U.S.C.	United States Code
ZEuP	Zeitschrift für Europäisches Privatrecht
ZGR	Zeitschrift für Unternehmens- und Gesellschaftrecht
ZIK	Zeitschrift für Insolvenzrecht und Kreditschutz
ZIP	Zeitschrift für Wirtschaftsrecht ZIP

LIST OF ABBRIVIATIONS OF OFTEN USED SOURCES

ABI Report (2014)	Report of the Commission to Study the Reform of Chapter 11 of the American Bankruptcy Institute
Commission's Recommendation (2014)	Commission Recommendation of 12.3.2014 on a new approach to business failure and insolvency, COM(2014) 1500 final
EU JudgeCo Principles (2015)	EU Cross-Border Insolvency Court-to-Court Cooperation Principles of 2015, which include also the EU JudgeCo Guidelines (2015)
EU JudgeCo Guidelines (2015)	EU Cross-Border Insolvency Court-to-Court Communications Guidelines (2015)
Proposal Restructuring Directive (2016)	Proposal for a Directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU, 22.11.106, COM(2016) 723
UNCITRAL Legislative Guide (2004)	UNCITRAL Legislative Guide on Insolvency Law of 2004 (with subsequent additions)
World Bank Principles (2016)	World Bank Principles and Guidelines for Effective Insolvency and Creditor Rights Systems (introduced in 2001, with subsequent additions)

BUSINESS RESCUE RECOMMENDATIONS

These recommendations are the result of a comparative and normative research, recorded in a report, which has been developed under the auspices of the European Law Institute's project 'Rescue of Business in Insolvency Law' (2014 – 2107), co-funded by the European Union and drafted by Professor Dr em Bob Wessels, University of Leiden, the Netherlands, and Professor Dr Stephan Madaus, Martin Luther University Halle-Wittenberg, Germany.

The addressees of these recommendations are the European Commission (and therefore the European Union (EU)), individual Member States and/or professionals (such as lawyers, accountants or turnaround advisors) active in the field of restructuring and insolvency. Often these addressees are obvious from the text of the recommendation itself, and in certain cases the Member States are addressed, however depending on the depth of harmonisation sought in the EU in matters of restructuring and insolvency, the EU itself is to be regarded the addressee.

Recommendations

Actors and procedural design

Recommendation 1.01: The EU as well as Member States should recognise that the success of any restructuring or insolvency system is very largely dependent upon those who administer it. Such a system can only function well when all stakeholders, including the general public, have confidence and respect in the courts and insolvency practitioners, and the way the roles of all parties involved are guaranteed and executed.

Recommendation 1.02: The EU as well as Member States should ensure that any restructuring and insolvency system includes transparent rules in the law for legal powers and duties, appointment, licensing, supervision, education and work standards and ethics for the key actors in that system. Such rules can be further elaborated in more depth and detail in European or national rules, including rules of practice. In setting professional and ethical standards, the EU and Member States should ensure that the relevant professional bodies are consulted and involved in the creation of such standards and that they take into account best practices for appropriately regulated professional parties as set out in principles and guidelines on regulation of the restructuring and insolvency profession, developed or adopted by European and international non-governmental organisations active in the area of restructuring and insolvency.

Recommendation 1.03: Member States should provide for specialised courts or chambers to handle restructuring and insolvency cases. In addition, Member States should introduce a further specialised subsection for hearing rescue and cross-border-cases which require a specific set of qualifications and experience that should be concentrated with specific judges specialised in these matters.

Recommendation 1.04: Member States and courts should recognise that the performance of restructuring and insolvency tasks by courts and its judges requires the continuous strengthening of judicial independence, and the appearance of such independence.

Recommendation 1.05: Member States should ensure the proper qualification of judges at such specialised courts when making appointment decisions. Member States should also ensure the further education of appointed judges by supporting further training and by setting mandatory minimum terms of judges within these courts to incentivise the acquisition of the requisite expertise and experience. They should also encourage and support judges to actively participate in national and international networks of insolvency judges.

Recommendation 1.06: The EU, Member States and courts should actively develop methods to effectively improve judges' performances by either

(i) concentration of courts with jurisdiction to decide in matters of restructuring and insolvency

(ii) selecting certain matters in which courts can be addressed to provide their view in certain matters of market uncertainties,

(iii) developing specific education beyond the boundaries of general legal competence,

(iv) developing and applying professional insolvency standards to assess performance,

or by a combination of these.

Recommendation 1.07: Member States should consider making more explicit provision for the involvement of mediators to resolve restructuring and insolvency disputes. Member States should recognise that the performance of a task in matters of restructuring and insolvency by a mediator could avoid unnecessary costs and could effectively assist parties in reaching a compromise on a restructuring plan, under the condition that a mediator acts independently.

Recommendation 1.08: In Member States where mediation is, or will soon be, an accepted form of dispute resolution in commercial cases, professional organisations should be encouraged to include mediators in restructuring and insolvency matters into a system of adherence to requisite standards of performance necessary for a fit and proper exercise of their task, where there is a dispute for which a mediator could usefully play a role and subject to controls designed to avoid unnecessary costs.

Recommendation 1.09: The European Commission or other European institutions should support a comparative and empirical study on the (desired) use of mediation in restructuring and insolvency matters.

Recommendation 1.10: Member States should assess whether a supervisor would bring additional value to their legal framework. If they conclude so, Member States should put in place legal and professional rules including rules on the independence and accountability of supervisors.

Recommendation 1.11: Member States should lay down explicitly in their laws that the professional performing restructuring and insolvency tasks is impartial, independent and competent. Being regulated as a lawyer or an accountant does in itself not sufficiently guarantee the standards of performance necessary for the proper exercise of the restructuring and insolvency tasks.

Recommendation 1.12: The European and national legislators should set professional and ethical standards for insolvency practitioners and ensure that the relevant professional bodies are consulted and involved in the creation of such standards and that they take into account best practices for appropriately regulated professional parties as set out in principles and guidelines on regulation of the restructuring and insolvency profession developed or adopted by European and international non-governmental organisations active in the area of restructuring and insolvency. Such standards should at least contain rules on licensing and registration, supervision and discipline, qualification and training, an appointment system, work standards during administration, legal powers and duties, remuneration, reporting and communication and ethical working standards (including rules on conflict of interests and a complaint procedure).

Recommendation 1.13: Member States should safeguard the independence and competence of insolvency practitioners by providing for a transparent and predictable process of appointment and resignation/removal as well as adequate means of supervision and an appropriate, timely remuneration in each individual case.

Recommendation 1.14: Member States should provide for a monitoring and reporting framework that includes a 're-capitalise or liquidate-rule' for companies and a duty to convene a shareholders' meeting upon loss of half of the subscribed share capital of the company.

Recommendation 1.15: During this meeting, the board has to present and discuss any proposed preventive restructuring measures, while the shareholders have a duty to decide to: (i) initiate workout negotiations, (ii) file for a restructuring procedure, (iii) to voluntarily wind up and liquidate the company, (iv) to file for insolvency liquidation.

Recommendation 1.16: Member States should introduce a 'safe harbour' defence to allow directors of a solvent company in financial distress to explore, with certain guidelines to be set, restructuring options without the risk of liability for insolvent (wrongful) trading.

Recommendation 1.17: Member States should provide for a duty for directors to timely inform shareholders and, where appropriate, other stakeholders (like e.g. suppliers or financial creditors) as soon as a business misses specific thresholds (e.g. a significant loss of capital or negative business earnings for a subsequent number of years or the moment the director foresees illiquidity). Any breach of such a duty should make the director liable against the company for damages. Member States should allow creditors and shareholder to initiate restructuring and insolvency proceedings based on such notice instead of a duty for company directors to file immediately.

Recommendation 1.18: The European Commission or other European institutions should support a comparative and empirical study on the duties and liability of directors of a failing company in the stage of a workout as well as in the position of a debtor in possession in proceedings.

Recommendation 1.19: Member States should ensure that the relevant professional bodies are involved in the creation of standards and guidelines that will apply to turnaround managers and that they take into account best practices for appropriately regulated professional parties as set out in principles and guidelines on regulation of the restructuring and insolvency profession developed or adopted by European and international non-governmental organisations active in the area of restructuring and insolvency, such as the INSOL Europe Turnaround Wing Guidelines (TW Guidelines).

Recommendation 1.20: The European Commission or other European institutions should support a comparative and empirical study on the role of a Chief Restructuring Officer (CRO) with the aim to formulate its specific (autonomous) powers, the way these relate to the other directors of the company as well as the CRO's accountability to all stakeholders involved and its liability for damages to third parties.

Recommendation 1.21: Member States should provide for and support early warning mechanisms that detect a deteriorating business development and signal the respective urgency to act. Possible instruments are accounting and monitoring duties for the debtor or the debtor's management according to company or tax law as well as reporting duties under loan agreements (covenants). In addition, third parties with relevant information (accountants, tax advisors, possibly also local "prevention groups" of senior businessmen) should be incentivised or even obliged under the law governing their duties to flag any relevant negative development of a debtor's business.

Recommendation 1.22: Soft law instruments like codes of conduct should be used to establish a culture of trust building workout negotiations amongst repeat players (like banks, suppliers, union representatives, insurers etc.). Such codes should follow the example of existing codes and provide for standstill agreements, confidentiality agreements, the way to organise and control a full disclosure (including the flow of information), and for rules how to conduct negotiations (including an option to involve third parties to act as supervisors or mediators). Member States should ensure that the relevant professional bodies are consulted and involved in the creation of such soft law instruments and that they take into account best practices as set out in principles and guidelines developed or adopted by European and international non-governmental organisations active in the area of restructuring and insolvency.

Recommendation 1.23: Member States should provide for the competence of a court to sanction a workout agreement against the veto of one or more (secured or unsecured) creditors who are not acting in good faith. Where a high percentage (75-80%) of equally affected creditors accept a workout solution, it should be assumed that a veto from a minority of dissenting creditor is held in bad faith unless good faith is proven to the court.

Recommendation 1.24: Such workout support proceedings should not be complemented by an option to apply for a collective stay. Instead, workout negotiations should be safeguarded by an option to apply for an individual stay against the creditor acting detrimental to the workout efforts.

Recommendation 1.25: Such workout support proceedings should only be available for the debtor. They should not require a specific access test referring to the situation of the debtor's business. Instead, the court would only require the debtor to submit a workout agreement with sufficient creditor support according to the stipulated majority requirements.

Recommendation 1.26: Any rescue-friendly restructuring and insolvency framework grounds on an efficient liquidation procedure that allows for the sale of the debtor's business as a going-concern free and clear of old debt. The instrument of an insolvency plan should be available to allow for a more flexible liquidation of the estate (e.g. through a liquidation or transfer plan or a composition with the debtor).

Recommendation 1.27: Member States should safeguard the interim continuation of the debtor's business until a decision about whether to sell or to reorganise or to close down is made. It should also provide for interim financing protection.

Recommendation 1.28: An efficient liquidation procedure should be accompanied by a debtor-friendly and predictable reorganisation procedure that is clearly distinct in the public eye from conventional insolvency (liquidation) proceedings.

Recommendation 1.29: In case of a competition between a liquidation (sale) and a restructuring, a restructuring attempt should prevail.

Recommendation 1.30: The combination of a pre-insolvency workout support procedure with a strong restructuring procedure for a (near) insolvent debtor constitutes a sufficient procedural framework for a business rescue, especially when pre-packaged sales and insolvency plans are additional available options in formal insolvency proceedings.

Recommendation 1.31: The grounds to open formal proceedings should be harmonised reflecting the rather similar standard already existing across Member States. Liquidation proceedings should be opened where the debtor is not able to pay its dues as they fall due for a certain period of time (the cessation of payment being a clear indicator). The right to file should be assigned to the debtor and all creditors. Restructuring proceedings should be opened if the debtor files and proves that he is insolvent or insolvency is imminent.

Recommendation 1.32: Member States should define clear and short periods for the debtor to reach milestones in procedures that make a stay or moratorium available for the debtor before creditors have voted to support the plan.

Recommendation 1.33: Member States should authorise courts to convert restructuring proceedings into insolvency proceedings (with a liquidation bias) only if the (imminent) insolvency of the debtor has already been established.

Recommendation 1.34: Member States should provide for common insolvency proceedings that allow for a quick and efficient piecemeal liquidation, but also a quick going-concern sale of the debtor's business or a different type of solution, even a restructuring, based on an insolvency plan adopted by the creditors and confirmed by the court.

Financing a rescue

Recommendation 2.01: Member States should ensure that the administrator of the estate (insolvency practitioner or debtor in possession) has the right to take out interim finance based on its own discretion to the extend it is obtained in order to continue a business as usual and, by doing so, to preserve the going concern value of the debtor's estate. The performance of this right should be disciplined by a personal liability in case of the later incapacity of the estate to repay. Only where such a borrowing decision would result in a significant administrative expense, a court or, preferably, a creditors' committee approval should be mandatory.

Recommendation 2.02: Member States should provide that any priority for new (plan implementation) finance repayment claims in a subsequent insolvency requires a specific clause in the restructuring plan and consequently require the approval of creditors and the court. In case of a workout, priority for new finance should also require a clause in the agreement and additional court approval of the financial part of the arrangement.

Recommendation 2.03: Member States should provide for a statutory safe harbour for interim and new finance from lenders liability or claw back claims in case of a subsequent (formal) insolvency.

Recommendation 2.04: Providing security for the lenders of interim or new financing should follow the general rules of civil law rules.

Recommendation 2.05: In a workout, all relevant creditors should be prepared to co-operate with each other to give sufficient (though limited) time (a "Standstill Period") to the debtor for information about the debtor to be obtained and evaluated and for proposals for resolving the debtor's financial difficulties to be formulated and assessed, unless such a course is inappropriate in a particular case. Member States should adopt or endorse principles and guidelines developed by international or European non-governmental organisations active in the area of restructuring and insolvency such as the INSOL International Workout Principles II.

Recommendation 2.06: In a workout support procedure, a stay should neither be automatic nor collective. Instead, a standstill agreement should protect the interest of all relevant stakeholders.

Recommendation 2.07: For safeguarding a workout, the debtor should be able to request a stay against a specific creditor whose actions have the capacity of frustrating all restructuring efforts. The duration and content of such an individual stay should be set by the court after hearing both sides. Any such stay is the result of a court's assessment of the application, laid down in a judicial order which is made to measure towards the individual circumstances as presented to the court and geared to the interests of all parties involved.

Recommendation 2.08: In formal restructuring or insolvency proceedings, a collective stay should be an automatic effect of the commencement of proceedings or available on request. Member States should provide for a stay to last as long as proceedings last, but should limit the duration of restructuring proceedings to avoid costly delay. A first, but extendable period of three month seems reasonable.

Recommendation 2.09: Any affected creditor may request to have the stay lifted with respect to its claims or interest and the court must decide, taking into account the interests of all parties involved.

Recommendation 2.10: Any judicial order regarding a stay may contain requirements or other conditions which support a speedy, inexpensive, negotiated adjustment of a debtor's debts, including conditions that affected creditors will be adequately protected during the period of the stay, such as a compensation for use of assets.

Executory contracts

Recommendation 3.01: Member States should follow the principle that the commencement of proceedings does not affect executory contracts of the debtor. Rights from such contracts should be subject to a stay and the administrator of the debtor's estate (insolvency practitioner or debtor in possession) should be allowed to decide on the continuation or rejection of any executory contract provided that the legitimate interests of the counterparty are respected. Exemptions for specific types of executory contracts should be limited, well considered and clearly defined.

Recommendation 3.02: Member States should limit the right to decide about the continuation or rejection of any executory contract to formal restructuring or insolvency proceedings. The tool should not be available in a workout or a workout support procedure.

Recommendation 3.03: Member States should consider specific legislation for executory contracts that are essential for continuing the business of the debtor like, for instance, real estate lease, energy supply, intellectual property and domain services, or license agreements. When doing so, Member States should take into account internationally accepted soft law rules.

Recommendation 3.04: Member States should provide that contractual acceleration or termination clauses in executory contracts themselves remain unimpaired and valid. However, acts of enforcement or execution of such clauses should have a no effect in case of a stay of enforcement actions under respective restructuring and insolvency law.

Recommendation 3.05: Member States should ensure the right to lift the stay as soon as efforts to continue the business fail and a (piecemeal) liquidation is inevitable.

Recommendation 3.06: Member States should introduce rules that allow for assigning all executory contracts that are still valid to the purchaser of the debtor's business in a going-concern asset deal. Such rules should include the right of the counterparty of the assigned contracts to file an objection to the court claiming to be worse off with the new contract party in comparison to the debtor.

Ranking of creditors

Recommendation 4.01: Member States should, in principle, respect pre-insolvency entitlements under their insolvency and restructuring law regimes unless there are legitimate grounds to a post-commencement preference.

Recommendation 4.02: Member States should ensure that classes of creditors are specified in clear terms, in particular identifying those creditors enjoying the right to be satisfied in a specified priority.

Recommendation 4.03: Member States should ensure the very commencement of orderly and efficient restructuring and insolvency proceedings by securing the payment of fees for the courts and insolvency office holders involved. While no assets cases should be financed by public funds, secured creditors should contribute to cover costs in other cases by introducing a clear and predictable deduction rule, e.g. a general deduction up to 10 per cent.

Recommendation 4.04: Member States should refrain from granting additional general preferences for specific groups of creditors in favour of other means of protection of social interests (e.g. insurance or guarantee schemes, statutory liens on specific assets). The actual need for protection should be scrutinised thoroughly, in particular the protection of fiscal interests, and be primarily determined by their general impact on rescue efforts.

Recommendation 4.05: Member States should ensure that their insolvency and restructuring framework comprises sufficient means to restructure secured credit as well as unsecured credit, meaning that restructuring plans should be able to include and to modify the entitlements of secured creditors.

Organisation of creditors

Recommendation 4.06: Member States should ensure that in workout-support proceedings a general meeting of creditors is not required and the establishment of creditors' committees is only an option in order to structure complex workout negotiations.

Recommendation 4.07: Member States should provide for a general meeting of creditors in formal restructuring or insolvency proceedings. Member States should allow for virtual meetings or online participation (including online voting).

Recommendation 4.08: Member States should secure the involvement of a creditors' committee in formal restructuring or insolvency proceedings provided that there are sufficient assets in the estate to justify the additional costs. Such a creditors' committee should not only have a supervisory function, but also be competent to approve decisions in the administration of the estate that may have a significant effect in the later distribution (except the decision about a restructuring or insolvency plan which is governed by separate rules).

Labour, benefit and pension issues

Recommendation 5.01: Member States ensure that employees and workers' councils receive timely notice about an imminent restructuring or insolvency.

Recommendation 5.02: Employment contracts should not end automatically upon the commencement of (pre-)insolvency proceedings. Member States should ensure that such contracts enjoy full labour law protection outside of formal insolvency proceedings while being treated under the applicable rules for executory contracts in insolvency proceedings.

Recommendation 5.03: Member States provide for a default continuation rule combined with the right of the insolvency practitioner or the debtor in possession to terminate employment contracts within a short period.

Recommendation 5.04: Labour law protection, including special protection for pregnant or ill employees, should only be applicable outside of formal insolvency proceedings. In formal restructuring proceedings, any redundancies should be required to follow from the necessities of the rescue strategy pursued by the restructuring plan. The plan should, in principle, provide for severance payments.

Recommendation 5.05: Employees whose employment contract was terminated in the course of formal insolvency proceedings, should be free to conclude a new contract with any employer available. Neither contractual non-competition clauses nor statutory non-competition rules should apply unless the employee receives adequate protection or compensation.

Recommendation 5.06: Member States should provide that, whenever a specific number of employees in an establishment are likely to be affected by a restructuring plan or a liquidation (including a business transfer), a representative should have a right to represent and to protect their interest by participating in formal restructuring and liquidation proceedings (e.g. in a creditors' committee).

Recommendation 5.07: The protection of unpaid salary claims can be achieved by treating them as preferred claims or even administrative expenses in a formal procedure. Where a cost-efficient guarantee institution exists, Member States should ensure rely on it and ensure that it covers as much unpaid salary as possible and allows for a timely payment to employees.

Recommendation 5.08: The European Commission is invited to conduct an overall comparative study on the laws relating to the treatment and protection of pension-related contribution and claims in case of an (imminent) insolvency of the contributing employer that includes all relevant aspects of EU rules as well as substantive national pension, labour, and insolvency law.

Recommendation 5.09: Member States should ensure that individual or occupational pension schemes are to be restricted to indirect pension schemes which either use (insolvency-remote) third parties or are protected by a guarantee scheme. The restructuring of pension entitlements from a direct pension scheme should only be possible where a guarantee protection scheme is in place.

Avoidance actions in out-of-court workouts and pre-insolvency procedures and possible safe harbours

Recommendation 6.01: In workout support proceedings, there should be no room for applying avoidance powers.

Recommendation 6.02: Member States should allow safe harbours for transactions made in the ordinary course of a debtor's business when concluded with the debtor during a formal restructuring or insolvency proceedings, including interim proceedings.

Recommendation 6.03: Member States should allow safe harbour for transactions made outside the ordinary course, such as new finance or new security rights for new finance lenders, only under the condition that these transactions are part of a restructuring plan which was approved by creditors and confirmed by a court.

Recommendation 6.04: Member States should ensure that a safe harbour rule is not available for transactions done in bad faith that disadvantage creditors in a subsequent insolvency. Member States should always allow for the recovery of fraudulent transfers (transactions in bad faith), even if there were based on a (now failing) plan.

Recommendation 6.05: When considering whether bad faith can be established for transactions in the ordinary course of business, account should be given to all circumstances of the case, including (i) the fact whether the debtor has demonstrated an early engagement with creditors, employees, shareholders and other stakeholders in reaching a solution to its financial troubles, (ii) has taken every reasonable step to properly and diligently try to avoid destruction of value, and (iii) has sought advice from a person that might objectively be considered to have has suitable business or industry experience and expertise and (iv) that the debtor conscientiously acted on the advice received.

Recommendation 6.06: Any safe harbour rule should be clearly defined so that parties can assess them in a predictable way when dealing with the debtor as well as during the negotiations and conclusion of a restructuring plan.

Recommendation 6.07: When bringing forward an avoidance action, the burden of proof should always be on the party that alleges that a wrong has occurred. Such a party is either the insolvency practitioner (or supervisor) appointed or a public institution such as a fraud office or public prosecutor.

Sales on a going-concern basis

Recommendation 7.01: Member States should ensure that every restructuring and insolvency framework is grounded on an efficient liquidation process that comprises both the options to sell the debtor's business (or parts of it) as a going or to sell individual assets (piecemeal liquidation) – depending on the best return for creditors.

Recommendation 7.02: Member States should ensure that their restructuring and insolvency framework includes the option for an accelerated liquidation, in particular when the debtor or a party in interest demonstrates by clear and convincing evidence that there is a high likelihood that the value of the debtor's assets will decrease significantly within 30 days ('melting ice cube' situation).

Recommendation 7.03: Member States should make a prepack sale available in their restructuring and insolvency framework. Rules should include the involvement of an independent insolvency practitioner, appropriately regulated, to supervise the sales process and safeguard minimum transparency. In addition, creditor approval for such a sale should be mandatory and given through their representative, usually the creditors' committee.

Recommendation 7.04: Member States should, preferably in consultation with associations of practitioners, set standards and practice rules in relation to the transparency of the negotiation process before the opening of formal proceedings, the information to and degree of involvement of all creditors, the identity and background of the buyer, the professional standard of the actors involved, and, if deemed necessary, the valuation of the assets included in the sales.

Recommendation 7.05: Member States should evaluate rules governing a prepack sale, including standards and practice rules, on a regular basis to ensure the integrity of the process.

Rescue plan issues: procedure and structure; distributional issues

Recommendation 8.01: Member States should ensure that in cases where the rescue of a business requires more than just a sale of the business, a restructuring plan is available that is binding on all parties of a restructuring if it receives sufficient actual support of affected stakeholders, and if a court confirms (ex officio or upon request) that the plan complies with all legal requirements.

Recommendation 8.02: Member States should grant the right to present a plan exclusively to the debtor, at least for an initial period of time long enough to negotiate and modify the proposed plan, and have a vote. An accepted debtor plan should be confirmed notwithstanding a competing plan.

Recommendation 8.03: Member States should require the plan proponent to disclose all information relevant for an informed decision about the proposed plan. Such a full disclosure should be easily accessible (electronically) and be accompanied by an executive summary.

Recommendation 8.04: Member States should allow a plan to contain all measures required to rescue the business. They should also require a plan to describe and explain these measures. The range of tools should include the impairment of security rights and shareholder rights. With respect to preferential claims, Member States should recognize that only a preferential treatment of stakeholders that are essential to keep the business alive should not be affected by a plan.

Recommendation 8.05: Member States should reflect the diversity of creditors and shareholders which can be affected by a plan by mandating a classification. They should prompt the court to scrutinise the non-discriminatory classification in a proposed plan.

Recommendation 8.06: All creditors and shareholders whose rights are impaired by the plan should be allowed to vote. The weight of their vote should reflect the value of their claim or right in a class. Disputes with regard to their claim, right or voting right should be solved immediately and finally by the disputing parties and, eventually, by the court without prejudice for a later proof of claims for distribution rights.

Recommendation 8.07: Pending further requirements under local constitutional law on fundamental rights, Member States should allow a cross-class cramdown against a class of creditors and shareholders. In case of a shareholder class, such a cramdown should only be available if affected shareholders took an interest in the firm in terms of a financial investment.

Recommendation 8.08: Member States should bind the court to confirm a plan unless it does not comply with specific legal requirements regarding content, acceptance and fairness of the plan.

Recommendation 8.09: The court should not be asked to make business decisions. It should only hear objections of creditors or shareholders who actually voted against the plan. Objections based on the valuation of the business should only be heard if the objecting party presents expert testimony showing that it would evidently do better in an alternative liquidation.

Recommendation 8.10: Member States should provide that a confirmed plan is binding on all parties. Any appeal against the confirmation order should, in principle, not stay the implementation of the confirmed plan.

Recommendation 8.11: Member States should allow any plan to provide for a supervision of the implementation of all plan provisions.

Recommendation 8.12: Member States should ensure that only a significant failure of the debtor to perform invalidate the plan and its effects. Here, the debtor may prevent such a harmful event by filing a modified plan which then must be accepted by affected creditors and confirmed by the court again.

Recommendation 8.13: Member States should ensure that a debt relief under the restructuring plan is not considered taxable income.

Corporate group issues

Recommendation 9.01: Members States individually and the European legislators, when reviewing the Insolvency Regulation (Recast), should provide for a specific framework to address insolvency in the context of group of companies, meaning a parent undertaking and all its subsidiary undertaking in the meaning of the definitions in the Insolvency Regulation (Recast), that contains the following elements.

Recommendation 9.02: Members States should ensure that a court, having to decide on a request for opening of insolvency proceedings with regard to a member of a corporate group, should verify whether a coordinated strategy is being considered for some or all of the members of the group.

Recommendation 9.03: The European and national legislators ensure that insolvency practitioners and courts are guided by the principles and guidelines set out in the Communication and Cooperation Guidelines for Cross-Border Insolvency Guidelines of 2007 ('CoCo Guidelines'), the EU Cross-Border Insolvency Court-to-Court Cooperation Principles of 2015 ('EU JudgeCo Principles'), which include EU Cross-Border Insolvency Court-to-Court Communications Guidelines ('EU JudgeCo Guidelines'). Communication and cooperation may take any form, including the conclusion of protocols. Such a protocol should include clauses regarding notices, the right of insolvency practitioners, creditors or other stakeholders to appear, access to data and information among insolvency practitioners, communication among committees, asset preservation, claim including specific rules for intercompany claims, submission of a restructuring plan of a liquidation plan, amendment of the protocol and the incorporation of the CoCo Guidelines, the EU JudgeCo Principles and EU JudgeCo Guidelines by reference and form part of this protocol in whatever form they are formally adopted by each court, in whole or in part and with or without modifications, if any, with the addition of a clause providing that where there is any discrepancy between the protocol and these principles and guidelines the protocol shall prevail.

Recommendation 9.04: The European and national legislators should mandate courts and insolvency practitioners to communicate and cooperate in international cases that do not fall under the application of the Insolvency Regulation (Recast) providing rules analogous to the CoCo Guidelines, the EU JudgeCo Principles and EU JudgeCo Guidelines. The fact the Insolvency Regulation (Recast) does not apply should not preclude insolvency practitioners and courts in relevant third country jurisdiction from communicating and cooperating with their respective counterparts to the extent that such communication or cooperation is compatible with the national laws of any such third country jurisdiction.

Recommendation 9.05: Member States should enable their courts to jointly open insolvency proceedings for several companies belonging to the same group if the court finds that the center of main interests (COMI) of those companies is located in their Member State.

Recommendation 9.06: The European and national legislators should ensure that group coordination proceedings under the Insolvency Regulation (recast) become more efficient.

Recommendation 9.07: The European and national legislators should provide that the court located in the COMI ('COMI court') of a member participating in group coordination proceedings may authorise the insolvency practitioner appointed to seek: (i) participation and to be heard in a coordinating proceeding taking place in another jurisdiction, (ii) recognition by the coordinating court of the proceeding in the COMI jurisdiction, whilst (iii) the coordinating court can receive such a request for recognition.

Recommendation 9.08: The European and national legislators should ensure that, while participation in group coordination proceedings is voluntary in principle, the decision not to participate is required to exclude a member from the effects of such proceedings (opt-out). In addition, the COMI court should be allowed to opt-out of its group member whenever the decision to opt out is not adopted in good faith. Where a high percentage (minimum of 80%) of equally affected members participate in group coordination proceedings, the COMI court should assume that an opt-out was decided in bad faith unless good faith is proven to the court.

Recommendation 9.09: Solvent members of a group should be allowed to formally participate in group coordination proceedings without such participation implying a submission to the jurisdiction of a court or to the applicability of its insolvency laws.

Recommendation 9.10: The European and national legislators should ensure that group coordination proceedings can result in a group restructuring or insolvency plan that is binding for all participating members. Creditors and stakeholders of participating group members would be placed in separate classes and vote under the rules according to the applicable national law in their own jurisdiction. Following the vote of the group restructuring or insolvency plan by relevant creditors and stakeholders, each COMI court would confirm the plan if it holds that the plan was accepted according to national law including all its cramdown options. A cross jurisdictional (cross entity) cramdown would not be possible.

Recommendation 9.11: The European and national legislators should ensure that the insolvency practitioner appointed in the group coordination proceedings (coordinator) should have the right of access to proceedings in each COMI court to be heard on issues related to implementation of the group restructuring plan.

Recommendation 9.12: The European and national legislators should ensure that a court may approve the substantive consolidation of the estates of jointly administered members of the group (see Recommendation 9.05), of parts of these estates, where (i) the assets and liabilities of all of the respective members have been commingled in a sense that they cannot easily be untangled without severe effort, delays and costs, or (ii) the group structure has been used to deceive creditors. They should also allow a group restructuring or insolvency plan to provide for such a form of consolidation in cross-border cases.

Special arrangements for small and medium-sized enterprises (SMEs) including natural persons (but not consumers)

Recommendation 10.01: Member States should define the scope of special provisions for small business restructuring and insolvency cases with a focus on micro and small businesses. Member States should not include medium-sized businesses as they usually not require a special treatment.

Recommendation 10.02: Member States should ensure that (near) insolvent micro and small businesses have access to orderly proceedings, regardless of available assets to cover the costs of proceedings.

Recommendation 10.03: Member States should allow for the payment of procedural costs (court, insolvency practitioner) to be deferred in order to allow for the thorough investigation and efficient enforcement of claims from fraudulent transfers and avoidance actions as well as of director liability claims.

Recommendation 10.04: Member States should consider financing procedural costs of restructuring and insolvency proceedings of no-asset cases by public funds, and further incentivising third party funding of restructuring and insolvency proceedings (e.g. by a first priority repayment of these funds and/or a tax deductibility).

Recommendation 10.5: Member States should lower the complexity and duration of small business cases in order to limit costs, but also to facilitate the access to procedures for average skilled sole entrepreneurs.

Recommendation 10.06: Member States should reflect the rational creditor passivity in the rules on the decision about the restructuring plan, a sale of the business, or a piecemeal liquidation by a deemed approval rule. To ensure speed and efficiency of proceedings, non-participating creditors should also not be able to delay proceedings at a later stage by appealing to (higher) courts.

Recommendation 10.07: Member States should ensure that facilitated procedures for micro and small businesses are not abused to disenfranchise creditors. The honesty of a debtor should, however, not be tested on the first day of proceedings based on extensive filing requirements, but instead be scrutinised during the cause of proceedings by investigations of the court, an insolvency practitioner, informed public authorities (tax or social security agencies) and creditors (financing bank; trade creditor). In case of a proven dishonesty, the denial of a discharge for the entrepreneur should work as an efficient sanction.

Recommendation 10.08: Member States should consider to have proceedings for micro and small businesses administered outside the court system (by public authorities or secured creditors or other private entities) and only involve courts in handling objections and appeals – as far as their respective constitutional law allows for it.

Recommendation 10.09: Member States should limit the administrative burden of micro and small business cases by using mandatory templates and modern IT tools like interactive templates.

Recommendation 10.10: Member States should only provide for very short periods of a stay or a plan proposal in order to limit the incentive for abuse as well as the overall duration of proceedings.

Recommendation 10.11: Member States should provide for a secured path for failed entrepreneurs to be discharged from all business related debt by the end of insolvency proceedings if there is no objection raised based on any fraudulent behaviour.

GLOSSARY OF TERMS AND DESCRIPTIONS IN RESTRUCTURING AND INSOLVENCY

Many states and regional public institutions, international non-governmental organisations and practitioners' associations all over the world have produced many laws, regulations, principles, guidelines and statements of best practices. All these forms of expressions aim for the better coordination of restructuring and insolvency measures or proceedings concerning economic enterprises which have operations, assets, activities, debtors or creditors in more than one state. In several instances these laws, regulations and principles provide for a list of definitions or terms, employed frequently within the legal context within which they function. This Appendix aims to further develop a European legal terminology, based on recent efforts to develop an uniform global legal terminology and therefore to assist legislators, insolvency practitioners and courts in their efforts of improving the components of their respective languages to facilitate and smoothen cross-border communication and coordination.[1] Legislators may find this appendix helpful in their efforts of creating or amending domestic rules relating to international insolvency or in efforts of approximation or harmonisation of domestic laws and regulations.

The methodology followed has been a general gathering of these terms and expressions from documents referred to in the footnotes which can contribute to a better understanding and knowledge of insolvency matters in a broader context. However, most terms in the Glossary have been adopted or proposed to be adopted by European institutions, especially those terms and definitions stemming from the European Commission's recommendation of March 2014 and its Proposal for a Restructuring Directive of November 2016, both related to pre-insolvency restructuring and second chance. It is underlined that terms presented as definitions in these text serve within the purpose of the respective text. The same is true for terms and expressions of the EU Insolvency Regulation (Recast; 2015). Where terms in the latter regulation do not refer the Member States' domestic laws, it is generally accepted that most of these terms or words have "… an autonomous meaning and must therefore be interpreted in a uniform way, independently of national legislation".[2] Such a form of interpretation, however, does not exclude the use of its given meaning for its original purposes while looking for a specific meaning or interpretation in another context.

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"Absolute priority rule"

The absolute priority rule (APR) has been developed in US bankruptcy law to address a common practice in early 1900's Equity Receiverships that featured going-concern asset sales to new corporations held by insiders of the old corporation in order to effectively

[1] This document finds its basis in an Appendix, published in the Global Principles for Cooperation in International Cases ('Global Principles'), drafted by Ian F. Fletcher and Bob Wessels, which were published in June 2012 by the American Law Institute (ALI) and International Insolvency Institute (III). See for the full text http://www.iiiglobal.org/component/jdownloads/finish/557/5932.htm. Additions to this Glossary have been added by the Reporters in cooperation with the TRI Leiden Research Team (www.tri-leiden.eu).

[2] See C-341/04 *Eurofood IFSC Ltd v Bank of America N.A* EU:C:2006:281 at 31 with regard to the term "centre of main interest".

freeze out entire classes of creditors when junior claimants, like shareholders, survived.[3] The rule held that the court could deny approval of such a sale where the distribution of value by such a sale violated the priority that would apply in a liquidation. The rule was held to be impractical and, thus, only has a limited scope in current US law. US Bankruptcy Code s. 1129 (b) only mandates the application of the rule when a court is asked to confirm a plan over the dissent of a class of creditors or shareholders (see "cross-class cramdown"). The rule provides that (a) a dissenting class of creditors can insist on being satisfied in full before a more junior class may receive any distribution or keep any interest under a restructuring plan, and (b) a dissenting class of creditors or shareholders can insist on being treated at least as well as those in another class that enjoys the same priority outside of bankruptcy.[4]

"Abusive filings"

The term "abusive filings" is used within the context of the ALI NAFTA Principles (2003) where it is introduced as a Procedural Principle.[5] Although it is not specifically defined, this legal instrument regulates that "when a non-main proceeding is filed in a NAFTA country and the court in that country determines that this country has little interest in its outcome as compared to the country that is the centre of the debtor's main interest, the court should (i) dismiss the bankruptcy case, if dismissal is permitted under its law and no legitimate interests would be damaged by dismissal; or (ii) ensure that the bankruptcy stay arising from the non-main proceedings had no effect outside that country."[6]

"Actio pauliana"

The "actio pauliana" was an avoidance action under Roman law which provided for the avoidance of transfers of property that are made to defeat or delay the claims of creditors or to put the property beyond the reach of creditors.[7] (See "Avoidance provisions")

"Administrative claim or expense"

An administrative claim or expense includes costs and expenses of the proceedings, such as remuneration of the insolvency representative and any professionals employed by the insolvency representative for the purposes of the administration, expenses for the continued operation of the debtor, debts arising from the exercise of the insolvency representative's functions and powers, costs arising from continuing contractual and legal obligations and

[3] See Stephen J. Lubben, 'The Overstated Absolute Priority Rule' 21 Fordham Journal of Corporate & Financial Law 2016, p. 581.
[4] See e.g. B E Adler, D G Baird and T H Jackson, *Bankruptcy* (4th edn, Foundation Press New York, 2007), 675. The APR definition in Article 2(10) of the proposed Restructuring Directive (2016) is insufficient as it does not contain the second standards of the rule.
[5] See American Law Institute, *Transnational Insolvency: Cooperation Among the NAFTA Countries: Principles of Cooperation Among the NAFTA Countries* (2003) (hereafter "ALI NAFTA Principles (2003)").
[6] ALI NAFTA Principles (2003), Procedural Principle 6.
[7] See also G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 448.

costs of proceedings.[8] This type of claims is sometimes alternatively referred to as: "Claim of the estate".

"Administrator"

The "administrator" of the estate is the person in control and in charge of the debtor's estate during restructuring or insolvency proceedings (see also "insolvency representative"). This person can be an insolvency practitioner unless the debtor remains in possession. (See "insolvency practitioner", "debtor in possession", but also "office holder", "liquidator" or "supervisor").

"Adopted"

A restructuring plan that has been approved by a vote of the requisite majority (in each class) of the affected creditors (and shareholders).[9]

"Affected party"

In its plural form, affected parties means creditors or classes of creditors and, where applicable under national law, equity holders whose claims or interests are affected under a restructuring plan.[10] Sometimes the term 'affected creditor' is used, being a creditor or the creditors collectively (including secured creditors) whose rights, obligations or interests are influenced by a (proposed) restructuring plan.[11]

"Applicable"

The term "applicable" has a broad meaning within the scope of insolvency issues. However, it may be considered that its most significant meaning is in relation to the applicable law.

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[8] UNCITRAL, *UNCITRAL Legislative Guide on Insolvency Law* (2004), para. 12, under B "Glossary, Terms and definitions" (hereafter "UNCITRAL Legislative Guide (2004)"). UNCITRAL uses terms and expressions in the UNCITRAL Legislative Guide (2004) and its addition the UNCITRAL Legislative Guide, Part Three: Treatment of enterprise groups in insolvency (2010) (hereafter "UNCITRAL Legislative Guide (2010)"), the UNCITRAL Practice Guide on Cross-Border Insolvency Cooperation (2009) (hereafter "UNCITRAL Practice Guide (2009)") and the UNCITRAL Judicial Perspective (2011) in a consistent way. Although several of these terms appear in all documents mentioned, they will not be mentioned in all cases in the following footnotes.

[9] See International Working Group on European Insolvency Law, *Principles of European Insolvency Law* (2003), Principle § 11.3 (hereafter "Principles of European Insolvency Law (2003)"); Commission Recommendation of 12.3.2014 on a New approach to business failure and insolvency, COM(2014) 1500 final, Recommendations 16 and 20 (hereafter "Commission's Recommendations (2014)"); Proposal for a Directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU, 22.11.106, COM(2016) 723, Article 9 (hereafter "Proposal Restructuring Directive (2016)").

[10] See Proposal Restructuring Directive (2016), Article 2(3).

[11] See also INSOL International, Statement of Principles for a Global Approach to Multi-Creditor Workouts II (2017), Third Principle (hereafter "INSOL International Workout Principles II (2017)").

The European Insolvency Regulation (2015) provides in Article 7 that the law applicable to insolvency proceedings and their effects shall be that of the Member State within the territory of which such proceedings are opened. Articles 8-18 European Insolvency Regulation (2015) provide for exceptions and limitations to this rule.

"Assets"

The term "assets" is referred to in several legal instruments in relation to the debtor's assets. The UNCITRAL Legislative Guide describes "assets of the debtor" as: property, rights and interests of the debtor, including rights and interests in property, whether or not in the possession of the debtor, tangible or intangible, movable or immovable, including the debtor's interests in encumbered assets or in third party-owned assets.[12] The European Insolvency Regulation (2015) provides that this "Regulation enables the main insolvency proceedings to be opened in the Member State where the debtor has the centre of its main interests. Those proceedings have universal scope and are aimed at encompassing all the debtor's assets".[13] Moreover, the European Communication & Cooperation Guidelines for Cross-border Insolvency (2007) provide that "In particular, these Guidelines aim to promote: The identification, preservation and maximisation of the value of the debtor's assets (which includes the debtor's undertaking or business) on a world-wide basis;"[14]

In addition, the Principles of European Insolvency Law (2003) determine as their first principle that "In an insolvency proceeding the assets of an insolvent debtor are collected and converted into money to be distributed among the creditors ('liquidation'), or the liabilities of an insolvent debtor are restructured in order to re-establish the debtor's ability to meet liabilities ('reorganisation'). The proceeding can be a combination of liquidation and reorganization".[15]

In the context of the Draft Common Frame of Reference (DCFR, 2009), the Study Group on a European Civil Code and the Research Group on EC Private Law (*Acquis* Group) have defined the term "assets" as "anything of economic value, including property; rights having a monetary value; and goodwill".[16]

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[12] UNCITRAL Legislative Guide (2004), para. 12, under B "Glossary, Terms and definitions". Similar: UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".

[13] Regulation (EU) 2015/848 of the European Parliament and the Council of 20 May 2015 on insolvency proceedings (recast), see O.J. L 141/19 of 5 June 2015 (hereafter "EIR (2015") or "European Insolvency Regulation (2015)"), Recital 23.

[14] European Communication and Cooperation Guidelines for Cross-Border Insolvency (2007), Guideline 2.2.ii (hereafter "CoCo Guidelines (2007)").

[15] Principles of European Insolvency Law (2003), Principle 1.1.

[16] Study Group on a European Civil Code and Research Group on EC Private Law (Acquis Group), *Principles Definitions and Model Rules of European Private Law* (European Law Publishers, 2009), Annex (Definitions), p. 546. The Reporters used the Outline Edition (hereafter "DCFR Outline Edition (2009)"). The Full Edition (6500 pages; six Volumes) was published late 2009, see Christian von Bar and Eric Clive (eds.), *Principles, Definitions and Model Rules of European Private Law. Draft Common Frame of Reference (DCFR)* (Full Edition, München/Oxford: Sellier. European Law Publishers/Oxford University Press 2009/2010). Presented as a blueprint for future European law of obligations and property law, the DCFR is heavily debated, see e.g. H. Eidenmüller, F. Faust, H.C. Grigoleit, N. Jansen & G. Wagner, R. Zimmerman, 'The Common Frame of Reference

"Attached right"

An attached right is a quasi-property law right, not vested in an asset, but attached to it. See also "vested right".

"Avoidance provisions"

"Avoidance provisions" are described in various ways: (i) Provisions of the insolvency law that permit transactions for the transfer of assets or the undertaking of obligations, including the granting of security interests, prior to insolvency proceedings to be cancelled or otherwise rendered ineffective and any assets transferred, or their value, to be recovered in the collective interest of creditors.[17] (ii) More generally, the scope of this expression is not necessarily limited to provisions contained within "the insolvency law", but may extend to provisions within the general law of the system concerned. This wider mode of reference is employed by the terms of Article 16 of the European Insolvency Regulation (2015). Likewise in the context of the Draft Common Frame of Reference (DCFR), the Study group on a European Civil Code and the *Acquis* Group provides: "Avoidance" of a juridical act or legal relationship is the process whereby a party or, as the case may be, a court invokes a ground of invalidity so as to make the act or relationship, which has been valid until that point, retrospectively ineffective from the beginning.[18]

"Balance sheet insolvency or balance sheet test"

A company debtor is insolvent whenever the value of the liabilities of a company or a person exceeds the value of their assets.[19]

"Best interest of creditors test"

The "best interest of creditors test" derives from US bankruptcy law. According to s. 5103 A of the Act of June 22, 1874 a composition agreement could only be confirmed over a minority of dissenting creditors if the court held that this was "for the best interest of all concerned".[20] In substance, the test requires that no dissenting creditor is worse off under the restructuring plan than in an alternative liquidation, whether piecemeal or sale as a going concern.[21]

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for European Private Law. Policy Choices and Codification Problems' Oxford Journal of Legal Studies 2008, p. 659-708.

[17] UNCITRAL Legislative Guide (2004), para. 12 under B "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".

[18] DCFR Outline Edition (2009), Annex (Definitions), p. 546.

[19] G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017) p. 448.

[20] See Jonathan Hicks, 'Foxes Guarding the Henhouse: The Modern Best Interests of Creditors Test in Chapter 11 Reorganizations', 5 Nev. L.J. 2005, p. 820.

[21] The test was also adopted by the Proposal Restructuring Directive (2016), see Article 2(9).

"Burdensome assets"

"Burdensome assets" are assets that may have no value or an insignificant value to the insolvency estate or that are burdened in such a way that retention would require expenditure that would exceed the proceeds of realization of the asset or give rise to an onerous obligation or a liability to pay money.[22] Such assets are also sometimes termed "onerous property" for the purpose of disclaimer by the administrator of the insolvency proceeding.

"Business"

The term business means any natural or legal person, irrespective of whether publicly or privately owned, who is acting for purposes relating to that person's self-employed trade, work or profession, even if the person does not intend to make a profit in the course of the activity.[23]

"Carve-out"

A proportion of recoveries under a security interest set aside for the benefit of parties other than the secured creditor.[24]

"Cash flow insolvency or cash flow test"

A company or a person is insolvent when there are unable to pay their debts as they fall due.[25]

"Cash proceeds"

"Cash proceeds" are proceeds of the sale of encumbered assets to the extent that the proceeds are subject to a security interest.[26]

"Centre of main interests"

In the European Insolvency Regulation (2015) the term "centre of main interests" is employed to demarcate the territorial applicability of the Regulation's provisions (Recital 25) and as the criterion for jurisdiction in the main proceedings (Article 3(1)). Generally, the

[22] UNCITRAL Legislative Guide (2004), para.12, under B "Glossary, Terms and definitions".
[23] DCFR Outline Edition (2009), Annex (Definitions), p. 547.
[24] G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 448.
[25] G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 448.
[26] UNCITRAL Legislative Guide (2004), para. 12, under B "Glossary, Terms and definitions".

acronym COMI ("Centre of main interests") is used. In the case of a company or legal person, the European Insolvency Regulation (2015) provides that the place of the registered office shall be presumed to be the centre of its main interests in the absence of proof to the contrary. The EIR (2015) also declares that in general the term "centre of main interests" shall be the place where the debtor conducts the administration of its interests on a regular basis and which is ascertainable by third parties.[27]

The UNCITRAL Model Law utilises this criterion as well and contains the following presumption: "In the absence of proof to the contrary, the debtor's registered office, or habitual residence in the case of an individual, is presumed to be the centre of the debtor's main interests".[28]

"Claim"

The UNCITRAL Legislative Guide describes a "claim" as a right to payment from the estate of the debtor, whether arising from a debt, a contract or other type of legal obligation, whether liquidated or unliquidated, matured or unmatured, disputed or undisputed, secured or unsecured, fixed or contingent, arisen on or before the commencement of the insolvency proceedings.[29] It adds as a "note": "Note: Some jurisdictions recognize the ability or right, where permitted by applicable law, to recover assets from the debtor as a claim". The Draft Common Frame of Reference (DCFR) describes a "claim" as a demand for something based on the assertion of a right,[30] and "claimant" as a person who makes, or who has grounds for making, a claim.[31] A "claim" is held by a "creditor" (see "creditor").

"Claim of the estate"

See "Administrative claim or expense".

"Class"

The term "Class" is used to denominate a group of claims of creditors that have – under an applicable law – a similar legal position, specifically its position in the proceeds to be distributed from the insolvency estate. Although the class relates to the nature of the claim, it is used to nominate the claimants, too. Generally, the following classes can be distinguished: (i) super-priority creditors, (ii) priority creditors, (iii) pari passu ("unsecured" or "ordinary") creditors, (iv) subordinated creditors, (v) equity holders. Under applicable law,

[27] EIR (2015), Article 3(1), last line.
[28] UNCITRAL Model Law on Cross-Border Insolvency Law (1997), Article 16.3 (hereafter "UNCITRAL Model Law (1997)").
[29] UNCITRAL Legislative Guide (2004), para. 12, under B "Glossary, Terms and definitions." UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations". The Concordat uses the term "Common Claim" for "A claim which is neither a secured claim nor a privileged claim."
[30] DCFR Outline Edition (2009), Annex (Definitions), p. 547.
[31] DCFR Outline Edition (2009), Annex (Definitions), p. 547.

creditors or shareholders of the same class may often be put into different sub-classes if their claims show sufficient (legal or economic) differences.

"Class formation"

The expression "class formation" means the grouping of affected creditors and equity holders in a restructuring plan in such a way as to reflect the rights and seniority of the affected claims and interests, taking into account possible pre-existing entitlements, liens or inter-creditor agreements, and their treatment under this restructuring plan.[32]

"Clause"

"Clause" refers to a provision in a document. A clause, unlike a "term", is always in textual form.[33]

"Collective proceedings"

The expression "collective proceedings" means proceedings which include all of the debtor's creditors. The European Insolvency Regulation (2015) expanded the term to include proceedings that only involve a significant part of a debtor's creditors, provided that the proceedings do not affect the claims of creditors which are not involved in them.[34]

"Commencement of proceedings"

"Commencement of (insolvency) proceedings" is the effective date of insolvency proceedings whether established by statute or a judicial decision.[35] See also "Opening of proceedings" and "Time of the opening of proceedings".

"Communication"

Contact between courts, or between insolvency administrators, or between courts and insolvency administrators, for purposes relating to the conduct of an insolvency proceeding. A potential outcome of such structured "Communication" has been described thus: "To harmonize and co-ordinate the administration of the Insolvency Proceedings, the [Country 1]

[32] See Proposal Restructuring Directive (2016), Article 2(6).
[33] Study Group on a European Civil Code, *Principles Definitions and Model Rules of European Private Law* (European Law Publishers 2008), Annex I (Definitions), p. 328. The definition is not included in DCFR Outline Edition (2009).
[34] See EIR (2015), Article 2(1).
[35] UNCITRAL Legislative Guide (2004), paras. 12, under B "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".

Court and the [Country A] Court may coordinate activities with each other [and consider whether it is appropriate to defer to the judgment of the other Court]."[36]

"Composition"

Composition is used as a term to reflect a proceeding with the goal of rehabilitating the business of the entity or individual that is involved in insolvency proceedings, possibly new owners, including arrangement, suspension of payment, reconstruction, reorganization, or similar processes, with distributions to creditors and/or shareholders or other equity holders of cash, property and/or obligations of, or interests in, the rehabilitated business.[37] See also "restructuring plan" or "reorganisation plan".

"Condition"

A "condition" is a provision which makes a legal relationship or effect depend on the occurrence or non-occurrence of an uncertain future event. A condition may be suspensive or resolutive.[38]

"Conduct"

"Conduct" means voluntary behaviour of any kind, verbal or nonverbal: it includes a single act or a number of acts, behaviour of a negative or passive nature (such as accepting something without protest or not doing something) and behaviour of a continuing or intermittent nature (such as exercising control over something).[39]

"Confirmation"

The approval by a court of a restructuring plan that has previously been adopted by the affected creditors.[40] The confirmation will make the plan binding on both the affected creditors that approved the restructuring plan and those that dissented from it.[41] Usually, the review of the restructuring plan by the court will comprise the conduct of the adoption process and other specified issues, and relies upon creditors having sufficient commercial acumen to make an informed decision on the adoption of the plan.[42] This would usually not include economic assessments of the feasibility of the plan but has a formal legal nature.[43]

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[36] III Committee on International Jurisdiction and Cooperation, *Prospective Model International Cross-border Insolvency Protocol* (Draft-Annotated, June 2009), Article 5(1)(b) (footnote omitted).
[37] International Bar Association, Cross-Border Insolvency Concordat (1995), Glossary of terms (hereafter "Concordat (1995)").
[38] DCFR Outline Edition (2009), Annex (Definitions), p. 548.
[39] DCFR Outline Edition (2009), Annex (Definitions), p. 548.
[40] Principles of European Insolvency Law (2003), § 11.3: Proposal Restructuring Directive (2016), Article 10.
[41] UNCITRAL Legislative Guide (2004), Part I (II), Point 31.
[42] UNCITRAL Legislative Guide (2004), Part I (II), Part I (III), Point 6.
[43] UNCITRAL Legislative Guide (2004), Part I (II), Part I (III), Part II (IV), Points 60 and 64.

Confirmation of a restructuring plan by a judicial or administrative authority is necessary to ensure that the reduction of the rights of creditors or interests of equity holders is proportionate to the benefits of the restructuring and that they have access to an effective remedy.[44]

"Connected person"

A "connected person" is any person or a company with a close relationship to the debtor, usually through association or blood.[45] See also "related person".

"Consumer"

A consumer is any natural person (individual) who is not an entrepreneur.[46]

"Cooperation"

The process of "Cooperation", and its main purpose, has been described thus: "To assist in the efficient administration of the Insolvency Proceedings and in recognizing that any of the Debtors may be creditors of any of the other Debtors' estates, the Debtors and the Estate Representatives shall, where appropriate: (a) cooperate with each other in connection with actions taken in the [Country 1] Court and the [Country A] Court and (b) take any other appropriate steps to coordinate the administration of the Insolvency Proceedings for the benefit of the Debtors' respective estates."[47]

"Court"

According to Article 2(6) of the European Insolvency Regulation (2015) "Court shall mean the judicial body or any other competent body of a Member State empowered to open insolvency proceedings, to confirm such openings or to take decisions in the course of such proceedings. Recital (20) explains that "insolvency proceedings do not necessarily involve the intervention of a judicial authority. The expression "court" in the EIR (2015) should be given a broad meaning and include a person or body empowered by national law to open insolvency proceedings."[48] The UNCITRAL Legislative Guide and the UNCITRAL Practice Guide use a rather similar expression for "Court": "a judicial or other authority competent to control or supervise insolvency proceedings".[49] Within the context of Article 234 EC Treaty,

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[44] Recital 30 to Proposal Restructuring Directive (2016).

[45] G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 448.

[46] See also G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 448.

[47] III-Committee on International Jurisdiction and Cooperation, *Prospective Model International Cross-border Insolvency Protocol* (Draft-Annotated, June 2009), Article 5(1)(a) (footnote omitted).

[48] EIR (2015), Recital (20).

[49] UNCITRAL Legislative Guide (2004), para. 12, under B "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".

the Court of Justice of the European Union has decided that a functional criterion, and not the national definition, should be used in order to decide whether an authority is to be regarded as a court.[50]

"Cram-Down"

The mechanism by which a restructuring plan, that has been adopted by the requisite majority, is made binding on dissenting creditors (including secured, unsecured and priority creditors).[51] See also "cross-class cramdown".

"Creditor"

The UNCITRAL Legislative Guide provides for "Creditor": a natural or legal person that has a claim against the debtor that arose on or before the commencement of the insolvency proceedings.[52] Within the framework of the DCFR the Study Group on a European Civil Code and the Acquis Group have defined a creditor as: "A person who has right to performance of an obligation, whether monetary or non-monetary, by another person, the debtor."[53] The ALI NAFTA Principles (2003), Appendix A, Definitions provide: "Creditor" refers to someone with a claim against a debtor, but also includes other persons with an interest in the proceeding, such as co-owners and others claiming property interests in the debtor's property.

"Creditors' committee"

A "creditors' committee" is a representative body of creditors appointed in accordance with the applicable insolvency law, having consultative and other powers as specified in the insolvency law.[54]

"Cross-border agreement"

A cross-border agreement is an agreement entered into, either orally or in writing, intended to facilitate the coordination of cross-border insolvency proceedings and cooperation

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[50] C-86/00 *HSB Wohnbau*,,EU:C:2001:394..

[51] UNCITRAL Legislative Guide (2004), Part II(IV), points 28, 29 and 54, and The World Bank, Principles for effective Insolvency and Creditor-Debtor Regimes (2016), Principle C14.5 (hereafter "World Bank Principles (2016)").

[52] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".

[53] DCFR Outline Edition (2009), Annex (Definitions), p. 330.

[54] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations". For an alternative, descriptive definition: "A committee of creditors recognized by the [Country 1 and/or Country A] Court in the [Country 1 and/or 2] Cases shall be referred to herein as "The Creditors' Committee", see III-Committee on International Jurisdiction and Cooperation, *Prospective Model International Cross-border Insolvency Protocol* (Draft-Annotated, June 2009), Article 2(1)(vii).

between courts, between courts and insolvency representatives, and between insolvency representatives, sometimes also involving other parties in interest.[55] See also "Protocol".

"Cross-class cram-down"

A "cross-class cram-down" would allow a court (or administrative authority) to confirm a restructuring plan over the dissent of one or several affected classes of creditors or shareholders.[56]

"Debtor"

The ALI NAFTA Principles (2003), Appendix A, Definitions, state as definition: "Debtor" in most contexts refers to a legal person who is the subject of a bankruptcy or insolvency proceeding.

The European Insolvency Regulation (2015) states that: "This Regulation should apply to insolvency proceedings … irrespective of whether the debtor is a natural person or a legal person, a trader or an individual." [57] A further definition is not provided. Within the framework of the DCFR the following definition is provided: "A person who has an obligation, whether monetary or non-monetary, to another person, the creditor."[58]

"Debt for equity swap"

A "debt for equity swap" is the process by which (a part of) the debtor's debt is conversed to equity, either by transferring existing shares or issuing new shares to creditors in turn for the cancellation of their claims. It results in the restoration of the balance sheet solvency of the debtor while distributing non-cash value to creditors.[59]

"Debtor in possession"

The UNCITRAL Legislative Guide provides a description for a certain kind of debtor, namely "debtor in possession", which is a debtor in reorganization proceedings which are so structured that the debtor him- or herself, or itself, (especially the board of a company) retains full control over the business, with the consequence that the court does not appoint an insolvency representative.[60] This last part is not included in the definition in the European

[55] UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".
[56] See Proposal Restructuring Directive (2016), Article 2(8).
[57] EIR (2015), Recital (9).
[58] DCFR Outline Edition (2009), Annex (Definitions), p. 550.
[59] INSOL International Workout Principles II (2017), p. 25, and UNCITRAL Legislative Guide (2004) Part II, (IV), point 44.
[60] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations". The ALI NAFTA Principles (2003), Annex A, Definitions, provide: "Debtor in possession" refers to the person or persons entitled to operate the affairs of a

Insolvency Regulation (2015): a 'debtor in possession' means a debtor in respect of which insolvency proceedings have been opened which do not necessarily involve the appointment of an insolvency practitioner or the complete transfer of the rights and duties to administer the debtor's assets to an insolvency practitioner and where, therefore, the debtor remains totally or at least partially in control of its assets and affairs.[61]

"Deferral"

When one court accepts the limitation of its responsibility with respect to certain issues, including for example, the ability to hear certain matters and issue certain orders, in favour of another court, this is named deferral.[62]

"Deferred creditor"

"Deferred creditors" are subordinated creditors meaning that, either under contractual agreements or by insolvency law, they only receive any distribution in insolvency proceedings after all other creditors were paid in full. See also "subordinated creditors".

"Discharge"

The release of a debtor from claims that were, or could have been, addressed in the insolvency proceedings.[63] Alternative: a court order or provision of an instrument effecting a composition releasing a debtor from all liabilities that were, or could have been, addressed in the insolvency proceeding, including contracts that were modified as part of a composition.[64]

"Disposal"

Every means of transferring or parting with an asset or an interest in an asset, whether in whole or in part, is named "disposal".[65]

"Disqualification"

A process that leads to a director being unable to act as a director and, in some jurisdictions, act in other capacities.[66]

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debtor under either a Chapter 11 reorganization in the United States or a concurso mercantil in Mexico, and includes a Mexican debtor in conciliation in Mexico."

[61] See EIR (2015), Article 2(3).

[62] UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".

[63] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions".

[64] Concordat (1995), Glossary of terms.

[65] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions".

“Dissenting creditors”

Creditors who reject a proposed plan in a voting process which means that they object to the terms of a restructuring plan.[67]

“Distribution”

Distribution means paying creditors and/or shareholders from proceeds of selling the assets of the estate.

“Domestic assets”

“Domestic assets” refers to assets within the territorial jurisdiction of a court, usually a recognizing court.[68]

“Duty”

A person has a “duty” to do something if the person is bound to do it or expected to do it according to an applicable normative standard of conduct. A duty may or may not be owed to a specific creditor. A duty is not necessarily an aspect of a legal relationship. There is not necessarily a sanction for breach of a duty. All obligations are duties, but not all duties are obligations.[69] See also “obligation”.

“Electronic”

“Electronic” means relating to technology with electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities. An “electronic signature” then means data in electronic form which are attached to, or logically associated with, other data and which serve as a method of authentication.[70]

“Enacting State”

An Enacting State is a State that has enacted legislation based on the UNCITRAL Model Law on Cross-Border Insolvency.[71]

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[66] See also G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 449.
[67] See also G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 449.
[68] ALI NAFTA Principles (2003), Appendix A, Definitions.
[69] DCFR Outline Edition (2009), Annex (Definitions), p. 553.
[70] See for both definitions DCFR Outline Edition (2009), Annex (Definitions), p. 553.
[71] UNCITRAL Judicial Perspective (2011), B “Glossary”, under (c).

“Encumbered asset”

An “encumbered asset” is an expression for an asset in respect of which a creditor has a security interest.[72]

“Enforcement process”

A procedure under the control of a court for collecting claims in respect of which there has been a court order, which may include seizing assets.[73]

“Entrepreneur”

An individual, with unlimited liability, carrying out a trade, profession, craft or business as a natural person.[74]

“Enterprise group”

An “enterprise group” has been described as: “Two or more enterprises that are interconnected by control or significant ownership”. In the given description, “enterprise” means “any entity, regardless of its legal form, that is engaged in economic activities and may be governed by the insolvency law”, whereas “control” means “the capacity to determine, directly or indirectly, the operating and financial policies of an enterprise”.[75]

“Equity holder”

An “equity holder” is the holder of issued stock or a similar interest that represents an ownership claim to a proportion of the capital of a corporation or other enterprise.[76]

“Establishment”

Article 2(10) of the European Insolvency Regulation (2015) defines "establishment" as meaning: “any place of operations where the debtor carries out or has carried out in the 3-months period prior to the request to open main insolvency proceedings a non-transitory economic activity with human means and assets.” This term is used primarily for the purpose of establishing territorial/secondary jurisdiction within the meaning of Article 3(2) European

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[72] UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”. UNCITRAL Practice Guide (2009), under B “Glossary”, in “2. Terms and explanations”.

[73] See also G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization*, Cheltenham 2017, p. 449.

[74] G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 449.

[75] UNCITRAL Legislative Guide (2010), “Glossary”, under (a), (b) and (c) respectively.

[76] UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”.

Insolvency Regulation (2015). A similar, though not completely identical, definition as in Article 2(10) of the European Insolvency Regulation (2015) is also contained in the UNCITRAL Model Law, which provides that "establishment" means "any place of operations where the debtor carries out a non-transitory economic activity with human means and goods or services."[77] It also misses the "anti-forum shopping" requirement '… or has carried out in the 3-months period prior to the request to open main insolvency proceedings'.

"Estate"

The term estate is used several times in the European Insolvency Regulation (2015), though not in the UNCITRAL Model Law. It is generally used to describe the object of insolvency proceedings, being the debtors' assets, to which the goal of such proceedings (either liquidation or reorganisation) relate.

"Executory contract"

An "executory contract" means a contract between the debtor and one or more creditors under which both sides still have obligations to perform at the moment the stay of individual enforcement actions is ordered.[78]

"Financial contract"

A financial contract is any spot, forward, future, option or swap transaction involving interest rates, commodities, currencies, equities, bonds, indices or any other financial instrument, any repurchase or securities lending transaction, and any other transaction similar to any transaction referred to above entered into in financial markets and any combination of the transactions mentioned above.[79]

"Foreign Court"

The UNCITRAL Model Law provides a specific definition of this term as: "A judicial or other authority competent to control or supervise a foreign proceeding."[80] See also the description of "Court" above.

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[77] UNCITRAL Model Law (1997), Article 2 (f). This definition also is provided in the UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions" and in the UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".
[78] See Proposal Restructuring Directive (2016), Article 2(5).
[79] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions".
[80] UNCITRAL Model Law (1997), Article 2(e).

“Foreign creditor”

In relation to any given jurisdiction, the term refers to a creditor whose address, as maintained in the business records of the debtor, is outside that jurisdiction.[81] In a European context, a “foreign creditor” means a creditor which has its habitual residence, domicile or registered office in a Member State other than the State of the opening of proceedings, including the tax authorities and social security authorities of Member States.[82]

“Fraud”

A misrepresentation (or: inaccurate impression) represents “fraud” or is fraudulent if it is made with knowledge or belief that it is false and is intended to induce the recipient to make a mistake to the recipient’s prejudice. A non-disclosure is fraudulent if it is intended to induce the person from whom the information is withheld to make a mistake to that person’s prejudice.[83]

“Full discharge of debt”

A “full discharge of debt” means cancellation of outstanding debt subsequent to a procedure comprising a realisation of assets and/or a repayment/settlement plan.[84] See also “discharge”.

“General body of creditors”

A collective expression denoting all those whose claims or rights are affected by the debtor’s insolvency, and whose interests are therefore of particular concern to the legal regime under whose auspices an insolvency proceeding is taking place. Acts to which the debtor is or has been a party, or which have taken place in relation to property of the debtor, may be subject to impeachment if they can be characterised as having been detrimental to the interests of the general body of creditors, even if one or more individual creditors’ interests have not been harmed or may have benefited thereby.

“Going-concern value”

The “Going-concern value” is the value of the debtor’s business if it is kept alive rather than liquidated. [85]

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[81] ALI NAFTA Principles (2003), Appendix A, Definitions.
[82] See EIR (2015), Article 2(12).
[83] DCFR Outline Edition (2009), Annex (Definitions), p. 554.
[84] See Proposal Restructuring Directive (2016), Article 2(14).
[85] See also G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 449.

"Good faith"
"Good faith" has been described as a mental attitude characterised by honesty and an absence of knowledge that an apparent situation is not the true situation.[86]

"Goods"

The term "goods" means any material object which can be subject to human control. See also "Assets"; "Establishment"; "Immovable property"; and "Movables".

"Group of companies"

A "group of companies" means a parent undertaking and all its subsidiary undertakings.[87] See also "enterprise group".

"Hybrid proceedings"

See "Workout support proceedings".

"Impaired claims"

A claim is impaired by a restructuring plan if the plan includes an alteration in the rights that the holder of a claim (or equity interest) would enjoy outside bankruptcy.[88]

"Informal arrangement"

Any contractual settlement of debts which is agreed without any involvement of a court.[89] See also "workout".

"Insolvency"

The definition of the term "insolvency" is usually taken from the national law of the Member State in which insolvency proceedings are opened. "Insolvency" is generally described as the moment when a debtor is generally unable to pay its debts as they mature ("cash flow insolvency"), or when its liabilities exceed the value of its assets ("balance sheet

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[86] DCFR Outline Edition (2009), Annex (Definitions), p. 555.
[87] EIR (2015), Article 2(13).
[88] See also G. McCormack & A. Keay, S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 450.
[89] See also G. McCormack & A. Keay, S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 450.

insolvency").[90] It may be also defined as: "A state of affairs where a debtor is being overwhelmed by liabilities and where, as a consequence, the creditors at large can no longer expect to receive fully and in time what is owed to them from a normal management of the debtor's affairs or business. Viewed by business standards, the debtor tends to act abnormally." [91] Accordingly, the term "insolvent" is attributed to a "debtor having liabilities that exceed the value of assets; having stopped paying debts in the ordinary course of business; or being unable to pay them as they fall due".[92] In the European Insolvency Regulation (2015), the term "insolvency" is not described as such; it only refers to "insolvency proceedings".

It is important to clarify that in legal literature the terms "bankruptcy" and "insolvency" are often used interchangeably,[93] although it should be noted that the terms have acquired in modern usage the separate meanings of procedures to be applied, in the former instance, to individuals, sole traders and partnerships and, in the latter, to corporate entities. This again is not the case in the United States, where bankruptcy is used for all such procedures.[94]

"Insolvency administrator"

The term "Insolvency administrator" refers to the person or entity that the bankruptcy law in a state places in charge of a bankrupt's property, including trustees, liquidators, sindicos, administrators, curators, monitors, interim trustees, court-appointed trustees and debtors in possession.[95] An "insolvency administrator" is a person or body, including one appointed on an interim basis, authorized in an insolvency proceeding to administer the reorganization or liquidation of the insolvent person's assets or affairs.[96] In the European Insolvency Regulation (2000) as a general term of reference to denote any of the recognised species and designations of insolvency office holders the word "liquidator" was used throughout. Under the EIR (2015) "liquidator" has been substituted by "insolvency practitioner". See also "liquidator", "office holder" and "practitioner in the field of restructuring".

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[90] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".
[91] See W.W. McBryde, A. Flessner and S.C.J.J. Kortmann, *Principles of European Insolvency Law* (Law of Business and Finance Vol. 4, Kluwer Legal Publishers 2003), p. 15.
[92] Study Group on a European Civil Code, *Principles Definitions and Model Rules of European Private Law*, European Law Publishers (2008), Annex I (Definitions), p. 333. The definition is not included in DCFR Outline Edition (2009).
[93] See Bob Wessels, Bruce A. Markell and Jason J. Kilborn, *International Cooperation in Bankruptcy and Insolvency Matters*, (Oxford University Press Inc., New York 2009), at 1.
[94] Paul J. Omar, *European Insolvency Law* (Ashgate 2004), p. 3.
[95] ALI NAFTA Principles (2003), Appendix A, Definitions. In the NAFTA context "administrator" also includes "sindicos" and "Mexican debtors in conciliations." The same set of definitions provide: "Sindico" refers to an administrator appointed under *La Ley de Quiebras y Concurso mercantil* in Mexico, and "Mexican debtor in conciliation" refers to the person or persons entitled to control the property and affairs of a debtor under a concurso mercantil in Mexico.
[96] Study Group on a European Civil Code, *Principles Definitions and Model Rules of European Private Law*, European Law Publishers (2008), Annex I (Definitions), p. 335. The definition is not included in the DCFR Outline Edition (2009), see footnote 136.

“Insolvency case”

See “Insolvency proceeding”/ “Insolvency proceedings”

“Insolvency estate”

An “insolvency estate” is formed by assets of the debtor that are subject to the insolvency proceedings.[97] See also “estate”.

“Insolvency practitioner”

An “insolvency practitioner” is any person or body whose function it is to represent the collective interest of creditors and to administer or liquidate the assets of which the debtor has been divested or to supervise the administration of the debtor’s affairs.[98] The European Insolvency Regulation (2015) provides a similar definition: any person or body whose function, including on an interim basis, is to: (i) verify and admit claims submitted in insolvency proceedings; (ii) represent the collective interest of the creditors; (iii) administer, either in full or in part, assets of which the debtor has been divested; (iv) liquidate the assets referred to in point (iii); or (v) supervise the administration of the debtor's affairs.[99]

“Insolvency proceedings”/ “Insolvency proceeding”

An insolvency proceeding (alternatively referred to in the plural form as “insolvency proceedings”) means a collective judicial or administrative proceeding, including an interim proceeding, in which the assets and affairs of a person who is believed to be insolvent are subject to control or supervision by a court or other competent authority for the purpose of reorganization or liquidation.[100] In the NAFTA context, “proceeding” refers to bankruptcy or insolvency proceedings, including a bankruptcy “case” in the United States.[101] The Draft Common Frame of Reference (DCFR) uses a nearly similar description.[102] “Insolvency proceedings” are: collective proceedings, subject to court supervision, either for reorganization or liquidation.[103]The European Insolvency Regulation (2015) specifies what

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97 UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”. UNCITRAL Practice Guide (2009), under B “Glossary”, in “2. Terms and explanations”.

98 G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 450.

99 See Article 2(5) EIR (2015). These persons and bodies listed in Annex B. The term insolvency practitioner replaces the term ‘liquidator’, used under the InsReg 2000.

100 *Black’s Law Dictionary* (Thomson West, Eight Edition 2004).

101 ALI NAFTA Principles (2003), Appendix A, Definitions.

102 DCFR Outline Edition (2009), Annex (Definitions), p. 556.

103 UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”. UNCITRAL Practice Guide (2009), under B “Glossary”, in “2. Terms and explanations”. ALI NAFTA Principles (2003), Appendix A, Definitions: “Bankruptcy proceeding” refers to a collective proceeding for the adjustment, collection, or payment of debts of a legal person on behalf of all creditors and other interested parties and includes proceedings often called “insolvency proceedings.” It includes any proceeding under the Bankruptcy and Insolvency Act or the Company Creditors Arrangement Act in Canada, under *La Ley de Concursos Mercantiles* in

are to be regarded as insolvency proceedings in the Member States to which this Regulation applies, listed for each Member State in an Annex A to the Regulation. For harmonisation purposes the indication “insolvency procedure” means a collective insolvency procedure which entails a partial or total divestment of the debtor and the appointment of a liquidator.[104]

“Insolvency representative”

An insolvency representative is a person or body, including one appointed on an interim basis, authorized in insolvency proceedings to administer the reorganization or the liquidation of the insolvency estate.[105] While this definition could include an insolvency practitioner as well as a debtor in possession, other, like the Principles of European Insolvency Law (2003), seem to restrict the meaning of this term to insolvency practitioners: “The creditors’ collective interests may be represented by a meeting of creditors, a creditors’ committee or a creditors’ representative.”[106]

“Interim Finance”

“Interim finance” describes short-term funds that are necessary for the debtor to cover administrative expenses after the commencement of restructuring or insolvency proceeding until either the implementation of the restructuring plan or the sale of the debtor’s business as a going concern. Such funds, therefore, usually allow for the continuation of the business by covering post-commencement expenses like e.g. costs for labour, insurance, rent, maintenance of contracts and other operating expenses, or other costs necessary for the preservation or enhancement of the value of the assets of the estate.[107] In the EU, the term “interim financing” has been used to describe any funds, whether provided by an existing or new creditor, that are reasonably and immediately necessary for the debtor's business to continue operating or to survive, or to preserve or enhance the value of that business pending the confirmation of a restructuring plan.[108] To be distinguished from “new financing”.

Mexico, and under the Bankruptcy Code in the United States.” And also: “Insolvency proceeding” refers to a bankruptcy proceeding as defined above.

[104] See Proposal Restructuring Directive (2016), Article 2(1), with ‘liquidator’ probably meaning ‘insolvency practitioner’. The term ‘insolvency proceedings’ means the proceedings listed in Annex A, Article 2(4) EIR (2015).

[105] UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”. UNCITRAL Practice Guide (2009), under B “Glossary”, in “2. Terms and explanations”.

[106] Principles of European Insolvency Law (2003), Principle 3.1.

[107] See UNCITRAL Legislative Guide (2004), Part II (II), Points 94 and 118, EBRD Core Principles for an Insolvency Law Regime (2004), Principle 8, and Commission’s Recommendation (2014), Point 6(e).

[108] See Proposal Restructuring Directive (2016), Article 2(12).

“Interim proceedings”

Insolvency laws may require a court to test the factual grounds of a motion to commence insolvency proceedings before deciding about the motion which results in a period between the petition to commence and the actual commencement of proceedings called “interim proceedings”. Respective laws commonly allow for “Interim measures” (see “preservation measures”).

“Intermediary”/ “Independent intermediary”

An intermediary or independent intermediary is a person who may be appointed by a court to facilitate coordination between insolvency proceedings concerning an insolvent debtor or a group of companies which will be, are, or were subject to insolvency proceedings in different states. An intermediary’s general task is to help ensure that a transnational insolvency proceeding is operated effectively, to establish practical means of conducting communication between the courts concerned, to address the practical issues generated by such factors as the different working languages in which the various courts are able to operate, and the logistical problems caused by the fact (if such is the case) that the courts are situated in different time zones thereby impeding the conduct of live communications during normal working hours. The European Insolvency Regulation (2015) uses (in Article 41(1)) the term ‘independent person or body’. For a person who may be appointed by a court to facilitate coordination of insolvency proceedings concerning enterprise group members taking place in different jurisdictions the UNCITRAL Legislative Guide uses the term “court representative”.[109]

“International insolvency case”

An insolvency case may be said to possess an international character when there are material elements within the case that actually or potentially engage the application of the laws of more than one state and its system of law including its rules of jurisdiction or recognition and its rules of private international law. Such cases are alternatively known as “cross-border” or “transnational” insolvency cases. See also “Insolvency proceeding”.

“International jurisdiction”

When a court exercises jurisdiction in accordance with principles laid down in the domestic law of the state in which it is established, the validity of such a proceeding for the purposes of international recognition and enforcement will depend on whether the circumstances under which such an exercise of jurisdiction by the first court has taken place are in conformity with the criteria established under the private international law of the recognising state. Where those criteria are met, the first court is said to have had “international jurisdiction” over the matter in question. There can be considerable variation between the private international law rules applied by different states with regard to the

[109] UNCITRAL Legislative Guide (2010), para. 37.

criteria which are applied for this purpose, thereby resulting in uneven (or "limping") levels of recognition and enforcement among the various sovereign states. Under international agreements certain criteria may come to be accepted as giving rise to international jurisdictional competence for the court in relation to which they are met in a given case, thereby transcending the rules of recognition of individual states and giving rise to a more uniform level of acceptance of the proceedings in question. See also "Recognition".

"Invalid"

"Invalid" in relation to a juridical act or legal relationship means that the act or relationship is void or has been voided.[110]

"Judge"

In UNCITRAL documents a "judge" is "a judicial officer or other person appointed to exercise the powers of a court or other competent authority having jurisdiction under legislation based on the Model Law".[111] Under the application of the European Insolvency Regulation (2015) for a similar function the term "court" is used. See "court".

"Judgment"

The European Insolvency Regulation (2015) provides that a "judgment opening insolvency proceedings" includes: (i) the decision of any court to open insolvency proceedings or to confirm the opening of such proceedings; and (ii) the decision of a court to appoint an insolvency practitioner.[112]

"Junior creditor"

See "deferred creditor" or "subordinated creditor".

"Jurisdiction"

The European Insolvency Regulation (2015) provides rules on jurisdiction in Article 3. It provides that in accordance with the principle of proportionality this Regulation should be confined to provisions governing jurisdiction for opening insolvency proceedings and judgments which are delivered directly on the basis of the insolvency proceedings and are closely connected with such proceedings.[113] The rules of jurisdiction set out in the European Insolvency Regulation establish only international jurisdiction, thus they designate the

[110] DCFR Outline Edition (2009), Annex (Definitions), p. 557.
[111] UNCITRAL Judicial Perspective (2011), B "Glossary", under (e).
[112] EIR (2015), Article 2(7).
[113] EIR (2015), Recital (6).

Member State the courts of which may open insolvency proceedings. Territorial jurisdiction within that Member State must be established by the national law of the Member State concerned.[114] The courts of the Member State within the territory of which the centre of a debtor's main interests is situated shall have jurisdiction to open insolvency proceedings. In the case of a company or legal person, the place of the registered office shall be presumed to be the centre of its main interests in the absence of proof to the contrary. Where the centre of a debtor's main interests is situated within the territory of a Member State, the courts of another Member State shall have jurisdiction to open insolvency proceedings against that debtor only if he possesses an establishment within the territory of that other Member State. The effects of those proceedings shall be restricted to the assets of the debtor situated in the territory of the latter Member State.[115] See also "International Jurisdiction".

"Legislative Recommendations"

"Legislative Recommendations" refers to recommendations for new legislation or international agreements that will go beyond current law to permit a substantially higher level of cooperation and integration.[116]

"Liquidator"

In general a liquidator may be defined as "a person appointed to wind up a business's affairs, by selling off its assets".[117] The European Communication & Cooperation Guidelines for Cross-border Insolvency (2007), the text of which has been set in the framework of the European Insolvency Regulation (2000), provides that "A liquidator is any appointed person or body whose function is to administer or liquidate assets of which the debtor has been divested or to supervise the administration of its affairs, either in reorganisation or in liquidation proceedings".[118] See also: "(Insolvency) administrator", "Insolvency practitioner" and "Office holder".

"Liquidation"

Liquidation is the process to sell and dispose of assets for the distribution of the proceeds to creditors in accordance with the insolvency law.[119]

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114 EIR (2015), Recital (26).
115 EIR (2015), Article 3.1-3.2.
116 ALI NAFTA Principles (2003), Appendix A, Definitions.
117 *Black's Law Dictionary* (Thomson West, Eighth Edition 2004).
118 CoCo Guidelines (2007), Guideline 4.1.
119 UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions".

“Local creditor”

“Local creditor” refers to a person who has an interest with an important and specific connection to a jurisdiction, a definition that includes a creditor secured in assets located in that jurisdiction or another person with a property (in rem) interest in assets located in the domestic jurisdiction, regardless of that person’s nationality, residence, or domicile.[120] In an EU context “local creditor” means a creditor whose claims against a debtor arose from or in connection with the operation of an establishment situated in a Member State other than the Member State in which the centre of the debtor's main interests is located.[121]

“Main Insolvency Proceeding”/ “Main insolvency proceedings”

Main insolvency proceeding refers to a full domestic bankruptcy case brought in the country that is the centre of the main interests of a debtor, so the ALI NAFTA Principles (2003), Appendix A, Definitions. In the European Insolvency Regulation (2015) the term “main insolvency proceedings” refers to the primary proceedings opened in the Member State where the debtor has the centre of his main interests (COMI). These proceedings have universal scope and aim at encompassing all the debtor’s assets.[122] Moreover, the UNCITRAL Model Law defines “foreign main proceeding as: a foreign proceeding taking place in the State where the debtor has the centre of its main interests.”[123]

“Mediator”

A “mediator” is a person who (possibly appointed by the court) assists the debtor and the creditors in negotiations on a restructuring plan.[124]

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[120] ALI NAFTA Principles (2003), Appendix A, Definitions.
[121] See EIR (2015), Article 2(11).
[122] EIR (2015), Recital 23. See *MG Probud Gdynia sp. z o.o. v Hauptzollamt Saarbrücken*, Case C-444/07, CJEU 21 January 2010, [2010] B.C.C. 453: “22 … it should be noted first of all that Article 3 of the Regulation makes provision for two types of insolvency proceedings. Insolvency proceedings opened, in accordance with Article 3(1), by the competent court of the Member State within the territory of which the centre of a debtor’s main interests is situated, described as the ‘main proceedings’, produce universal effects in that the proceedings apply to the debtor’s assets situated in all the Member States in which the Regulation applies. Although, subsequently, proceedings under Article 3(2) may be opened by the competent court of the Member State where the debtor has an establishment, those proceedings, described as ‘secondary proceedings’, produce effects which are restricted to the assets of the debtor situated in the territory of the latter State (see Case C-341/04 Eurofood IFSC [2006] ECR I-3813, paragraph 28).” Referring affirmatively to the cited passage, see CJEU 17 November 2011, Case C-112/10 (*Procureur-generaal bij het hof van beroep te Antwerpen v ZaZa Retail BV*) and CJEU 15 December 2011, Case C-191/10 (*Rastelli Davide e C. Snc v Jean-Charles Hidoux, in his capacity as liquidator appointed by the court for the company Médiasucre international*).
[123] UNCITRAL Model Law (1997), Article 2(b). UNCITRAL Practice Guide (2009), under B “Glossary”, in “2. Terms and explanations”.
[124] See also G. McCormack & A. Keay, S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 450.

"Moratorium"

A "moratorium" is a legal bar on creditors commencing or continuing legal action to recover debt.[125] See also "stay of proceedings".

"New financing"

The expression "new financing" means any new funds, whether provided by an existing or a new creditor, that are provided to fund the implementation of a restructuring plan.[126] To be distinguished from "interim finance".

"No asset case"

A "no asset case" is an insolvency case where the debtor has no estate left to be distributed – a phenomenon often described in small business cases or personal bankruptcies.

"No creditor worse off"

See "best interest test".

"Non-Participating Creditor(s)"

Creditor(s) who decide(s) not to participate in insolvency proceedings, despite receiving due notice of the initiation of such proceedings, and having the opportunity to participate. A restructuring plan will be binding on them if the court has jurisdiction.[127]

"Office holder"

The EBRD Insolvency Office Holder Principles includes detailed rules on office holders, but do not include a clear definition. In Annex A to the European Insolvency Regulation (2015) around one hundred national names are listed for those persons or bodies that in the context of the Regulation have been given one designation, namely one or more "insolvency practitioner". See also "Insolvency Administrator". Because of the tasks that an office holder might be expected to perform, the responsibilities that an office holder will have and the trust that is reposed in an office holder, it should be the case that an office holder should have some fundamental qualifications. These include general ability and intelligence, experience, professional knowledge and good character. Further, in several countries

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[125] See also G. McCormack & A. Keay, S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 450.

[126] See also the Proposal Restructuring Directive (2016), Article 2(11).

[127] See Commission's Recommendation (2014), Recommendation 25 and 26, and EU Cross-Border Insolvency Court-to-Court Cooperation Principles (2014), Principle 25 and commentary.

professions are regulated by a system of licensing. Office holders should be regarded as a professional body of persons and licensed accordingly.[128] Under the application of the European Insolvency Regulation (2015) an insolvency practitioner "is required to act with the appropriate knowledge of the Insolvency Regulation and its application in practice", and "is required to act honestly, objectively, fairly and expeditiously in dealing with all parties concerned, including the courts."[129]

"Ordinary course of business"

With "ordinary course of business" generally is meant transactions consistent with both: (i) the operation of the debtor's business prior to insolvency proceedings; and (ii) ordinary business terms.[130]

"Out-of-the-money creditors and/or shareholders"

Parties in restructuring or insolvency proceedings who cannot expect to receive any payment or other consideration in case of a (piecemeal or going concern) liquidation are held to be "out of the money" in negotiations about an alternative restructuring/insolvency plan.[131]

"Over-indebted entrepreneur"

An "over-indebted entrepreneur" means a natural person exercising a trade, business, craft or profession, who is otherwise than temporarily unable to pay debts as they fall due.[132]

"Par est condicio omnium creditorum"

Literally: 'The condition of all creditors is: equal'. This maxim is widely employed to express the principle of equality of treatment and status to be accorded to all creditors in collective insolvency proceedings. It is a principle which suffers numerous exceptions under the laws of the various countries. See also "pari passu principle".

"Parent undertaking"

In an EU context "parent undertaking" means an undertaking which controls, either directly or indirectly, one or more subsidiary undertakings. An undertaking which prepares

[128] EBRD Insolvency Office Holders Principles (2007), Principle 1 (hereafter "EBRD IOH Principles (2007)").
[129] CoCo Guidelines (2007), Guideline 4.2 – 4.3 (still referring to EIR (2002)).
[130] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".
[131] See also G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 450.
[132] See Proposal Restructuring Directive (2016), Article 2(13).

consolidated financial statements in accordance with Directive 2013/34/EU of the European Parliament and of the Council shall be deemed to be a parent undertaking.[133]

"Pari passu principle"

Latin for "equally and without preference" (literally "on an equal footing", hence "proportionately"). This term is often used in bankruptcy proceedings where creditors are said to be paid pari passu, that is each creditor is paid pro rata in accordance with the amount of his claim.[134]

The European Insolvency Regulation (2015) provides that in order to ensure equal treatment of creditors a creditor who has, in the course of insolvency proceedings, obtained a dividend on his claim shall share in distributions made in other proceedings only where creditors of the same ranking or category have, in those other proceedings, obtained an equivalent dividend.[135] The same principle is reflected in the ALI NAFTA Principles (2003): "A creditor should not be able to use distributions in multiple countries to recover in any country more than the percentage recovered by other creditors of the same class in that country."[136] Likewise for "Pari passu", the UNCITRAL Legislative Guide comprises the principle according to which similarly situated creditors are treated and satisfied proportionately to their claim out of the assets of the estate available for distribution to creditors of their rank.[137]

"Party"

In the context of a legal proceeding, the term "party" may bear a narrow, technical meaning or a broader, more general one. In its narrow, technical sense, more fully expressed as "party to proceedings", the term denotes any person (whether natural or legal) who is formally joined in the legal process, either voluntarily or involuntarily. Such persons may be identified by name in the formal documentation relating to the conduct of the proceeding, or alternatively they may be referred to in less specific terms. In the more general sense, the term "party" may be used to denote any persons who are, or who may be, in some way materially affected by the outcome of the proceeding. Such persons are more aptly referred to as "parties in interest" (see below).

"Party in interest"

A party in interest is any party whose rights, obligations or interests are affected by insolvency proceedings or particular matters in the insolvency proceedings, including the debtor, the insolvency representative, a creditor, an equity holder, a creditor committee, a government authority or any other person so affected. It is not intended that persons with

133 See EIR (2015), Article 2(14).
134 Sands & Associates, Insolvency Dictionary (2000), available at www.sands-trustee.com/pq.htm.
135 EIR (2015), Article 23.2.
136 ALI NAFTA Principles (2003), General Principle VII.
137 UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions".

remote or diffuse interests affected by the insolvency proceedings would be considered to be a party in interest.[138]

"Payment plan"

A "payment plan" is a schedule of payments over a specified time period agreed between the debtor and creditor or imposed by the court.[139]

"Plan of reorganization"

See "Restructuring plan".

"Plenary proceeding"

A forum or insolvency proceeding which addresses, on a plenary basis, administrative matters, including, on the one hand, operation of the debtor's business or assets, and, on the other hand, the filing, processing and allowance of claims and distributions to creditors.[140]

"Post-commencement claim"

A claim against the estate arising after commencement of insolvency proceedings.[141]

"Practitioner in the field of restructuring"

In the EU the expression "practitioner in the field of restructuring" has been suggested, and it means any person or body appointed by a judicial or administrative authority to carry out one or more of the following tasks:
(a) to assist the debtor or the creditors in drafting or negotiating a restructuring plan;
(b) to supervise the activity of the debtor during the negotiations on a restructuring plan and report to a judicial or administrative authority;
(c) to take partial control over the assets or affairs of the debtor during negotiations.[142]

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[138] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".
[139] See also G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 451.
[140] Concordat (1995), Glossary of terms.
[141] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions".
[142] See Proposal Restructuring Directive (2016), Article 2(15).

“Post-commencement privilege”

See “administrative expense”.

“Preference”

The term “preference” may have different meanings. In the context of avoidance laws, a preference is any transaction which results in a creditor obtaining an advantage or irregular payment. Such transactions may be recovered under preference laws in insolvency proceedings.[143] In the context of ranking creditor claims in insolvency proceedings, a preference is a right to be paid ahead of other creditors according to insolvency law. See also “priority”, “priority claim”, “privileged claim” or “ranking”.

“Pre-insolvency transaction”

A transaction entered into by a company before it has become subject to some form of formal insolvency proceedings.[144]

“Pre-pack”

A “pre-pack” (sometimes “pre-packaged” sale) is a method in which the contract for sale of all or a substantial part of the assets of a debtor is negotiated confidentially prior to the commencement of an insolvency proceeding, without consultation with all creditors, which takes effect immediately on the commencement of the formal proceedings.

“Preservation Measures”

In relation to this term, the European Insolvency Regulation (2015) provides that the court having jurisdiction to open the main insolvency proceedings should be enabled to order provisional and protective measures from the time of the request to open proceedings. Preservation measures both prior to and after the commencement of the insolvency proceedings serve as an important guarantee to the effectiveness of the insolvency proceedings.[145] Further, the court may grant provisional relief when necessary to preserve the ability to grant effective relief by final judgment or to maintain or otherwise regulate the status quo. Provisional measures are governed by the principle of proportionality.[146]

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[143] UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”.
[144] See also G. McCormack, A. Keay &, S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 451.
[145] EIR (2015), Recital (36).
[146] ALI/UNIDROIT Principles of Transnationsl Civil Procedure (2004), Principle 8.1.

“Priority”

A priority is the right of a claim to rank ahead of another claim where that right arises by operation of law.[147]

“Priority claim”

“Priorities” (or “privileges”) refers to rights to a distribution in a bankruptcy proceeding prior to or with a priority over the rights of other creditors.[148] A “priority claim” is a claim that will be paid before payment of general unsecured creditors.[149]

“Privileged claim”

A “privileged” claim is a claim that, pursuant to statutory or other law, or pursuant to ranking rules, is given a preference or priority over common claims, including a public law claim arising from the public law of a nation.[150]

“Protection of value”

“Protection of value” reflects measures directed at maintaining the economic value of encumbered assets and third party owned assets during the insolvency proceedings (in some jurisdictions referred to as “adequate protection”). Protection may be provided by way of cash payments, provision of security interests over alternative or additional assets or by other means as determined by a court to provide the necessary protection.[151]

“Protocol”

American Law Institute’s Procedural Principle 14 (“Cooperation”) reads as follows: “A. The administrators in parallel proceedings should cooperate in all aspects of the case. Such cooperation is best obtained by way of an agreement or ‘protocol’ that establishes decision making procedures, but many decisions may be made informally as long as the essentials are agreed. B. A protocol for cooperation among proceedings should include, at a minimum, provisions for coordinated court approvals of decisions and actions when required and for communication with creditors as required under each applicable law. To the extent possible, it should also provide for timesaving procedures to avoid unnecessary and costly court hearings and other proceedings.” From its elucidation, it follows that Procedural Principle 14A goes to the first level of cooperation (cooperation between administrators), while

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[147] UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”. UNCITRAL Practice Guide (2009), under B “Glossary”, in “2. Terms and explanations”.
[148] ALI NAFTA Principles (2003), Appendix A, Definitions.
[149] UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”.
[150] Concordat (1995), Glossary of terms.
[151] UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”.

Procedural Principle 14B (interpreted as "Protocols approved by the courts") is regarded as a superior method of cooperation.[152] In the European Communication & Cooperation Guidelines for Cross-border Insolvency a similar description is used: "Cooperation may be best attained by way of an agreement or "protocol" that establishes decision-making procedures, although decisions may continue to be made informally as long as they are compatible with the substance of any such (insolvency) agreement[153] or "protocol"."[154] The European Insolvency Regulation (2015) uses the terms "agreement" and "protocol".[155]

"Public Register"

In general, a public register means a register, open for the public, in which the legal status of property (assets, goods) is registered. The European Insolvency Regulation (2015) provides that the liquidator may request that the judgment opening the proceedings referred to in Article 3(1) be registered in the land register, the trade register and any other public register kept in the other Member States. However, any Member State may require mandatory registration.[156]

"Ranking"

"Ranking" in relation to claims means putting the claims in an order of priority or subordination, which is determined by the law applicable.[157]

"Recognition"

Within the field of recognition of judgments, the ALI/UNIDROIT Principles require that a final judgment awarded in another forum in a proceeding substantially compatible with these Principles must be recognized and enforced unless substantive public policy requires

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[152] See Westbrook (reporter), *International Statement of United States Bankruptcy Law* (2nd volume, American Law Institute, Transnational Insolvency: Cooperation Among the NAFTA Countries, 4 Volumes, JP Juris Publishing, Inc., 2003), p. 66 et seq.
[153] UNCITRAL Practice Guide (2009), under B "Glossary", in "1, Notes on terminology": "Cross-border agreements are most commonly referred to in some States as "protocols", although a number of other titles have been used including insolvency administration contract, cooperation and compromise agreement, and memorandum of understanding. These Notes attempt to compile practice with respect to as many forms of cross-border agreement as possible and, since the use of the term 'protocol' does not necessarily reflect the diverse nature of the agreements being used in practice, these Notes use the more general term 'cross-border agreement'".
[154] CoCo Guidelines (2007) Guideline 12.4. For a sample of a protocol, see III-Committee on International Jurisdiction and Cooperation, *Prospective Model International Cross-border Insolvency Protocol* (Draft-Annotated, June 2009), available at www.iiiglobal.org. See for clauses which can be used in drafting a protocol UNCITRAL Practice Guide 2009.
[155] See EIR (2015), Article 41(1).
[156] EIR (2015), Article 29.
[157] Study Group on a European Civil Code, Principles Definitions and Model Rules of European Private Law, European Law Publishers (2008), Annex I (Definitions), p. 339. The definition is not included in DCFR Outline Edition (2009), "Ranking rules" are the rules by which claims and equity interests are ranked, see Concordat (1995), Glossary of terms.

otherwise. A provisional remedy must be recognized in the same terms.[158] Moreover, as a general principle of recognition, the ALI NAFTA Principles (2003) demand that the bankruptcy of a debtor in one NAFTA country should be recognized and given appropriate effect under the circumstances in each of the other NAFTA countries. Recognition should be granted as quickly and inexpensively as possible, with a minimum of legal formalities.[159]

The European Insolvency Regulation (2015) provides its own system of recognition of judgments concerning the opening, conduct and closure of insolvency proceedings which come within its scope and of judgments handed down in direct connection with such insolvency proceedings and which are handed down by another Member State. The system is based on immediate recognition. Such an automatic recognition means that the effects attributed to the insolvency proceedings by the law of the State in which the proceedings were opened extend to all other Member States, as recognition of judgments delivered by the courts of a Member State should be based on the principle of mutual trust. To that end, grounds for non-recognition should be reduced to the minimum necessary.[160] Further, the European Insolvency Regulation (2015) states that any judgment opening insolvency proceedings handed down by a court of a Member State which has jurisdiction pursuant to Article 3 shall be recognized in all the other Member States from the time that it becomes effective in the State of the opening of proceedings.[161] The European Insolvency Regulation (2015) establishes as an effect of recognition of judgments that the judgment opening the proceedings referred to in Article 3(1) shall, with no further formalities, produce the same effects in any other Member State as under the law of the State of the opening of proceedings, unless the European Insolvency Regulation (2015) provides otherwise and as long as no proceedings referred to in Article 3(2) are opened in that other Member State.[162]

“Related person”

The term “related person” as to an insolvent debtor is used to express that in the case that the debtor is a legal entity, a related person would include: (i) a person who is or has been in a position of control of the debtor; and (ii) a parent, subsidiary, partner or affiliate of the debtor. As to a debtor that is a natural person, a related person would include persons who are related to the debtor by consanguinity or affinity.[163] See also “connected person”.

“Remuneration”

In general “remuneration” is the compensation (honorarium) for an insolvency office holder: “Except as otherwise provided … each Country’s Representatives and their respective employees, members, agents and professionals: (a) shall be compensated for their services solely in accordance with the legislation and other applicable laws of that Country or orders

[158] ALI/UNIDROIT Principles of Transnational Civil Procedure (2004), Principle 30.
[159] ALI NAFTA Principles (2003), General Principle II A-B.
[160] EIR (2015), Recital 65.
[161] EIR (2015), Article 19.
[162] EIR (2015), Article 17.
[163] UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”.

of that Country's Court and (b) shall not be required to seek approval of their compensation in the Court of the other Country."[164]

"Reorganisation"

A "reorganisation" is any business rescue meaning the process by which the financial well-being and viability of a debtor's business can be restored and the business continue to operate, using various means possibly including debt forgiveness, debt rescheduling, debt-equity conversions and sale of the business (or parts of it) as a going concern.[165] The term is used in the US Bankruptcy Code and has spread from there. See also "restructuring".

"Reorganization plan"

See "restructuring plan".

"Rescue"

See "reorganisation" or "restructuring".

"Res judicata"

"Res judicata" is the plea that the matter in issue has already been the subject of a final adjudication by a court of competent jurisdiction.

"Restructuring"

The term "restructuring" is sometimes used synonymously to the term "reorganisation".[166] It should, however, be stressed that our report refers to a "restructuring" only when the business remains with the debtor as a result of the restructuring process. Thus, we would not include a sale of the business to the means of a restructuring, because such a sale is a form of a liquidation from the debtor's perspective.

"Restructuring plan"

A plan by which the financial well-being and viability of the debtor's business can be restored by maximizing the possible eventual return to creditors, which should provide a

[164] III-Committee on International Jurisdiction and Cooperation, *Prospective Model International Cross-border Insolvency Protocol* (Draft-Annotated, June 2009), Article 6.4.
[165] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".
[166] See the Proposal Restructuring Directive (2016), Article 2(2).

better result than if the debtor were to be liquidated. The restructuring plan should address operational, financial and strategic issues that provide evidence that the business can generate sufficient cash flow and profit to meet its obligations after implementation.[167]

"Safe harbour"

Safe is a term used to express that the assessment of a certain act or behaviour, although literally falling in the scope of a particular legislative provision is not to be regarded as violated or breached, with as a consequence that this act or behaviour will not result in liability, for instance in case of rules and sanctions for transaction avoidance. The safe harbour doctrine encompasses cases in which '… the Legislature has permitted certain conduct or considered a situation and concluded no action should lie'.[168]

"Sale as a going concern"

Sale as a going concern (or: sales on a going concern basis) is the sale or transfer of a business in whole or substantial part, as opposed to the sale of separate assets of the business. It is a form of liquidating the debtor's estate.

"Secondary Insolvency Proceedings"

The European Insolvency Regulation (2015) aims to protect the diversity of interests, for which reason secondary proceedings can be opened to run in parallel with the main proceedings. Secondary proceedings may be opened in the Member State where the debtor has an "establishment". See "establishment". The effects of secondary proceedings under the European Insolvency Regulation (2015) are limited to the assets located in that State. The major features of this concept in connection with main insolvency proceedings in the Regulation have been included above in the description of "Parallel Insolvency Proceedings". See also "(Foreign) non-main proceedings."[169]

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[167] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations", and Part II(IV), Point 3, ABA Asia-Pacific Informal Workout Guidelines for Promoting Corporate Restructuring in the Region and Model Agreement to Promote Corporate Restructuring (2013), "Achievable Business Plan", Commission's Recommendation (2014), Recital 16. From the Explanatory memorandum (p. 13) of the Proposal Restructuring Directive (2016): "A successful restructuring plan will turn non-performing loans into loans a company can actually pay back. In liquidation, secured creditors have to consider the possibility of substantial reduction in the value of their claims. In restructuring, on the other hand, insolvency is avoided, contract debts are in general paid, and negotiations concern in most cases only the financial debt. Data shows that the highest recovery rates for creditors are in economies where restructuring is the most common insolvency proceeding and that 45 % of OECD economies use restructuring as the most common way to save viable firms. They also have an average recovery rate of 83 cents on the dollar, versus 57 cents on the dollar in countries where liquidation is the prevalent outcome50. Another important factor to improve the overall recovery rates, and thus the residual value of potential non-performing loans, is the swift handling of restructuring and insolvency cases" (footnotes omitted).

[168] See *Cel-Tech Comms., Inc. v L.A. Cellular Tel. Co*., 20 Cal. 4th 163, 182 (Cal. 1999).

[169] UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations" provides for "secondary proceedings": "non-main proceedings conducted in European Member States under the EC Regulation".

"Shareholder loan"

A "shareholder loan" is a lending agreement between a company and (one of) its shareholders. While being valid, the repayment claim from such an arrangement may be subject to a subordination in case of an insolvency of the company under some national insolvency laws.

"Stakeholder"

A "stakeholder" is any person whose rights or interests are affected directly or indirectly by insolvency or restructuring proceedings which is why they may have to be involved under insolvency and restructuring laws.

"Stay"

A "stay" or a "stay of individual enforcement actions" means a temporary suspension of the right to enforce a claim (or supporting contractual rights to terminate or accelerate) by a creditor against a debtor, ordered by a judicial or administrative authority.[170] In the context of insolvency, the ALI NAFTA Principles establishes as a recommendation for legislation or international agreement that: "The NAFTA countries should provide that a bankruptcy case that is a main proceeding in any of them will produce an automatic stay under domestic law in all three countries."[171] The UNCITRAL Legislative Guide holds that a "Stay of proceedings" is a measure that prevents the commencement, or suspends the continuation, of judicial, administrative or other individual actions concerning the debtor's assets, rights, obligations or liabilities, including actions to make security interests effective against third parties or to enforce a security interest; and prevents execution against the assets of the insolvency estate, the termination of a contract with the debtor, and the transfer, encumbrance or other disposition of any assets or rights of the insolvency estate."[172]

"Subordinated creditor"

"Subordinated creditors" are creditors who would, either under contractual agreements or by insolvency law, only receive any distribution in insolvency proceedings after all other creditors were paid in full. See also "deferred creditors".

"Subordination"

Subordination means that a creditor or shareholder is not ranked equal with other holding a similar right in insolvency proceedings. Such unequal treatment requires a statutory or

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[170] Proposal Restructuring Directive (2016), Article 2(4).

[171] ALI NAFTA Principles (2003), Recommendation 2.

[172] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions". Ditto: UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".

contractual basis. In case of "shareholder loans", the principle of "equitable subordination" may suffice to subordinate a repayment claim from a shareholder loan as the arrangement is held to constitute a disguised capital contribution and is therefore subordinated to ordinary unsecured claims on this basis.[173]

"Super priority"

A "super priority" is a preference granted for "interim finance" or "new finance" in a restructuring plan or restructuring proceedings. Based on a court approval and adequate protection to impaired creditors, a fresh money lender would take priority with the repayment claims over other creditors or receive a first priority lien on an already encumbered asset of the estate.

"Supervisor"

A "supervisor" is any person who is appointed to oversee the activities of the debtor and takes the necessary measures to safeguard the legitimate interests of creditors and other interested parties.[174]

"Suspect period"

The "suspect period" is the period before a company or person enters formal insolvency proceedings. Transactions within such a period may be avoided.[175] A COMI shift within such a period may be disregarded.[176]

"Term"

"Term" means any provision, express or implied, of a contract or other juridical act, of a law, of a court order or of a legally binding usage or practice: it includes a condition.[177]

"Termination"

"Termination", in relation to an existing right, obligation or legal relationship, means bringing it to an end with prospective effect except in so far as otherwise provided.[178]

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[173] See also G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 449.
[174] See also G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization*, Cheltenham 2017, p. 451.
[175] See also G. McCormack, A. Keay & S. Brown, *European Insolvency Law reform and harmonization* (Cheltenham 2017), p. 451.
[176] See InsReg (2015), Article 3.
[177] DCFR Outline Edition (2009), Annex (Definitions), p. 568.
[178] DCFR Outline Edition (2009), Annex (Definitions), p. 568.

“Time of Opening of Proceedings”

The European Insolvency Regulation (2015) provides that "the time of the opening of proceedings" means the time at which the judgment opening insolvency proceedings becomes effective, regardless of whether it is a final judgment or not.[179]

“Unsecured creditor”

A creditor without a security interest.[180]

“Valid”

“Valid”, in relation to a juridical act or legal relationship, means that the act or relationship is not void and has not been voided.[181]

“Void”

“Void”, in relation to a juridical act or legal relationship, means that the act or relationship is automatically of no effect from the beginning.[182] “Voidable”, in relation to a juridical act or legal relationship, means that the act or relationship is subject to a defect which renders it liable to be avoided and hence rendered retrospectively of no effect.[183]

“Voluntary restructuring negotiations”

Negotiations that are not regulated by the insolvency law and generally will involve negotiations between the debtor and some or all of its creditors aiming at a consensual modification of the claims of participating creditors.[184] See also “workout”.

“Workout”

A “work-out” (sometimes private work-out or informal work-out) is the designation of an out-of-court (informal) privately arranged (with majority of involved stakeholders) restructuring or sales on a going-concern basis of all or substantially all of a company’s liabilities, laid down in an agreement when insolvency looms.[185]

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[179] EIR (2015), Article 2(8).
[180] UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”.
[181] DCFR Outline Edition (2009), Annex (Definitions), p. 569.
[182] DCFR Outline Edition (2009), Annex (Definitions), p. 569.
[183] DCFR Outline Edition (2009), Annex (Definitions), p. 569. The Concordat (1995), Glossary of terms, uses “Voiding rules”, for “Rules relating to voidness, voidability or enforce-ability of claims or pre-insolvency transactions.”
[184] UNCITRAL Legislative Guide (2004), para. 12, under B, “Glossary, Terms and definitions”.
[185] See also INSOL Internationa Workout Principles II (2017).

“Workout support proceedings”

“Workout support proceedings” are court proceedings that aim at finalising a restructuring agreement that was negotiated voluntarily and privately (“workout”), but did not find the support of all required creditors. Given the support of a significant majority of creditors, the debtor may initiate proceedings with the sole purpose of a plan confirmation which would give the plan effect to all creditors of the negotiations. As courts would not supervise the negotiations and voting process, such proceedings are often called “hybrid” proceedings, combining workout and formal restructuring elements.

INTRODUCTION

1. Overview

1. This is an Instrument of the European Law Institute on Rescue of Business in Insolvency Law. An ELI Instrument, developed and carried out under the auspices of the ELI, is the result of a medium-to long-term project, the added value of which is to provide, through the independence, excellence and diversity of its project team and the on-going critical guidance of a very broad constituency of jurists, well-founded solutions that have the support of the European legal community.

2. The objective of the project on 'Rescue of Business in Insolvency Law' (by those involved kindly referred to as Business Rescue Project) was to design (elements of) an appropriate legal enabling framework, which includes certain statutory procedures that encourage parties to negotiate rescue solutions in a situation of business distress. Such a framework would include rules to determine in which procedures and under which conditions an enforceable solution can be imposed upon creditors (including equity holders) despite their lack of consent.

3. The Business Rescue Project has produced four different outcomes:
- Inventory Reports on national insolvency laws of EU Member States;
- Inventory Report on International Recommendations from Standard-Setting Organisations;
- Normative Reports on the feasibility of a harmonised legal enabling framework for businesses in distress, and
- the present Report ('ELI Business Rescue Report'), providing a menu of recommendations and proposals for a legal framework aimed at supporting the rescue of a business in distress.

4. The final chapter of this ELI Business Rescue Report identifies a number of topics that, in our view, are ripe for further approximation or harmonisation across Europe. Unlike harmonisation or convergence of company law,[186] the approximation, including achieving greater coherence or harmonisation of insolvency laws is a rather new phenomenon in the European Union. However, during the six years after the European Parliament's 2011 call for harmonisation of certain matters relating to an EU corporate insolvency framework had broken an undiscussed taboo,[187] the European Commission has worked on approximation of

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[186] In the EU this is already ongoing for some three decades through regulations, directives, recommendations and corporate governance codes, and e.g. in July 2015 by a European Model Company Act (EMCA), available at http://law.au.dk/en/research/projects/european-model-company-act-emca/. For further background, see Marco Ventoruzzi, 'The New European Model Company Act', 14 October 2015, available at http://corpgov.law.harvard.edu/2015/10/14/the-new-european-model-company-act/.

[187] 'The H-word is out!' observed Bob Wessels, 'Harmonization of Insolvency Law in Europe', 8 European Company Law 2011, Issue 1, 27 et seq. See also Christoph G. Paulus, 'EuInsVO: Änderungen am Horizont und ihre Auswirkungen', Neue Zeitschrift für das Recht der Insolvenz und Sanierung (NZI) 2012, 297 et seq., qualifying the proposals of the European Parliament as carrying a *recht radikales Vereinheitlichungsbestreben*' (a clear ambition for radical unification). See also Motion for a European Parliament resolution with recommendations to the Commission on insolvency proceedings in the context of EU company law (2011/2006(INI) of 17 October 2011, available at

areas of insolvency law via several workstreams (see para. 2). Although 'harmonisation' sounded new,[188] actually the revisions of many EU Member States' laws during the last ten years had already suggested a certain degree of convergence in Member State rescue-oriented legislation. A study of Piekenbrock found that in England, Italy, France, Belgium, Germany and Austria several common tendencies in proceedings, which have the general aim of rescuing a company's business, could be observed. This development of non-deliberate, creeping convergence of laws relate in these countries to the possibility of (i) an earlier recourse (an earlier moment of starting a rescue process, compared to the moment of commencing formal insolvency proceedings), (ii) to have the management of the company not replaced by an insolvency administrator, but to stay in control of the business ('debtor in possession'), (iv) the possibility of a stay (or moratorium), either automatic, by operation of law, or at request, the possibility of a debt for equity swap (the conversion of a creditors claim into shares in the capital of the company), and (v) the mechanism of binding dissenting creditors to a rescue plan.[189] It is clear that '*… [t]he pace of insolvency law reform has been fast and even, at times, relentless*.'[190] Our Business Rescue Project aims at directing these efforts and energies to those topics that allow for further approximation without conflicting with major principles and values in national law traditions as well as international norms and standards.

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http://www.europarl.europa.eu/sides/getDoc.do?type=REPORT&reference=A7-2011-0355&format=XML&language=EN.

[188] On the proposals of the European Parliament, see Ian F. Fletcher and Bob Wessels, *Harmonisation of Insolvency Law in Europe, Reports presented to the Nederlandse Vereniging voor Burgerlijk Recht (Netherlands Association of Civil Law)* (Deventer: Kluwer 2012). The authors summarised their findings and presented their conclusions in a final chapter, which is published separately, see http://bobwessels.nl/wordpress/?attachment_id=2409.

[189] Andreas Piekenbrock, 'Das ESUG – fit für Europa?', NZI 22/2012, 906 et seq. The same author has presented the theme in a broader context with focus on Germany, as a continuous work in progress, see Andreas Piekenbrock, 'Das Insolvenzrecht zu Beginn des 21. Jahrhunderts: ein Dauerbaustelle', in Werner Ebke, Christopher Seagon, Michael Blatz (eds.), *Solvenz – Insolvenz – Resolvenz* (Baden-Baden: Nomos 2013), 79 et seq. See also M. Adalet McGowan and D. Andrews, *Insolvency Regimes And Productivity Growth: A Framework For Analysis* (OECD Economics Department Working Papers, No. 1309, OECD Publishing, Paris 2016), available at http://dx.doi.org/10.1787/5jlv2jqhxgq6-en. These authors present an analysis of the corporate and personal insolvency regimes of nearly all EU Member States in terms of their goals, optimal design (including trade-offs) and key features relevant for explaining cross-country differences in productivity. Although their paper proposes a strategy to obtain policy indicators that better capture cross-country differences in the key design features of corporate and personal insolvency regimes, with a view to facilitate further research on exit policies and productivity growth, their preliminary observation is (p. 19) that there has been some convergence across countries towards the US-style restructuring system over time and that the limited available evidence suggests that this has been associated with favourable outcomes. They refer to reforms in a number of European countries introducing some of the features conducive to successful restructuring have resulted in lower incidence of liquidations (the United Kingdom, Spain), shorter insolvency proceedings (Spain) and increased restructuring as a share of total insolvency related procedures and higher recovery rates (Italy), referring to Impact Assessment accompanying the document Commission Recommendation on a New Approach to Business Failure and Insolvency', 12.3.2014, SWD(2014) 61 final (hereafter "Impact Assessment (2014)").

[190] See Catherine Bridge, 'Insolvency – a second chance? Why modern insolvency laws seek to promote business rescue' Law in transition 2013, 28 et seq, mentioning (non-EU) changes in insolvency laws over the last five years in Albania, Kazakhstan, Moldava, Russia, Serbia and Ukraine. Harmonising continental European insolvency law therefore seems much less illusory as over a decade ago, as observed rightly by Eric Dirix, 'Het insolventierecht anno 2014', in H. Braekmans, E. Dirix, M.E. Storme, B. Tilleman en M. Vanmeenen (eds.), *Curatoren en vereffenaars: actuele ontwikkelingen III* (Antwerpen – Cambridge: Intersentia 2014), 3 et seq, at 7.

2. Background of the Report

2.1. Harmonisation efforts of the European Commission

5. Although the ELI projects started as an independent and general effort to design rescue solutions for situations of business distress, the Report supports efforts of the European Commission to further harmonise rescue-related insolvency law provisions in the laws of the EU Member States. Since 2012 the Commission has taken three determinative actions: (i) In 2014 the European Commission published a recommendation on '*A new European approach to business failure and insolvency*' (see para. 2.1.1). (ii) In 2015 the renewed (recasted) text of the European Insolvency Regulation (2015) was enacted (see para. 2.1.2), (iii) in the same year the Commission published its Green Paper on the establishment of a Capital Markets Union (CMU) followed, in September 2015, by its Action Plan (see para. 2.1.3) and a year later, in November 2016, the publication of a Proposal Restructuring Directive (2016) (see para. 2.1.4).[191]

2.1.1. Recommendation on A New European approach to business failure and insolvency

6. On 12 December 2012, the European Commission responded to the harmonisation challenge of the European Parliament and stated a new policy, named '*A new European approach to business failure and insolvency*' ('Recommendation'). The Commission, through identifying issues on which the new European approach to business failure and insolvency should focus, wishes: '*… to develop a rescue and recovery culture across the Member States*'. On 12 March 2014 the Commission issued its Recommendation on a new approach to business failure and insolvency, in it the Commission stated that many European restructuring frameworks '*… are still inflexible, costly and value destructive*'.[192]

7. The Recommendation has two major objectives. It aims to: '*… ensure that viable enterprises in financial difficulties, wherever they are located in the Union, have access to national insolvency frameworks which enable them to restructure at an early stage with a view to preventing their insolvency, and therefore maximise the total value to creditors, employees, owners and the economy as a whole. The Recommendation also aims at giving honest bankrupt entrepreneurs a second chance across the Union.*'[193] In order to achieve these aims, the Commission deemed it necessary to: '*… encourage greater coherence between the national insolvency frameworks in order to reduce divergences and inefficiencies which hamper the early restructuring of viable companies in financial difficulties and the possibility of a second chance for honest entrepreneurs, and thereby lower the cost of restructuring for both debtors and creditors. Greater coherence and increased efficiency in those national insolvency rules would maximise the returns to all types of creditors and investors and encourage cross-border investment. Greater coherence would also facilitate the restructuring of groups of companies irrespective of where the members of the group are*

[191] It should be disclosed that co-reporter Wessels served as an Expert, advising the European Commission in its preparation for the Comission's Recommendation (2014) and the Proposal Restructuring Directive (2016).
[192] See Impact Assessment (2014), p. 2.
[193] The European Commission emphasised the reduction of the 'stigma of bankruptcy' and a fresh start for (non-culpable) debtors, and more generally benchmarking well against international standards on consumer insolvency since 2002. For an overview, see Donna McKenzie Skene, 'Credit where Credit is Due: The Effect of Devolution on Insolvency Law in Scotland' 2013 1 NIBLeJ 5, 51 et seq.

located in the Union.'[194] As an aside, the Commission does not use the term 'harmonisation' in the text.

8. The Recommendation has in total 20 recitals and 36 recommendations.[195] In essence, it exhorts each EU Member State to establish a preventive insolvency framework that would provide for (i) early recourse, (ii) minimised court involvement, (iii) a debtor-in-possession model which ensures minimum disruption to the operations of the debtor and allows him to carry on his day-to-day operations, (iv) a court-ordered stay, (v) the ability to bind dissenting creditors to a restructuring plan, and (vi) certain protection for new finance.[196]

9. In a paper published in September 2015, the Commission presented some empirical support for their claim that efficient pre-insolvency frameworks play an important role in fostering a culture of early restructuring and second chances in EU Member States.[197]
The Commission's evaluation, eighteen months after the date of issuing the Recommendation, reveals that, although the Recommendation provided a useful focus for those Member States undertaking reforms in the area of insolvency, the implementation was only partial. The Recommendation had been taken up only to some extent by Member States. Among these were especially by those receiving insolvency recommendations in the context of the so-called European Semester and the Macroeconomic Imbalance Procedure, and also these states have been rather selective in taking up the Recommendation.[198]

10. The reception of the Recommendation by legal scholars in Europe has been rather mixed. The sheer possibility of approximation or harmonisation of insolvency laws is seriously doubted by some scholars. In some cases on subsidiarity-grounds, in other instances by expressing doubts about the extent of the benefits of any harmonisation,[199] the unrealistic nature – given the many differences in national insolvency systems – of the prescribed principles[200] or the pace of the Recommendation's envisaged execution (the 'high

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[194] See Recitals 1 and 11 of the Commission's Recommendation (2014) respectively.

[195] Commission's Recommendation (2014). For an overview, see Stephan Madaus, 'The EU Recommendation on Business Rescue – Only Another Statement or a Cause for Legislative Action Across Europe?', 27 Insolvency Intelligence 2014, no. 6, 81 et seq.; Bob Wessels, 'Rescue on the rise' eurofenix Autumn 2014, p. 12-15; E. Schmieman, 'De aanbeveling van de Europese Commissie inzake een nieuwe aanpak van faillissement en insolventie', Ondernemingsrecht 2014/77, 369 et seq.; A.M. Mennens and P.M. Veder, 'Clementie en recht: het dwangakkoord buiten insolventie', NTBR 2015/2. Uwe Goetker and Benedikt Schultz, 'Vorinsolvenzliches Sanierungsverfahren – Warum braucht die Praxis ein solches und wie könnte es aussehen', ZIP 44/2016, 2095 et seq.; N.W.A. Tollenaar, *Het pre-insolventieakkoord. Grondslagen en raamwerk* (PhD, Groningen 2016), Chapter 9.

[196] For an analysis see Kristin van Zwieten, 'Restructuring law: recommendations from the European Commission', Law in Transition *online* (EBRD publication), 2015.

[197] See Mihaela Carpus Carcea, Daria Ciriaci, Carlos Cuerpo Caballero, Dimitri Lorenzani and Peter Pontuch, 'The Economic Impact of Rescue and Recovery Frameworks in the EU', European Economy Discussion Paper 004, September 2015, available at http://ec.europa.eu/economy_finance/publications/eedp/index_en.htm.

[198] Directorate-General Justice & Consumers of the European Commission, 'Evaluation of the implementation of the Commission Recommendation of 12.3.2014 on a new approach to business failure and insolvency', 30 September 2015.

[199] Adrian Cohen and Gabrielle Ruiz, 'Living in perfect harmony? A new European approach to business failure and insolvency', 6 Corporate Rescue and Insolvency 2013, 151 et seq.

[200] Alan Bennett, 'To harmonise or not to harmonise, that's the question' 8 Corporate Rescue and Insolvency 2015, 98 et seq.

degree of impatience' the Commission demonstrates).[201] Other scholars, on the contrary, generally adhere or support the Recommendation and explain how existing drafts of legislation for reviewing national laws are generally in line with it[202] or how existing already recently renewed legislation should be improved by the topics addressed in the Recommendation, e.g. in Germany,[203] France,[204] and – later – in the United Kingdom.[205] Others support the Recommendation, but like Eidenmüller,[206] regret that the harmonisation effort is limited, leaving too much room for residual diversity in EU Member States, a lack of definitions on key concepts,[207] or express concern over certain requirements that have been recommended by the Commission.[208]

11. In June 2016, in a macroeconomic study,[209] the following reform priorities from an economic perspective were drawn:

[201] Christoph Paulus, 'Europeanisation of the Member States' Insolvency Laws' 3 NIBLeJ 2015, p. 17.

[202] For the Netherlands regarding the programme of recalibration ('*herijking*') in the insolvency legislation, see E. Schmieman, 'De aanbeveling van de Europese Commissie inzake een nieuwe aanpak van faillissement en insolventie' Ondernemingsrecht 2014/77, p. 369 et seq.

[203] Sacha Lürken, 'Not so dead yet – A fresh impetus from Brussels for a pre-insolvency restructuring procedure' 6 International Insolvency Law Review 3/2015, p. 224 et seq.

[204] Reinhard Dammann et Francois-Xavier Lucas, 'Faut-il déjà réformer la réforme du 12 mars 2014'Bulletin Joly Entreprises en difficulté, May-June 2014, p. 1 et seq.

[205] UK Insolvency Service, A Review of the Corporate Insolvency Framework. A consultation on options for reform (May 2016), available at https://www.gov.uk/government/consultations/a-review-of-the-corporate-insolvency-framework. For a critique (in 2 parts), 14 and 15 June 2016, see Jennifer Payne,'New UK Debt Restructuring Regime Critique Insolvency Service' (Oxford Business Law Blog 2016), available at https://www.law.ox.ac.uk/business-law-blog/blog/2016/06/new-uk-debt-restructuring-regime-critique-insolvency-service.

[206] Horst Eidenmüller, 'Die Restrukturierungsempfehlung der EU-Kommission und das deutsche Restructurierungsrecht', KTS 2014, p. 401 et seq, also available at http://ssrn.com/abstract=2519010; Horst Eidenmüller, 'A New Framework for Business Restructuring in Europe: the EU Commission's Proposals for a Reform of the European Insolvency Regulation and Beyond', ECGI Law Working Paper No. 199, 2013, available at http://ssrn.com/abstract=2230690.

[207] Such as 'framework', 'viable enterprises in financial difficulties', 'honest entrepeneur', 'fraud, evasion or abuse', 'likelihood of insolvency', to mention a few.

[208] Horst Eidenmüller and Kristin van Zwieten, 'Restructuring the European Business Enterprise: The EU Commission on a New Approach to Business Failure and Insolvency', European Corporate Governance Institute (ECGI) - Law Working Paper No. 301, 2015; Oxford Legal Studies Research Paper No. 52/2015, available at http://ssrn.com/abstract=2662213. In Germany in 2016 a pragmatic approach has been chosen: the pre-insolvency proceeding will arrive, see Gottwald, 'NZI Editorial', Heft 18/2016. The lack of such proceedings has led to discussion on how to best draft this figure, see Uwe Goetker and Benedikt Schultz, 'Vorinsolvenzliches Sanierungsverfahren – Warum braucht die Praxis ein solches und wie könnte es aussehen', ZIP 44/2016, 2095 et seq., and the 'Grundsätze eines Vorinsolvenzlichen Sanierungsverfahren' (Principles for a pre-insolvency proceeding), of VID, an insolvency practititoners asssotiation. The present situation will only strengthen a crisis, thus Volker Beissenhirtz, 'Bedingt sanierungsbereit. Restructuring, sanierung und Insolvenzverwaltung', ZInsO 36/2016, 1778 et seq.

For proposals to amend a pending draft in legislation in the Netherlands, see N.W.A. Tollenaar, *Het pre-insolventieakkoord. Grondslagen en raamwerk* (PhD Groningen 2016), Chapter 9. See also Juana Pulgar Ezquerra, 'Corporate Restructuring: The European Recommendation and the Spanish Model', i: Rebecca Parry and Paul Omar (eds.), *Reimagining Rescue* (INSOL Europe, Nottingham Paris 2016), p. 119-138.

[209] Jean-Charles Briconge, Maria Demertzis, Peter Pontuch and Allessadro Turrini, 'Macro Relevance on Insolvency Frameworks in a High-debt Context: An EU Perspective' European Economy Discussion Paper 032, June 2016.

1. Countries where reforms are primarily motivated by the need to address the debt overhang and where early restructuring possibilities exist should (i) complete their recent reforms, monitoring the outcomes and assess the effectiveness of the reforms both quantitatively and qualitatively and identify any malfunctioning or weaknesses in the system that need to be addressed[210], (ii) in already planned or on-going broad reforms, the design of a new system should reflect broad economic principles and international best practices.[211]

2. Reforms could aim at enhancing institutional frameworks to ensure an efficient functioning of insolvency procedures and to make the 'institutional settings' for insolvency more efficient, e.g. by increasing court capacity and creating specialised in-court resources for insolvency cases. Skills of extrajudicial practitioners should be enhanced. The study concludes that their performance should be subject to supervision and monitoring and that their remuneration should be designed to strengthen the incentives for swift resolution. In parallel, the quality and availability of information about debtors (liabilities, assets, and income) should be improved in such a way to ensure proper functioning of the insolvency frameworks in place.

3. The study notes, under reference to the Recommendation, that progress seems possible for what concerns the modernization of relevant features of insolvency frameworks, notably in terms of dealing with debt distress at an early stage and providing for a possibility of a genuine fresh start: 'However, even those Member States which have taken up the European Commission Recommendation did so in a selective manner, meaning that differences remain quite pervasive.'

4. More generally, the study notes, progress could be achieved over time in terms of reducing large asymmetries in insolvency frameworks across EU countries, with a view to fostering cross-border investment within the framework of Capital Markets Union.

See with regard to 'Capital Markets Union', para. 2.1.3 below.

2.1.2. European Insolvency Regulation (2015)

12. The second action from the Commission results from the legislative process that started on the basis of Article 46 of the European Insolvency Regulation (EC) No 1346/2000 ('EIR (2000)' or 'European Insolvency Regulation (2000)'), in legal force since May 2002.[212] Article

[210] The study mentions that several countries received recommendations aimed at ensuring the effectiveness of recent reforms as part of the program conditionalities, post-program surveillance or in the context of the European Semester, including Croatia, Cyprus, Ireland, Portugal and Spain.

[211] Mentioning some of the best practices we have studied in relation to our report, see para. 3.1.4. A third point within this priority is to accompany recent reforms with adequate flanking policies to make the existing insolvency framework effective in resolving debt (mainly in the financial sector to ensure a speedy resolution of high stocks of non performing loans (NPLs)). See Günther M. Bredow et al, 'NPL-Verkäufe von insolvenzforderungen in der Praxis' NZI 4/2017, 89 et seq.

[212] See Council Regulation (EC) 1346/2000 of 29 May 2000 on insolvency proceedings, OJ L 160 of 30 June 2000. It should be mentioned that the European Insolvency Regulation (2000) itself and its accompanying Annexes have been amended seven times, and that Croatia, through its accession, has been included in the Annexes of

46 of the EIR (2000) obliges the European Commission to present to the European Parliament, the Council and the Economic and Social Committee *'… a report on the application of this Regulation*'.[213] Article 46 EIR (2000) furthermore requires that the report '… *shall be accompanied if need be by a proposal for adaptation of this Regulation*.' The Commission's proposal of 12 December 2012[214] is based on said report, together with discussions and consultations with a group of experts and an appraisal of the effects on existing EU policy.[215] The existing EIR (2000) will be repealed on the day of the entry into force of the European Insolvency Regulation (2015) ('EIR (2015)'), which is 26 June 2017, see Article 92 EIR (2015) ('Entry into force').

13. In the area of business rescue it is worth mentioning[216] that the EIR (2015) has broadened the European Insolvency Regulation (2000)'s scope beyond the typical insolvency liquidation proceedings. The new rules also cover, e.g. (i) proceedings which provide for the restructuring of a debtor at a stage where there is only a likelihood of insolvency, (ii) proceedings which leave the debtor fully or partially in control of his assets and affairs, and (iii) proceedings providing for a debt discharge or a debt adjustment of consumers and self-employed persons.[217] The result of the Recommendation of 12 March 2014 is supposed to dovetail with the application of the EIR (2015). As explained, one of the amendments to the EIR (2000) is the widening of its scope, to include certain debtor-in-possession and pre-insolvency procedures. The 'preventive restructuring framework' drafted in national insolvency systems will, in general when they are in line with the Commission's

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the EIR, these were most recently amended with the Council Implementing Regulation (EU) 663/2014 of 5 June 2014, replacing Annexes A, B and C to Regulation (EC) No 1346/2000 on insolvency proceedings, OJ L179/4 see http://eur-lex.europa.eu/legal-content/EL/TXT/PDF/?uri=OJ:L:2014:179:FULL&from=GA. A 2016 proposal is pending to update the Annexes once more, see COM(2016) 366 final. Denmark is not bound by the European Insolvency Regulation (2000) and EIR (2015) (see Recital 33 EIR (2000) and Recital 88 EIR (2015)).

[213] This report is commonly referred to as the Heidelberg-Luxembourg-Vienna Report, a title which reflects to involved (professors of the) universities as principle drafters, see http://ec.europa.eu/justice/civil/files/evaluation_insolvency_en.pdf. Separately published as: Burckhart Hess, Paul Oberhammer and Thomas Pfeiffer, European Insolvency Law, *The Heidelberg-Luxembourg-Vienna Report* (C.H. Beck – Hart – Nomos 2014).

[214] European Commission, Proposal for a Regulation of the European Parliament and of the Council Amending Council Regulation (EC), No. 1346/2000 on Insolvency Proceedings, COM(2012) 744 final.

[215] Commission Staff Working Document, Impact Assessment, Accompanying the document Revision of Regulation (EC) No 1346/2000 on insolvency proceedings, SWD(2012) 416 final, see http://ec.europa.eu/justice/civil/files/insolvency-ia_en.pdf.

[216] In addition, the EIR (2015) clarifies the rules of international jurisdiction of courts of the EU Member States for opening insolvency proceedings, this includes a large number of rules on cooperation and communication between the actors involved in the insolvency proceedings pending in two or more EU Member States (such as insolvency practitioners and courts), among others Articles 41-44 EIR (2015). These states will also be required to publish relevant information in cross-border insolvency cases in a publicly accessible electronic register, which should improve the information of creditors and courts involved. These registers will be interconnected via the e-Justice portal to facilitate access to that information for creditors and courts located in other EU Member States. The EIR (2015) also introduces a set of procedural rules aimed at ensuring the efficient administration of insolvency proceedings relating to different companies forming (a part of) a group of companies. On a voluntary basis, it is possible to appoint of a 'group coordinator', whose recommendations are not binding on the other insolvency practitioners.

[217] The process of recalibration of insolvency in the Netherlands will lead to a legislative regime for 'pre-pack proceedings', which will also be covered by the wider scope of the EIR (2015). For the UK this will mean that company voluntary arrangements (CVAs) will be included, however not schemes of arrangement. These new possibilities have, however, not led to a change of the title, being Regulation on 'insolvency proceedings'.

Recommendation, be also within the scope of the EIR (2015). The system of the EIR (2015) governing jurisdiction to open proceedings, and the effect of proceedings once opened will therefore apply to these restructuring procedures.[218]

14. Over a decade ago, in May 2002, when the EIR (2000) came into effect, it expressly stated – in Recital 11 EIR (2000) – that it is based on the acknowledgment of '*… the fact that as a result of widely differing substantive laws it is not practical to introduce insolvency proceedings with universal scope in the entire Community*.'[219] The Recital continues: '*… The application without exception of the law of the State of opening of proceedings would, against this background, frequently lead to difficulties. This applies, for example, to the widely differing laws on security interests to be found in the Community. Furthermore, the preferential rights enjoyed by some creditors in the insolvency proceedings are, in some cases, completely different*.'[220] Meanwhile it has been submitted that the 'chaos' of preferential rights and securities should be dealt with on a European level,[221] an invitation that has not yet been responded to.

15. It should nevertheless be mentioned that several provisions of the European Insolvency Regulation (2000) can be characterized as substantive rules and are therefore now accepted throughout the Union as unified rules concerning the topics to which they relate, see for example Articles 7(2) (retention of title in case of insolvency of the seller of an asset), 20 (return and imputation), 29-35 (several rules regarding secondary proceedings), 39 (right to

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[218] Horst Eidenmüller and Kristin van Zwieten have submitted that a restructuring proceeding as proposed in the Commission's Recommendation (2014) would not necessarily be within the scope of the EIR (2015), see Horst Eidenmüller and Kristin van Zwieten, 'Restructuring the European Business Enterprise: The EU Commission on a New Approach to Business Failure and Insolvency', European Corporate Governance Institute (ECGI) - Law Working Paper No. 301, 2015; Oxford Legal Studies Research Paper No. 52/2015, available at http://ssrn.com/abstract=2662213

[219] In the English, French, German and Dutch versions the recital refers to 'insolvency proceedings' and not to *eines einheitlichen Insolvenzrechts* (in the Dutch version: *een uniform insolventierecht*), meaning 'a uniform insolvency law', as Advocate General Kokott in her Opinion of 24 May 2012, Case C-116/11 (C-116/11 *Bank Handlowy and Ryszard Adamiak v Christianapol sp.z. o.o*. EU:C:2012:739) seems to suggest.

[220] This observation has direct historic roots in a comparative survey (of domestic laws of the original six EU Member States of the EC at that time) conducted by the Dutch professor Sauveplanne, published in October 1963 as EEC Commission Doc 8838/IV/63-E. For a recent application, see CJEU 7 October 2015, EU:T:2015:756 (*Accorinti/ECB*), in which the position '*… that the Principles Consultative Group (PCG) proposed, in its 2010 report 'Principles for Stable Capital Flows and Fair Debt Restructuring in Emerging Markets', as regards the 'emerging markets', that the application of the pari passu clause should be recognised internationally has no relevance to the existence of such a rule in the legal order of the European Union. Nor does it avail the applicants to refer to Council Regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings (OJ 2000 L 160, p. 1). On the contrary, that regulation noted the existence of widely differing arrangements in that respect in the national legal orders, including the preferential treatment of creditors (recital 11 of that regulation) and merely established uniform rules on conflict of laws for the purpose, in particular, of coordinating the distribution of the proceeds of the realisation of assets in order to preserve as much as possible the equal treatment of creditors (recitals 21 and 23 of that regulation).*

100 Incidentally, in so far as a rule which imposed the pari passu principle would entail equal treatment for creditors without taking into account the distinct situations of, in particular, private investors, on the one hand, and the Eurosystem central banks, acting in the exercise of their tasks pursuant to Article 127 TFEU and Article 18 of the Statute, on the other hand, the recognition of such a rule in the EU legal order might well be incompatible with the principle of equal treatment, as referred to in paragraph 87 above.'

[221] See A. Piekenbrock, 'Insolvenzprivilegien im deutschen, ausländischen und europäischen Recht', p. 122 Zeitschrift für Zivilprozess 2009-1, 63 et seq., who presents a comparative overview. See also: Paul Omar, 'The challenge of diverse priority rules in European insolvency laws' eurofenix Autumn 2011, 32 et seq.

lodge claims) and 40 (duty to inform creditors) EIR (2000). Under the EIR (2015) it will be possible that a court seized with a request to open secondary proceedings is able to postpone or refuse the opening of such proceedings, e.g. in the event that the insolvency practitioner appointed in the main proceedings promises the local creditors in another EU Member State that they would be treated in the main proceedings as if secondary proceedings had been opened and that the rights they would have had in such a case with respect to the determination and ranking of their claims would be respected in the distribution of the assets. Since such a practice was not possible under the law of many EU Member States, a rule of substantive law has been introduced enabling the insolvency practitioner to give such an 'undertaking' to local creditors in another EU Member State, with binding effect on the estate.[222]

2.1.3. Establishing a Capital Markets Union

16. A third action by the European Commission was announced on 18 February 2015, when the Commission launched a landmark project to '*… unlock funding for Europe's businesses and to boost growth in the EU's 28 Member States with the creation of a true single market for capital.*' The idea is that such a Capital Markets Union (CMU) aims to break down the barriers that are blocking cross-border investments in the EU and preventing businesses from getting access to finance. Unlike in other parts in the world, in Europe businesses remain heavily reliant on banks and relatively less on capital markets. With the CMU, the Commission also wants to clear obstacles that are preventing those who need financing from reaching investors and make the system for channelling those funds as efficient as possible. In the Commission Staff Working Document on Initial Reflections on the Impediments to the Development of Deep and Integrated EU Capital Markets it is stated that 'insolvency frameworks' and the effectiveness and enforcement of contract law continue to differ significantly across EU Member States, despite ongoing efforts to improve the efficiency of European insolvency and restructuring procedures: '*… The considerable differences in the insolvency laws of Member States create additional costs for foreign investors to assess the risk properly and thus hamper the emergence of pan-European credit markets. In particular, the lack or inadequacy of rules enabling early debt restructuring in many Member States, the absence of provisions to give a second chance for entrepreneurs and the length and costs of formal insolvency proceedings in many Member States lead to low recovery rates for creditors and discourage investors who either hold back from investing or do so only at a higher premium.*' In its plan the Commission regards the implementation of the Recommendation of 12 March 2014 on a new approach to business failure and insolvency only as '*… a first step*', as the Recommendation '*… does not touch upon the main bulk of the insolvency law, namely formal insolvency proceedings which end in the liquidation of the debtor and the distribution of the proceeds to creditors.*'[223]

[222] The English practice of such 'synthetic secondary proceedings' has been codified in Article 38 EIR (2015).

[223] The Commission continues: '*Yet for most debtors formal insolvency proceedings are the only and best solution, and investors need to have confidence that, in the event of an insolvency, they will recover their claims or at least a high percentage of those claims. However, the differences between the Member States' laws and practices in the field of insolvency – which have developed so far outside any Union involvement – are significant. Minimum standards in this area would ensure that investors have greater clarity and predictability when it comes to the substantive insolvency rules affecting their claims. As a measure of the effectiveness of insolvency laws, proceedings should also be relatively short (e.g. maximum 2 years), cost-effective and transparent, and thereby capable of yielding higher returns to creditors. As long as insolvency law remains*

17. In September 2015 the Commission announced in an Action Plan that it would propose a legislative initiative on business insolvency, including early restructuring and second chance, drawing on the experience of the Commission's Recommendation (2014). It added to the Recommendation's aims, mentioned earlier, a new one, namely '*The initiative will seek to address the most important barriers to the free flow of capital, building on national regimes that work well*'. In other words, the Commission's focus here was on ensuring that insolvency laws would be drafted in a way that would make it much easier for investors to assess credit risk, particularly regarding cross-border investments.[224]

2.1.4. Proposal for a Restructuring Directive (2016)

18. In November 2016, the Commission presented its 'Proposal for a Directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU' ("Proposal Restructuring Directive (2016)").[225]

Recital 1 of the Proposal Restructuring Directive (2016) sets out its goal: 'The objective of this Directive is to remove obstacles to the exercise of fundamental freedoms, such as the free movement of capital and freedom of establishment, which result from differences between national laws and procedures on preventive restructuring, insolvency and second chance. This Directive aims at removing such obstacles by ensuring that viable enterprises in financial difficulties have access to effective national preventive restructuring frameworks which enable them to continue operating; that honest over indebted entrepreneurs have a second chance after a full discharge of debt after a reasonable period of time; and that the

national in character, it will be difficult for investors to assess the risks they assume when investing in securities issued in other jurisdictions. This is harmful as regards cross-border investments in secured securities, but also detrimental when it comes to unsecured debt (e.g. high yield bonds), which carries as a result a much higher risk in case of default. A more harmonised and efficient insolvency law would increase the recovery rates for creditors (bad debt loss in the EU was estimated at €350 billion in 2013) and thus encourage investment.' See para. 3.7.4 (footnotes omitted) in the Working Document. For related documents, see http://ec.europa.eu/finance/capital-markets-union/index_en.htm. In the 'Five Presidents Report - plans to strengthen Economic and Monetary Union' as of 1 July 2015, available at http://www.eubusiness.com/topics/finance/5-presidents/, concrete measures have been published to create '*… a deep and genuine EMU [which] would provide a stable and prosperous place for all citizens of the EU Member States that share the single currency, attractive for other EU Member States to join if they are ready to do so*'. Again, in this Report, the national insolvency frameworks are regarded as an obstacle to create a CMU.

[224] The Commission stated in this respect: '*… Convergence of insolvency and restructuring proceedings would facilitate greater legal certainty for cross-border investors and encourage the timely restructuring of viable companies in financial distress. Consultation respondents broadly agreed that both the inefficiency and divergence of insolvency laws make it harder for investors to assess credit risk, particularly in cross-border investments*.' For the Action Plan, see COM(2015) 468 final, http://ec.europa.eu/finance/capital-markets-union/docs/building-cmu-action-plan_en.pdf. For a survey, see Diego Valiante, *Europe's Untapped Capital market: Rethinking financial integration after the crisis* (CEPS Paperback, London: Rowman & Littlefield International 2016). Hopt observes that the creation of a CMU will be long-lasting and complex, however necessary, see Editorial Europäische Zeitschrift für Wirtschaftrecht 8/2015. In a similar vein Marie Luise Graf-Schlicker, 'Der Aktionsplan zur Schaffung einer Kapitalsmarktunion' ZIP 22/2016 (Beilage Festschrift Katherine Knaut).

[225] See (COM)(2016) 723 final ('Restructuring Directive). See for all related documents http://ec.europa.eu/newsroom/just/item-detail.cfm?item_id=50043.

effectiveness of restructuring, insolvency and discharge procedures is improved, in particular with a view to shortening their length.' We observe that this objective amalgamates the objectives expressed in the Recommendation of March 2014 and the CMU Action Plan of September 2015.

19. The Proposal Restructuring Directive (2016) contains an Explanatory Memorandum (23 pages) and the text with 47 recitals and 36 Articles.[226] In contrast, the earlier Recommendation had a total of 20 recitals and 36 recommendations.[227] The proposal is based on seven '… key principles to ensure insolvency and restructuring frameworks are consistent and efficient throughout the EU: (i) companies in financial difficulties, especially SMEs, will have access to early warning tools to detect a deteriorating business situation and ensure restructuring at an early stage, (ii) flexible preventive restructuring frameworks will simplify lengthy, complex and costly court proceedings. Where necessary, national courts must be involved to safeguard the interests of stakeholders, (iii) the debtor will benefit from a time-limited 'breathing space' (or: stay) of a maximum of four months from enforcement action in order to facilitate negotiations and successful restructuring, (iv) dissenting minority creditors and shareholders will not be able to block restructuring plans but their legitimate interests will be safeguarded, (v) new financing will be specifically protected increasing the chances of a successful restructuring, (vi) throughout the preventive restructuring procedures, workers will enjoy full labour law protection in accordance with the existing EU legislation, and (vii) training, specialisation of practitioners and courts, and the use of technology (e.g. online filing of claims, notifications to creditors) will improve the efficiency and length of insolvency, restructuring and second chance procedures.[228]

2.2. A global dimension

20. Doing business is a fundamental part of taking part in (the global) society. As with businesses themselves, having the ability to operate, trade or invest all over the world, research on matters of business rescue cannot be limited to the European Union (or within it its Eurozone). The European Commission's general aim to have established insolvency frameworks for stimulating economic growth and employment finds it endorsement in a statement of the General Assembly of the United Nations, issued in 2012, reaffirming its commitment to the rule of law: '*8. We recognize the importance of fair, stable and*

[226] It enters into force 20 days after publishing in the Official Journal of the EU, and Member States (Article 34) shall implement '… the laws, regulations and administrative provisions necessary to comply with this Directive' two years from the date of entry into force'.

[227] Commission's Recommendation (2014). For an overview, see Stephan Madaus, 'The EU Recommendation on Business Rescue – Only Another Statement or a Cause for Legislative Action Across Europe?', 27 Insolvency Intelligence 2014, no. 6, p. 81 et seq.; Bob Wessels, 'Rescue on the rise' eurofenix Autumn 2014, p. 12-15; E. Schmieman, '*De aanbeveling van de Europese Commissie inzake een nieuwe aanpak van faillissement en insolventie*', Ondernemingsrecht 2014/77, p. 369 et seq.; A.M. Mennens and P.M. Veder, Clementie en recht: het dwangakkoord buiten insolventie' NTBR 2015/2. Uwe Goetker and Benedikt Schultz, 'Vorinsolvenzliches Sanierungsverfahren – Warum braucht die Praxis ein solches und wie könnte es aussehen' ZIP 44/2016, 2095 et seq.; N.W.A. Tollenaar, *Het pre-insolventieakkoord. Grondslagen en raamwerk*, (PhD Groningen 2016), Chapter 9.

[228] This overview is taken from the press release. In general the proposal has been welcomed, see Jack Barton, 'Experts in harmony over strengths of proposed EU directive', Global Restructuring Review, 29 November 2016, available at http://globalrestructuringreview.com/article/1078233/experts-in-harmony-over-strengths-of-proposed-eu-directive.

predictable legal frameworks for generating inclusive, sustainable and equitable development, economic growth and employment, generating investment and facilitating entrepreneurship, and in this regard we commend the work of the United Nations Commission on International Trade Law in modernizing and harmonizing international trade law.'[229]

21. On a global level, it has been recognised that the many differences between national insolvency systems '*… hamper the rescue of financially troubled businesses, are not conducive to a fair and efficient administration of cross-border insolvencies, impede the protection of the assets of the insolvent debtor against dissipation and hinder maximization of the value of those assets. Moreover, the absence of predictability in the handling of cross-border insolvency cases impedes capital flow and is a disincentive to cross-border investment …*'.[230] This view also forms the foundation for the creation of the UNCITRAL Model Law on Cross-border Insolvency.[231]

Another UNCITRAL work is the Legislative Guide on Insolvency Law ('Legislative Guide') of which parts one and two were published in 2004.[232] The purpose of the Legislative Guide is to assist the establishment of an efficient and effective legal framework to address the financial difficulty of debtors. The Legislative Guide is intended to be used by national authorities and legislative bodies as a non-binding reference when preparing new laws and regulations or reviewing the adequacy of existing laws and regulations.

22. In 2015, based on an assessment according to the World Bank Principles and Guidelines for Effective Insolvency and Creditor Rights Systems (introduced in 2001 and have since been revised multiple times)[233] and the UNCITRAL Legislative Guide on Insolvency Law, the World Bank published its Regional Profile 2015 for the European Union.[234] This Profile strongly speaks out for a robust national bankruptcy system, which functions as a filter, '*… ensuring the survival of economically efficient companies and reallocating the resources of inefficient ones. Fast and cheap insolvency proceedings result in the speedy return of businesses to normal operation and increase returns to creditors. By improving the expectations of creditors and debtors about the outcome of insolvency proceedings, well-functioning*

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[229] See Declaration of the High-level Meeting of the General Assembly of the U.N. at the National and International Levels, Sixty-seventh session, Resolution adopted by the General Assembly on 24 September 2012, A/RES/67/1.

[230] UNCITRAL Legislative Guide (2014), at. p. 13.

[231] See UNCITRAL Guide to Enactment and Interpretation (2013), nr. 5. The UNCITRAL Model Law (1997), is presently is applied in close to forty countries, including Australia, Japan, USA, and the Central-African States, forming OHADA (*Organisation pour l'Harmonisation en Afrique de Droits des Affaires* or Organisation for the Harmonization of Business Law in Africa) and in Europe, in Greece, Poland, Romania, Slovenia and the UK.

[232] Following parts one and two of the Legislative Guide, in 2010 the third part on the treatment of enterprise groups insolvency was presented, and a fourth part in 2013 on directors' obligations in the period approaching insolvency. See Bob Wessels and Gert-Jan Boon, *Cross-Border Insolvency Law, International Instruments and Commentary*, (2nd Ed., Alphen aan den Rijn: Kluwer Law International 2015), at p. 12 and 13.

[233] Latest revisions were incorporated in 2011 and 2015, see Bob Wessels and Gert-Jan Boon, *Cross-Border Insolvency Law*, *International Instruments and Commentary*, (2nd Ed, Alphen aan den Rijn: Kluwer Law International 2015), at p. 1.

[234] See World Bank Doing Business Report (2015), available at http://www.doingbusiness.org/Reports/~/media/GIAWB/Doing%20Business/Documents/Profiles/Regional/DB2015/DB15-European-Union.pdf.

insolvency systems can facilitate access to finance, save more viable businesses and thereby improve growth and sustainability in the economy overall'.[235]

23. It is widely acknowledged that Chapter 11 U.S. Bankruptcy Code, introduced in 1978, has been a source of inspiration for many legislators, both in Europe and beyond. In the USA, several changes in the business environment have led to proposals for reform of Chapter 11. There are several reasons for a critical look at Chapter 11. Since the U.S. Bankruptcy Code's enactment in 1978, there has been a significant increase in the use of secured credit, placing secured debt at all levels of the capital structure. Chapter 11, furthermore, assumes the presence of asset value above the secured debt, but asset value is often not present in many of today's Chapter 11 cases. The debt and capital structures of most U.S. debtor companies have grown much more complex, with multiple levels of secured and unsecured debt, often governed by equally complex inter-creditor agreements. Also, the market in the USA has changed. It is acknowledged that the growth of distressed debt markets, with the introduction of other types of lenders (hedge funds, often unregulated investors) and claims trading (without a court's involvement),[236] introduced another factor which was absent when in 1978 Chapter 11 was enacted. The nature of businesses has changed: Chapter 11 was developed in an era when the biggest employers were manufacturers with domestic operations. Today, many of the biggest employers are service companies, such as Amazon, Apple, Facebook and Google. Many of the remaining American manufacturers are less dependent on hard assets, and more dependent on contracts and intellectual property as principal assets.[237] The U.S. Bankruptcy Code does not clearly provide for the treatment of such assets and affected counterparties. Finally, the last decade demonstrated an increased focus on acquiring control over a distressed business through a sales process, where the original function of Chapter 11 (the company's rehabilitation) has evolved in merging businesses or sales of the debtor's assets. One could say that the reorganisation process of Chapter 11 has become a sophisticated M&A transaction practice.[238] And of course, debtors are much more often multinational companies than 30 years ago, with the means of production and other operations offshore, constituting international law and choice of law implications. These developments have called for a fresh assessment of the purposes and goals of a U.S. restructuring regime in the US, which has been undertaken by a special Commission of the American Bankruptcy Institute (ABI). Following an extensive study of twelve topics,[239] the Commission's report was published in December 2014.[240]

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[235] See also José M. Garrido, *Out-of-Court Debt Restructuring, A World Bank Study*, (Washington: International Bank for Reconstruction and Development / International Development Association or The World Bank 2012), who presents and analyses the lessons learned by the staff of the World Bank about the use of out-of-court debt restructuring mechanisms in addressing the problem of corporate distress.

[236] Also termed 'debt trading', in which debt is traded as a commodity and its owners will have different intentions and objectives then the original creditors.

[237] Bo Xie, '*Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue (*Edward Elgar Publishing 2016), 7, notes that the basis of the modern economy has transformed from the traditional manufactoring activity to the information-based economy, in which the most valuable resource may be human capital and relationship networks.

[238] See Douglas G. Baird and Robert K. Rasmussen, 'The End of Bankruptcy', 55 Stanfort Law Review 2002, 751 et seq. More recently: G. Ray Warner, 'Reimagining Rescue: The View from the United States', in Rebecca Parry and Paul Omar (eds.), *Reimagining Rescue*, (INSOL Europe, Nottingham Paris 2016), p. 175-186; Mark J. Roe, 'Three Ages of Bankruptcy', 18 November 2016, available at https://ssrn.com/abstract=2871625.

[239] These topics were: (1) Financing Chapter 11, (2) Governance and Supervision of Chapter 11 Cases and Companies, (3) Multiple Enterprise Cases/Issues, (4) Financial Contracts, Derivatives and Safe Harbours, (5)

24. In this study for the ELI we have compared the items which the Recommendation of March 2014 aims to harmonise with the topics identified by the ABI Commission on the Reform of Chapter 11, and we have studied the findings in the ABI Commission's report. These developments have been taken in close consideration in further designing this study, as will be explained in the methodology (see para. 3.1).[241]

25. As a fundamental starting point in this Report we adhere to the view that 'insolvency law' is an integral part of the development and functioning of an internal market, in the meaning of Article 114 TFEU. With e.g. Manfred Balz, one of the principle architects of the European Insolvency Regulation (2000), we believe that a '… functioning bankruptcy system is essential to any economy that aspires to achieve the freedoms of establishment of business and the free flow of goods, services and capital, and to integrate national markets into a unitary internal market.'[242] Undoubtedly, in many countries to the term 'insolvency'

Executory Contracts and Leases, (6) Administrative Claim Expansion, Critical Vendors and Other Pressures on Liquidity; Creation and / or Preservation of reorganization Capital, (7) Labor and Benefit Issues, (8) Avoidance Powers, (9) Sales of Substantially All of the Debtor's Assets, Including Going-Concern Sales, (10) Plan Issues: Procedure and Structure; Plan Issues: Distributional Issues, (11) Bankruptcy Remote Entities, Bankruptcy-Proofing and Public Policy, and (12) The Role of Valuation in Chapter 11.

[240] American Bankruptcy Institute, '2012-2014 Final Report and Recommendations', (2014) (hereafter "ABI Report (2014)"), available at https://abiworld.app.box.com/s/vvircv5xv83aavl4dp4h. See for some criticism Bob Wessels and R.J. de Weijs, 'The Reform of Chapter 11: Its Process and the Recommendation Made', in Bob Wessels and Rolef J. de Weijs (eds.), *International Contribution to the Reform of Chapter 11 U.S. Bankruptcy Code* (European and International Insolvency Law Studies 2, The Hague: Eleven International Publishing 2015), p. 3-40. The ABI Commission, in 2013, established an international working group with the task to address questions raised by the Commission regarding how particular issues had been addressed in several countries, where the country's approach may be relevant to the Chapter 11 model. The countries identified included e.g. Australia, Canada, China and Japan. The participating European countries were Austria, Belgium, France, Germany, Italy, the Netherlands and Spain. See Bob Wessels and Rolef de Weijs, 'Revision of the iconic US Chapter 11: its global importance and global feedback', 5 International Insolvency Law Review 4/2014, p. 441-445. In addition, recent court decisions in the USA under the Trust Indenture Act (TIA) have been regarded as making out-of-court restructurings involving bonds covered by the TIA by a less than unanimous bondholder vote more difficult than previously thought by requiring affected lenders' unanimous consent to an out-of-court workout. The National Bankruptcy Conference (NBC) has, early 2016, proposed to facilitate court supervision of bond restructurings under a new Chapter 16 of the U.S. Bankruptcy Code, which focusses on pure financial restructuring. Connected as it is to TIA we decided not to extend our research into this proposal, see Richard Levin, 'National Bankrupty Conference Proposed Amendments to Bankruptcy Code to Facilitate Restructuring of Bond and Credit Agreement Debt', Harvard Law School Bankruptcy Roundtable, 2016, available at http://blogs.harvard.edu/bankruptcyroundtable/2016/02/09/national-bankruptcy-conference-proposed-amendments-to-bankruptcy-code-to-facilitate-restructuring-of-bond-and-credit-agreement-debt/.

[241] We also studied the English 'Scheme of Arrangement' with more depth. Hess notes in 2013 that this English example in rather different formes and shapes have been introduced in Belglium. Estonia, France, Greece, Ireland, Italy, Latvia, Lithuania, Malta, the Netherlands, Poland, Rumania, Spain and Sweden, see Burkhard Hess, 'Hybride Sanierungsinstrumente zwischen der Europäischen Insolvenzverordnung und der Verordnung', in Alexander Bruns, Christoph Kern, Joachim Münch, Andreas Piekenbrock, Astrid Stadler and Dimitros Tsikrikas (eds.), *Internationales, europäisches und auslandisches Recht, Festschrift für Rolf Stürner zum 70. Geburtstag*, (Tübingen: Mohr Siebeck 2013), p. 1253-1261.

[242] Manfred Balz, 'The European Convention on Insolvency Proceedings', 70 American Bankruptcy Law Journal 1996, p. 485 et seq., at p. 490. 'Effective and efficient insolvency and creditor rights systems are widely recognized as important elements of financial system stability. These systems help to ensure efficient access to credit and allocation of resources, enhancing productivity and growth. They also enable commercial stakeholders to better manage financial risk and other difficulties in the enterprise sectors in a timely way, so as to minimize systemic risk, particularly in the banking system', see World Bank Principles (2011), p. 3.

sticks the halo or stigma of failure, or still invites a suggestion of such failure by a company's management or suggestion of fraud. However, as indicated in the business world of trade and investment, insolvency law is *'… a main pillar of market economy'*[243] and the view prevails that '*insolvency has become a calculable and acceptable risk*'.[244] In many countries the importance of a solid insolvency system to the economy is increasingly acknowledged.[245]

26. Who sets the standards for a system of insolvency law? Where does 'insolvency law' come from? Leaving aside specific European regulations, the general responsibility for the legal framework for pre-/insolvency procedures, including its substantive and procedural rules, is in the hands of the primary national legislator. In the National Reports this proposition has been confirmed, as well as the view that primary insolvency legislation cannot function on its own. In several Member States rules of practice have been established by the court, sometimes after consulting e.g. the local bar. In this report this 'self-regulatory' set of non-binding rules will be discussed as well.

2.3. A contractual context

27. Finally, it is important to note that negotiations leading (or failing to lead, as the case may be) to a restructuring plan, which in essence is an agreement, is in in nearly all Member States unregulated in the sense that parties are free to negotiate to conclude a contract and to negotiate about the contents of such a contract (unless the law determines otherwise).[246] A debtor therefore generally is also free to renegotiate the contents of an agreement. Sometimes existing contracts, to which the debtor is bound, contain contractual clauses relating to the provision of certain financial information to the other party or the initiation of negotiation, sometimes 'renegotiation'. It may be the case that it is a duty for the parties to negotiate, e.g. based on a rule regarding 'hardship' or: *force majeur*.247 Since October 2016 such a duty to renegotiate has been included in the French civil law system.[248]

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[243] Christoph G. Paulus, Stathis Potamitis, Alexander Rokas and Ignatio Tirado, 'Insolvency Law as a Main Pillar of Market Economy – A Critical Assessment of the Greek Insolvency Law', 24 International Insolvency Review 2015, p. 1 et seq. Concurring: Valeria Confortini, 'Privatautonomie and Corprate Reorganisations: Legal Treatment of Shareholders under Insolvenzordnung and Italian Insolvency Law', International Insolvency Law Review 1/2016, p. 6 et seq.

[244] In this way Jay Lawrence Westbrook, Charles D. Booth, Christoph G. Paulus, Harry Rajak, *A Global View of Business Insolvency Systems*, (The World Bank, Washington DC 2010), p. 143, submitting '… that insolvency is an enterprise risk.'

[245] See Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee, A new European approach to business failure and insolvency, 12.12.2012, COM(2012) 742 final.

[246] It should be noted that Article 1337 of the Italian Civil Code provides that during contract negotiations parties have a mutual duty of good faith conduct. In some countries, such a duty may follow from case law, e.g. in the Netherlands.

[247] The phenomenon of hardship is known under most legal systems in the EU, with a variety of labels (frustration of purpose, *Wegfall der Geschäftsgrundlage*, *imprévision*, *onvoorziene omstandigheden*, *eccessiva onerosità sopravvenuta*). In international contract practice the term 'hardship' is used. The impact of a hardship is acknowledged in international soft law instruments. See Article 6:111 (ex Article 2.117) ('Change of Circumstances') of the Principles for European Contract Law:

'(1) A party is bound to fulfil its obligations even if performance has become more onerous, whether because the cost of performance has increased or because the value of the performance it receives has diminished.

28. However, financial distress and/or operating in circumstances close to insolvency generally is not regarded as 'hardship'. Such a risk is to be borne by the party affected by it, i.e. the debtor. These legal rules may indirectly influence the background within which (re)negotiations take place. From our National reports and our own study, however, a specific influence of statutory hardship rules with regard to (re)negotiations leading to a restructuring plan has not been demonstrated.

29. Another contractual issue regarding the result of a negotiated restructuring (its result: the restructuring plan) can present itself – generally and in theory – in two forms: (i) a set of mutually dependent bilateral contracts with creditors, or (ii) the promotion of an existing group of contracts with different obligations (of separate creditors with one debtor) to another level: a multi-party contract with in principle uniform obligations towards the creditors (the restructuring plan). There is little consideration in literature and academia of a 'restructuring plan' as a multi-party contract (as e.g. a workout) compared to bilateral contracts.[249] The view of a private out-of-court workout as a multi-party agreement does, however, raise some questions. Just to mention a few of them are mentioned here: What is the interrelationship between the earlier contract (between creditor and debtor) and the obligation to perform in good faith in concluding a new contract, for instance to hear the other party and/or for this party to (at least) take part in restructuring negotiations? Would

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(2) If, however, performance of the contract becomes excessively onerous because of a change of circumstances, the parties are bound to enter into negotiations with a view to adapting the contract or terminating it, provided that:

(a) the change of circumstances occurred after the time of conclusion of the contract,

(b) the possibility of a change of circumstances was not one which could reasonably have been taken into account at the time of conclusion of the contract, and

(c) the risk of the change of circumstances is not one which, according to the contract, the party affected should be required to bear.'

See also Article 6.2.2 (Definition of hardship) of the UNIDROIT Principles of International Commercial Contracts UPIIC):

'There is hardship where the occurrence of events fundamentally alters the equilibrium of the contract either because the cost of a party's performance has increased or because the value of the performance a party receives has diminished, and

(a) the events occur or become known to the disadvantaged party after the conclusion of the contract;

(b) the events could not reasonably have been taken into account by the disadvantaged party at the time of the conclusion of the contract;

(c) the events are beyond the control of the disadvantaged party; and

(d) the risk of the events was not assumed by the disadvantaged party.'

Article 6.2.3 (Effects of hardship) UPIIC provides:

'(1) In case of hardship the disadvantaged party is entitled to request renegotiations. The request shall be made without undue delay and shall indicate the grounds on which it is based.

(2) The request for renegotiation does not in itself entitle the disadvantaged party to withhold performance.

(3) Upon failure to reach agreement within a reasonable time either party may resort to the court.

(4) If the court finds hardship it may, if reasonable,

(a) terminate the contract at a date and on terms to be fixed, or

(b) adapt the contract with a view to restoring its equilibrium.'

[248] In France, since 1 October 2016, a renewed Article 1195 Code Civil, introduces – inspired by soft law instruments – the rule that the court can change (or terminate) a contract in case of '… *un changement de circonstances imprévisible lors de de la conclusion du contrat rend l'exécution excessivement onéreuse pour une partie qui n'avait pas accepté d'en assumer le risque*', including a duty to renegotiate before seising the court.

[249] For a contractual theory of German insolvency plans, see Stephan Madaus, *Der Insolvenzplan*, (Mohr Siebeck, Tübingen 2011).

a general contractual norm (good faith/ '*Treu und Glauben'*) in a single relation between the debtor and a creditor have the effect that this creditor is required to take into account the position of the other parties (creditors) who have a contract with the debtor? In Germany, an issue of discussion has been that the contractual provisions of a restructuring plan are not coming out of the blue, rather they are based on e.g. a supplier agreement or so from several years ago. A debtor may propose to change the existing contract or suggest a novation, but should he propose so to all affected creditors? In the Netherlands, there has been a discussion about a multi-party agreement with a collective element in this way that a party cannot call in misrepresentation or defect of such an agreement. Also, collectivity of this new contract leads to a specific contract where the principle of good faith or a hardship provision may hardly have any room. The conclude: when the phenomenon of a restructuring plan is adopted, national contract law principles should apply and contract law rules should be developed to give a statutory basis to these plan-contracts. In addition, further research into the intersection of contract, company and insolvency law seems required to fully understand the mechanics of restructuring plans adopted in workouts, pre-insolvency and insolvency proceedings.

30. Furthermore, the negotiation of a restructuring plan, even if intended to be concluded 'purely contractually' (i.e. without recourse to any state-supplied procedure to facilitate restructuring), will naturally be influenced by the restructuring and insolvency laws to which the debtor may become subject. Negotiations leading to a restructuring plan typically take place close to the point at which the debtor is expected to reach the formal threshold for triggering (or entitlement to trigger) the opening of formal insolvency proceedings. Parties will negotiate restructuring terms '… in the shadow of insolvency law'. This does not mean of course that the rules (for example, regarding a stay or a cram-down) have some direct effect prior to their actual application. Rather, it means that parties will negotiate their position against the backdrop of the possibility of these proceedings being opened and with regard to their entitlements in them. In these contracts they may 'borrow' tools available in formal proceedings, such as an inter-creditor agreement or an ad-hoc standstill agreement, because as such, formal restructuring and insolvency proceedings, in as far as they are efficient and promote the interests involved with the continuation of viable businesses, can promote restructuring within a contractual setting. In a few instances, we posed questions to our national correspondents whether in EU Member States in a workout setting such instruments indeed were used. This brings us to our methodology.

3. Methodology

3.1. The project design

31. The ELI project on 'Rescue of Business in Insolvency Law' made its start. The focus of the project was the legal rules relevant for the rescue of financially distressed business and the application of such rules in practice. The ultimate aim was to design a framework that will enable the further development of coherent and functional rules for business rescue in Europe. The ELI Business Rescue Project ran over a period of 42 months which resulted in the following four outcomes:

1. Inventory reports on national insolvency regimes in Europe;

2. Inventory report on international recommendations from standard-setting organisations;
3. Normative reports on the feasibility of an appropriate legal enabling framework for distressed businesses; and
4. The present ELI Business Rescue Report.

32. At the outset of the project, three Reporters were appointed by the ELI to take responsibility for the project, coordinate the first three project outcomes and to produce the final outcome of the project: the present ELI Business Rescue Report describing an appropriate legal enabling framework that supports the rescue of viable businesses in a situation of distress. Prof Dr em Bob Wessels (University of Leiden), Prof Dr Stephan Madaus (Martin Luther University Halle-Wittenberg) and Associate Prof Kristin van Zwieten (Oxford University) kindly agreed to act as Reporters and lead the project. They are renowned experts in the analysis and practicability of legal frameworks aiming at a business rescue. In their work, the Reporters were assisted by Gert-Jan Boon LL.M MSc, and the ELI Secretariat (the 'Project Team').[250]

33. The Business Rescue Project was supported by an Advisory Committee that sponsored renowned experts from very different fields of law (e.g. labour law, contract law, competition law, mediation and dispute resolution) and an Observer that provided for valuable input to the project. Committee members and the Observer are listed in Acknowledgments. Furthermore, National Correspondents (NCs) provided insights into the national insolvency regimes of EU Member states by preparing inventory as well as normative reports. The project also draws from the expertise of the Members Consultative Committee (MCC) consisting of ELI Members that took an interest in the project and its outcomes. Their names are listed in Acknowledgments.

3.1.1. Inventory and Normative Questionnaires

34. The Reporters developed a detailed Inventory Questionnaire to obtain information on the rescue-related laws of each selected jurisdiction. The Questionnaire consists of 10 parts, each of which is addressed a specific rescue-related topic. These 10 major themes resulted from merging the topics the Reporters selected for study in their initial proposal to ELI and the topics identified by the Consultation of 5 July 2013 of the European Commission (which led to the Recommendation of March 2014), and a comparison with those studied by the American Bankruptcy Institute's Commission on the reform of U.S. Chapter 11. For each of the selected major topics questions were developed that would allow National Correspondents to provide very specific information in their Inventory Reports. In terms of scope, National Correspondents were asked to consider all pre-/insolvency procedures (supplied by national law) that could be used to achieve a business rescue outcome, and to identify other legal rules that facilitate the achievement of a business rescue outcome out-

[250] Due to reasons unrelated to the project since April 2016 Kristin van Zwieten stepped down from being a reporter for the project. In addition to Gert-Jan Boon, Dr. Samantha Renssen, assistant professor of Corporate and Insolvency Law, Maastricht University, has assisted with studying several matters of corporate law. The support of Leiden Law School student-interns Nastia Grishkova and Robert de Regt during the academic year 2015-2016 as well as Olga Korneeva during the academic year 2016-2017 is gratefully acknowledged. Also Ioannis Sidiropoulos, PhD candidate at Leiden Law School, and Nicolò Nisi, research assistant at Martin Luther University Halle-Wittenberg, supported the study with valuable input.

of-court (through a private work-out). The Inventory Reports therefore include national responses to such matters as: (i) governance and supervision of a rescue in court and out-of-court (including the position and liabilities for a director and the 'debtor-in-possession', and the position of insolvency practitioners as well as turnaround managers), (ii) special protection for financing a rescue; the stay, (iii) treatment of executory contracts, (iv) ranking of creditor claims, (v) labour issues, (vi) avoidance powers, (vii) sales of substantially all of the debtor's assets on a going-concern basis, (vii) designing and approving restructuring plans, (ix) multiple enterprise/corporate group issues, (x) special arrangements for SMEs.[251]

35. In addition, a Normative Questionnaire with a set of eight questions was developed that asked National Correspondents to critically evaluate their national insolvency systems in their own view and to report about the view of all major stakeholders. The Normative Questionnaire also asked for opinions on areas that were not appropriate for harmonization across national legal systems, as well as initiatives that would be welcomed as positive additions to national law and would be capable of effective implementation.[252]

3.1.2. Selecting 13 EU jurisdictions

36. The factual basis of this ELI Business Rescue Report is the Inventory Reports prepared by the National Correspondents (as described above) on the current status of rescue-related insolvency, company and contract law in selected EU Members States. At the outset of the Business Rescue Project, the Reporters decided that it would be impractical and unnecessary to generate reports on all 28 EU Member States. Instead, 13 EU jurisdictions were selected to be a representative sample of the legal traditions and range of insolvency laws and practices across Europe. The sample includes all major economies (Germany, France, UK, Italy, Poland, Spain, The Netherlands, Belgium, Austria), a representative of the Nordic States (Sweden), the Baltic States (Latvia) and representatives of smaller economies (Hungary, Greece). The selection was approved by the Advisory Committee and the Board of ELI.

37. Developments in non-selected EU Member States have, of course, not been ignored but also influenced the present report (see para. 3.3.2), just as international developments and instruments have (see para. 3.3.4). Moreover, views from scholars (see para. 3.3.5), practical approaches to business rescue and non-public discussions with interests groups (see para. 3.3.6) as well as open discussions with practitioners, judges and academics (see para. 3.3.7) have assisted the reporters in the development of their proposals.

3.1.3. National Correspondents and their National Reports

38. The task of answering our Questionnaires was given to 26 National Correspondents (NCs). The Reporters decided to pair an expert with an academic background with a renowned insolvency practitioner in each of the selected 13 jurisdictions, an overview of all NCs is listed in Acknowledgments. The National Correspondents were approached on the basis of their knowledge and experience of the legal rules and approaches in practice on the

[251] For a sample of the Questionnaire, see Annex 1.
[252] See Annex 2.

matters addressed by the Questionnaires.[253] All NCs filed their reports which led to the first project outcome of 13 Inventory and Normative Reports on their respective national insolvency laws. All Inventory and Normative Reports are publicly available.[254] They state the laws of their respective countries as it was understood to be on 30 November 2016.

3.1.4. Inventory Report on International Recommendations

39. Furthermore, an Inventory Report on International Recommendations from Standard-Setting Organisations, such as the World Bank and UNCITRAL, was drafted by a distinguished young researcher from Leiden University, Gert-Jan Boon, LL.M MSc. This report was published with all National Inventory and Normative Reports and served as a basis for the present ELI Business Rescue Report as well. As indicated, doing business is a global phenomenon and the call for improving rules on rescue of distressed businesses is heard all over the world. Standard-setting organisations have developed international recommendations,[255] numerous (non-)binding (soft law) instruments for the development and further alignment of insolvency laws, either nationally, regionally or globally.[256] The inventory report covered fifteen sets of these instruments, with the aim of reflecting on certain matters in the area of business rescue from the perspective of the goals said organisations wish to achieve.[257] For its stock-taking and an analysis, see the report which is

[253] Whether the specific matter at hand in a national legal system is dealt with in an Insolvency Act, a Company Law Act or an Act on Civil Procedural Law.

[254] The original Inventory and Normative Reports have been available for the Reporters during their study as of March 2015 onwards. The Inventory Reports, as published, state the law as at 15 November 2016. See Bob Wessels & Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming).

[255] These 'international recommendations from standard-setting organisations' are formed by comprehensive sets of non-binding recommendations to national legislators which can be of assistance to practitioners, judges, policy-makers in their respective activities. These are usually prepared by what is called 'formulating agencies' or 'standard-setting organisations' which have a good repute for their expertise and/or experience, see Bob Wessels, *International Insolvency Law, Part. I Global Perspectives on Cross-Border Insolvency Law* (4th ed., Deventer: Kluwer 2015), para. 10090.

[256] For a more encompassing overview of these instruments, see Bob Wessels & Gert-Jan Boon (eds.), *Cross-Border Insolvency: Instruments and Commentary* (2nd Ed., Alphen aan den Rijn: Kluwer Law International 2015). For the influence of changing market conditions and the gradual loss of function of soft law (in this case the so-called London Approach), see Sarah Paterson, 'Bargaining in Financial Restructuring: Market Norms, Legal Rights and Regulatory Standards', Journal of Corporate Law Studies, October 2014, p. 333-365; Bo Xie, *Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue* (Edward Elgar Publishing 2016), p. 22 et seq.

[257] These instruments are (in short): INSOL International Workout Principles II (2017); International Working Group on European Insolvency Law, Principles of European Insolvency Law (2003); UNCITRAL Legislative Guide (2004, and its additions of 2010 and 2013); EBRD Core Principles for an Insolvency Law Regime (2004); EBRD IOH Principles (2007); UNCITRAL Practice Guide (2009); The World Bank Principles for (2016); Asian Bankers Association, Asia-Pacific Informal Workout Guidelines for Promoting Corporate Restructuring in the Region and Model Agreement to Promote Corporate Restructuring: A Model Adaptable for Use Regionally, by a Jurisdiction, or for a Particular Debtor (2013); III Guidelines for Coordination of Multinational Enterprise Group Insolvencies (2013); INSOL Europe, Draft Statement of Principles and Guidelines for Insolvency Office Holders in Europe (2014); EU Cross-Border Insolvency Court-to-Court Cooperation Principles (2015) (comprising also EU Cross-Border Insolvency Court-to-Court Communications Guidelines (2015)); Nordic-Baltic Network, *Nordic-Baltic Recommendations on Insolvency Law* (Sweden: Wolters Kluwer 2016).

publicly available.[258] Also for this part of the report, the reference date has been 30 November 2016.

3.2. The project report

3.2.1. Reports and studies

40. The present report ('ELI Business Rescue Report') has been written by the Reporters and is based on *inter alia* the information gathered from all national reports (Inventory and Normative Reports by NCs) and the Inventory Report on International Recommendations from Standard-Setting Organisations – the first two outcomes of the project were published in 2017. The additional views presented in this ELI Business Rescue Report is based on the laws as understood to be by the Reporters on 28 February 2017.

41. In addition, the Reporters have studied national laws and comparative studies from nearly all EU Member States, therefore, including states in the Northern and Eastern region of Europe, which are absent in the National Reports. Fortunately, there has been a significant amount of recent literature offering detailed analysis of national insolvency laws across Europe. The relative weak presence in the set of National reports of EU Member States in Central- and South-Eastern Europe and in the Nordic countries therefore has been compensated by further study of general national insolvency law overviews (particularly those focused on restructuring regimes) of Central-Eastern European Member States[259] or Northern Europe.[260] In 2015 another detailed overview of expedited corporate debt restructuring in all 28 EU Member was published.[261] Also detailed studies on selected topics in the national laws of some 20 jurisdictions (including nine EU Member States) have been

[258] See Bob Wessels & Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming).

[259] See Thomas Jungreithmeir, Ulla Reish, Gerhard Schilcher, Christian Grininger, *Handbuch Insolvenzrecht – Osteuropa* (Wien: Linde Verlag 2012) (including Russia, Serbia and Ukraine); Christin Hammerl, Christian Hönig, *Insolvency and Restructuring Law in Central & Eastern Europe* (Wien: Linde Verlag 2014) (including Albania, Bosnia and Herzegovina, Kosovo, Serbia and Ukraine); Christoph Paulus, Stathis Potamitis, Alexander Rokas and Ignatio Tirado, 'Insolvency Law as a Main Pillar of Market Economy – A Critical Assessment of the Greek Insolvency Law' 24 International Insolvency Review 2015, p. 1 et seq. The general conclusion of the latter authors (the idea underlying recent global reforms is that keeping the debtor alive may be the best (and sometimes the only) way to provide the creditors with a chance of satisfaction) is supported by Confortini, based on a study of German and Italian law, see Valeria Confortini, 'Privatautonomie and Corporate Reorganisations: Legal Treatment of Shareholders under Insolvenzordnung and Italian Insolvency Law'International Insolvency Law Review 1/2016, p. 6-19.

[260] See Erik Hellström, *Nordic/Baltic company reorganisation law – a comparative report* (Uppsala: Iustus Förlag 2013). The author expresses that liquidation proceedings in the Nordic legal systems historically have been formulated in close cooperation and therefore demonstrate great similarities. Insolvency laws in the Baltic States, however, have developed in greater isolation, as is also true for the Nordic rules on reorganisations of companies in economic difficulties. A Nordic-Baltic Insolvency Network was formed with the aim to agree upon a number of common insolvency law principles, with the objective to strengthen the Nordic (including Norway and Denmark) and Baltic influence in the international process of harmonisation of insolvency laws. The book mentioned served as a basis compilation of national systems and a summery comparison, two years later leading to: Nordic-Baltic Insolvency Network, *Nordic-Baltic Recommendations on Insolvency Law* (Sweden: Wolters Kluwer 2016), available at: http://www.sccl.se/wp-content/uploads/2017/04/Nordic-Baltic-Recommendations-Final-Version-bok-rotated.pdf.

[261] Rodrigo Olivares-Caminal (ed.), *Expedited Corporate Debt Restructuring in the EU* (Oxford: Oxford University Press 2015).

published, on commencement of proceedings, the treatment of contracts in insolvency or priorities and ranking of claims.[262] These publications have been subject of study. In the languages the Reporters master (Dutch, English, German and some French), we have taken into account scholarly comparative studies as well.[263]

42. We have also considered available evidence of the day-to-day operation in business rescue practice, and taken note of considerations regarded as essential to achieving a successful restructuring. In this regards the report has benefited particularly from reports of restructuring cases.[264]

3.2.2. Presentations and discussions

43. From the beginning the reporters have adopted an open, inclusive approach. Evidently, they have discussed their drafts with those who were included in the Reporters' team. Furthermore, they have discussed and sought ideas, opinions and evidenced successes to include in the process of the development of their report:

- ELI Annual Conference: and MCC meeting, September 2014, Zagreb (Croatia);

[262] See Dennis Faber, Niels Vermunt, Jason Kilborn and Thomas Richter (eds.), *Commencement of Insolvency Proceedings*, (Oxford International and Comparative Insolvency Law Series, Oxford University Press 2012); Dennis Faber, Niels Vermunt, Jason Kilborn and Kathleen van der Linde (eds.), *Treatment of Contracts in Insolvency*, (Oxford International and Comparative Insolvency Law Series, Oxford University Press 2013); Dennis Faber, Niels Vermunt, Jason Kilborn, Thomas Richter and Ignacio Tirado, *Ranking and Priority of Creditors*, (Oxford International and Comparative Insolvency Law Series, Oxford University Press 2016).

[263] See e.g. Axel Flessner, 'Insolvenzverfahren ohne Insolvenz?, Vorteile und Nachteile eines vorinsolvenzlichen Reorganisationsverfahren nach französischem Vorbild' KTS 2010, 127 et seq.; Stephan Madaus, *Der Insolvenzplan*, (Jus Privatum. Beiträge zum Privatrecht, Band 157, Tübingen: Mohr Siebeck 2011) (comparing Chapter 11 and German ESUG law); Reinhard Bork, *Rescuing Companies in England and Germany* (Oxford University Press 2012); R.D. Vriesendorp and R. van den Sigtenhorst, ‚Herstructureringen in de modern financieringspraktijk: Nederland vs. de V.S.' Nederlands Tijdschrift voor Handelsrecht 2013-2, p. 94-102; Andrea Brown, *Die vorinsolvenzliche Sanierung von Unternehmen. Ein Vorslag für ein neues Restrukturierungsverfahren unter Berücksichtigung der englischen Arrangem*ents (Schriften zur Restructurierung, Band 8, Diss. Univ. Erlangen, Baden-Baden: Nomos 2015); Jochem Hummelen, *Distress Dynamics. An efficiency assessment of Dutch Bankruptcy Law* (The Hague: Eleven International Publishing 2015). See Gerry McCormack, Andrew Keay & Sarah Brown (eds.), *European Insolvency Law: Reform and Harmonisation* (Edward Elgar Publishing 2016); Stefan Sax and Artur M. Swierczok, 'Das englische Scheme of Arrangement – ein taugliches Sanierungsinstrument für deutsche Unternehmen!', in ZIP 41/2016, 1945 et seq., part of a discussion with Hoffmann and Giancristofano, in ZIP 2016/28, 1151 et seq, and ZIP 41/2016, 1951; Bo Xie, *Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue* (E.dward Elgar Publishing 2016); N.W.A. Tollenaar, *Het pre-insolventieakkoord. Grondslagen en raamwerk*, (PhD Groningen 2016).

[264] See e.g. Christopher Mallon and Shai Y. Waisman, *The Law and Practice of Restructuring in the UK and US* (Oxford University Press 2011); Frank Richter, Christian Timmreck (eds.), *Effizientes Sanierungsmanagement – Krisenunternehmen zielgerichtet und konsequent restrukturieren* (Stuttgart: Schäffer-Poeschel 2013); Kon Asimacopoulos and Justin Bickle (eds.), *European Debt Restructuring Handbook. Leading Case Studies from the Post-Lehman Cycle* (London: Globe Law and Business 2013); Andrea K. Buth, Michael Hermanns, *Restrukturierung, Sanierung, Insolvenz Handbuch* (4th ed., München: Verlag C.H. Beck 2014); Christopher Mallon (ed.), *The Restructuring Review* (7th ed., London: Law Business Research 2014); Lana Ashby, 'The Enigma of 21st century corporate restructuring: successes and failures (ten steps best-practice framework)', 9 Insolvency and Restructuring International, September 2015, p. 9 et seq.

- ELI Annual Conference: panel session (including the Reporters, Prof Paul Oberhammer (Vienna) and Stephan Taylor, international insolvency practitioner) and an MCC meeting, September 2015, Vienna (Austria); and
- ELI Annual Conference, forum discussions (including the Reporters, Arno Metzler, Prof Heinz Vallender and Prof Matthias Storme, September 2016, Ferrara (Italy)).

44. After a non-public discussion with NCs in Vienna (March 2015) on the ELI Business Rescue Project, a selection of its topics were presented and discussed in June 2015 at the 16th Colloquium of IEEI (Lisbon, Portugal). In the later stages of the project:

- Conference of Arbeitskreis Reorganisation, Sanierung, Insolvenz, November 2015, Nürnberg (Germany);
- Telephone Conference with representatives of Council of Bars and Law Societies of Europe (CCBE), November 2015;
- First Lustrum Conference of Institute for Corporate Law, Governance and Innovation Policies (ICGI), November 2015, Maastricht (the Netherlands);
- 3rd research Turnaround Rescue and Insolvency Seminar, discussions with international students, December 2015, Leiden (the Netherlands);
- Stockholm Centre for Commercial Law-ELI Conference on Nordic-Baltic Guidelines on Insolvency Law, February 2016, Stockholm (Sweden);
- International Colloquium at the Catholic University of Lille, March 2016, Lille (France);
- 17th IEEI International Colloquium, June 2016, Chicago (USA);
- Conference on convergence of insolvency frameworks within the European Union – the way forward, July 2016, Brussels (Belgium);
- INSOL International Academics Colloquium, July 2016, London (UK);
- INSOL Europe Academic Forum, September 2016, Lisbon (Portugal);
- Hochschule in Kufstein, Institut für Grenzuberschreitende Restrukturierung, 5. Internationals Symposium Restrukturierung, October 2016, Kufstein (Austria);
- ELI Business Rescue Conference, hosted by ELI and the University of Leiden, 16 and 17 November 2016, Leiden (the Netherlands) (for discussion with NCs and European insolvency judges);
- 4th research Turnaround Rescue and Insolvency Seminar, discussions with international students, December 2016, Leiden (the Netherlands);

4. The Reporter's report

4.1 Objectives

45. The resulting present report ('ELI Business Rescue Report')[265] is designed to assist those involved in a process of law reform and those setting standards for soft law (the constituency addressed includes EU Member States, associations of practitioners, such as insolvency office holders, accountants, lawyers and turnaround advisors, and judges) in the business rescue context. Of course, the proposals in this ELI Business Rescue Report do not

[265] The report was submitted to ELI for purposes of discussions and approval on 28 March 2017. A commercial edition at [publisher] is forthcoming.

claim to be mandatory harmonisation instruments, as EU Member States or others addressed are obviously not bound to follow them. The topics addressed in this Report, however, are intended to present a tool for better regulation in the EU, developed in the spirit of providing a coherent, dynamic, flexible and responsive European legislative framework for business rescue. The Report's addressees are invited to regard the proposals as a set of tools for evaluating the efficiency, effectiveness and suitability of their present system of rules or their current legislative drafts. Evidently, and deliberately, our proposals allow for any particular reform initiative to be tailored to local context or to be aligned with certain tendencies in regional convergence.

46. In the grey area of 'hybrid' or 'pre-insolvency' proceedings, it is clear that judicial, court-covered proceedings in general would warrant an efficient proceeding within which the interests of all stakeholders concerned will be protected. The advantages of such proceedings are less obvious, if at all taken into account, if these are compared with a contractual method of rescue. The latter sometimes is called a 'work-out', generally to be described as a privately, negotiated adjustment of creditor-debtor relations. The general advantages of a work-out (leaving aside that part of the answer flows from the question which law is applicable to the work-out) are (i) a work-out is more effective than a court-supervised proceeding, (ii) pre-petition-negotiated restructuring agreements should reflect a well thought out reorganisation attempt, (iii) (dependent on the negotiation skills of the board of the debtor) lower administrative costs and professional fees, (iv) a stronger management control of the restructuring plan's outcome, (v) less negative publicity, and (vi) relatedly, better preservation of the going concern value. The disadvantages may be summarised here as follows (unless specific contract clauses address these issues):

a. There is no automatic stay or stay on request;
b. Lack of influence and lack of transparency for an Ad hoc creditors' committee or (smaller) creditors individually;
c. There is no method or ability to bind dissenting (individual of classes of) creditors;
d. No ability to unilaterally reject executory contracts; and
e. No ability to recover pre-petition ('bad faith') transfers.

In the Report we analyse these disadvantages and formulate recommendations to lessen and limit these disadvantages or even have them turn into an advantage, i.e. have them function to the advantage for a success of reaching the goal of continuing viable businesses.

4.2 Assisting present harmonisation efforts

47. The March 2014 Recommendation states under Recital 11: 'It is necessary to encourage greater coherence between the national insolvency frameworks in order to reduce divergences and inefficiencies which hamper the early restructuring of viable companies in financial difficulties and the possibility of a second chance for honest entrepreneurs, and thereby to lower the cost of restructuring for both debtors and creditors. Greater coherence and increased efficiency in those national insolvency rules would maximise the returns to all types of creditors and investors and encourage cross-border investment. Greater coherence would also facilitate the restructuring of groups of companies irrespective of where the members of the group are located in the Union.' A deliberate process of seeking such 'coherence' could be described as approximation or as harmonisation. Indeed, the Proposal

Restructuring Directive (2016), issued in November 2016, uses the term harmonisation six times, including the use of the term in the following policy goal: 'A higher degree of harmonisation in insolvency law is thus essential for a well-functioning single market and for a true Capital Markets Union. This is why the issue has long attracted considerable interest at EU level.'[266]

48. However, it should be kept in mind that several obstacles, restraints or disadvantages to harmonisation of national insolvency laws have been identified.[267] These relate to *inter alia* (i) the submission that harmonisation results in the loss of national peculiarities of insolvency law, (ii) that it will result in losing the dynamic possibilities associated with regular competition between countries to create better law systems, in which (a) they can learn from each other, (b) that individual countries will also be confronted with an extreme slowing down of the process of amending the law, and (c) the possibility of adapting it due to the need to maintain conformity with the harmonised 'norm', but also that (iii) the social policies, cultural manifestations or political ideologies underpinning the existing display of different rules on e.g. protecting secured rights, employees' rights or national systems of priorities hardly do allow for harmonisation, or (iv) harmonised rules will be extremely difficult to implement, given the fact that 'insolvency' is generally an integral part in a countries' system of private (commercial and contract) law.[268] Not all of these arguments are equally persuasive.[269] As to (i) we would argue that 'procedural matters' historically have been closely linked with a county's identity, however in cases that involve business restructuring and insolvency cases in which the efficient case management is a prerequisite and in which the principle of equality of arms is fully observed, not all national procedural folklore is meaningful. Moreover, streamlining procedural peculiarities seems in general to involve advancing the level playing field's rules for operating and competing by businesses in distress. The second alleged disadvantage (ii) the 'better national law' argument, as the

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[266] Explanatory Memorandum, at p. 2.

[267] See Ian F. Fletcher and Bob Wessels, *Harmonisation of Insolvency Law in Europe, Reports presented to the Nederlandse Vereniging voor Burgerlijk Recht (Netherlands Association of Civil Law)* (Deventer: Kluwer 2012), p. 49 et seq. Generally on legal culture, see Peter Mankowski, *Rechtskultur, Beiträge zum ausländischen under Internationalen Privatrecht* (Mohr Siebeck 2016), and on cultural differences to overcome in a cross-border workout, see Allan Nackan, Paul Keenan Jr., Jean Baron and Rodrigo Callejas, 'Cultural Matters in Fashioning a Cross-Border Workout', Annual Review of Insolvency Law, 2012, available at http://www.scribd.com/doc/188819174/Restructuring-Culture-Paper.

[268] See Jennifer L.L. Gant, 'The impact of social policy on cross-border insolvency', eurofenix Autumn 2014, p. 32-33; Michael A. Horn, *Die Anforderungen an die Arbeitnehmer in der insolvenzbedingten Unternehmenssanierung* (Nomos Universitätsschriften – Recht, Band 846, Baden-Baden: Nomos 2014); Irene Lynch Fannon, 'Comparative Corporate Law Theory and Harmonisation of EU Insolvency Law: Understanding the Impact of Path Dependency', in Michael Veder and Paul Omar (eds.), *Teaching and Research in International Insolvency Law: Challenges and Opportunities* (Nottingham: INSOL Europe & NACIIL 2015), p. 43-57; Paul Omar, 'Modern prospects for European insolvency law harmonisation' Global Law and Business, 15 September 2015, available at http://globelawandbusiness.com/blog/modern-prospects-for-european-insolvency-law-harmonisation; Paul Wright, Challenges to the Harmonisation of Business Law: Domestic and Cross-border Insolvency, 2015, available at https://ssrn.com/abstract=2658230; Jennifer L.L. Gant, Convergence of Social Policy, 'Employment and Labour: The European Equation', 2016 4(2) NIBLeJ 11; Jennifer L.L. Gant, *Balancing the Protection of Business and Employment in Insolvency. An Anglo-French Perspective* (European and International Insolvency Law Studies (EIILS) (volume 4), The Hague: Eleven International Publishing 2017).

[269] Some of the arguments made have been critically addressed by Ian F. Fletcher and Bob Wessels, *Harmonisation of Insolvency Law in Europe, Reports presented to the Nederlandse Vereniging voor Burgerlijk Recht (Netherlands Association of Civil Law)* (Deventer: Kluwer 2012), p. 49 et seq.

result of regular competition, does not exclude the possibility that the results of harmonisation will be even better (under the condition that it is possible to formulate what 'better' is). The third topic (iii) seems to purely focus on (hard) law and is overlooking the fact that rescue solutions can be achieved in the realm of negotiations with all stakeholders and that the legal rules surrounding businesses in financial distress also could be drafted in a more flexible way, allowing judicial (or creditor) discretion, in a field where there is hardly one single solution, many times in a process with many parties of interest and where many times only private money is involved. The last point ((iv) insolvency as part of system of private law) does not have sufficient merit when timely restructuring of viable businesses improves the outcome for creditors and enhances the interests of other stakeholders, such as the employees or the economy as a whole.

49. A possible answer to challenges in harmonization is to deliberately seek to preserve flexibility in the design of legal rules and/or the processes of their implementation, whilst at the same time ensuring as far as possible that situations in comparable circumstances receive in substance an equal treatment. In this regard, other instruments may be helpful as well, e.g. an Opinion of the European Commission addressed to a certain audience, soft law rules with or without the instruction of 'comply or explain', encouragement of forms of self-regulation, or as an invitation to further study a certain topic or practice, etc.

50. Mindful of the European Commission's commitment to better legal drafting[270] the Report's proposals are formulated as comprehensible, clear, and consistent as possible. Still, our recommendations are not designed to be overly prescriptive of specific outcomes, given the need for commercial flexibility and in recognition of the fact that parties will bargain in the 'shadow of insolvency law'. In certain circumstances, national legislation could include – if not already included – a provision for delegation of the implementation of certain of our recommendations to subordinate legislation, e.g. procedural practice rules or circulars, that can be more easily kept up to date than 'traditional' legislation, or would be more tailor-made to certain situations, on a more concrete level compared to national legislation. A similar mechanism can be suggested to 'empower' a creditors' committee, and delegate certain tasks to such a committee.

4.3. The structure of the report

51. From a legal perspective, the Reporters have chosen to set out their proposals in the form of Recommendations, numbered throughout the full report. Many times the addressees are clear from the text of the nature of any specific recommendation. The addressees, generally, are Member States, professional bodies (for insolvency practitioners or judges) and/or the European Commission.

The Reporters' proposals in their substance are a set of rules for all types of a business rescue (including rescue options in a workout, pre-insolvency and insolvency proceedings) drawn from the study, research and discussion of the goals of such procedures, the interests that are at stake and the interests that should be protected, as well as the requirements to guarantee a transparent process, in which all stakeholders are sufficiently informed. Our

[270] See the Regulatory Fitness and Performance Programme (REFIT), available at http://ec.europa.eu/smart-regulation/better_regulation/documents/com_2015_215_en.pdf.

study, therefore, encompasses issues of contract law, corporate law, employment law, the law of secured rights, in certain cases complemented by judicial involvement, although entering into these legal areas has been kept to a minimum.[271] Our study does not however focus on so-called flanking measures.[272]

4.4 Theoretical foundation of the report

52. The Reporters have been led by the aspiration that an effective insolvency regime is a key component of the internal market, a free market economy that values entrepreneurship and competition. At the same time, it has been recognised as providing an important toolkit for dealing with the aftermath of the global financial crisis, which has affected so many businesses and sectors of the economy. Nevertheless, even where restructuring and insolvency laws legislate for business rescue, a careful balancing exercise will still need to take place between the interests of all of the various parties: the debtor, its creditors, its members or shareholders, with a view to the broader interests of society and the economy as a whole. In recent years Europe has produced several important law reforms, both national and on a European level. A key component in these reforms, reflecting a global trend,[273] is the encouragement of restructurings of businesses, for (start-up) SMEs to multinational companies, with an increasing emphasis on private (out-of-court) workouts or (in-court) formal reorganisation proceedings underlining the essence of preserving enterprise value for the benefit of the body of creditors as well as other constituencies and stakeholders.[274]

53. From general theoretical studies, reflecting on its historic origins and its anticipated development in future over the last decade, there has been a paradigm shift in European national insolvency laws. In short: the aim of insolvency legislation/regulation has shifted (i) from being rather exclusively to protect the creditors' private law interests, to being deployed for rehabilitation of the debtor and the continuity of its business (increased group of interested stakeholders), (ii) from viewing insolvency as a terminal proceeding for business ending in liquidation, to the recognition of insolvency proceedings as a gateway to potential business rescue ('instrumentalisation' of insolvency law), (iii) from insolvency being seen as a personal 'sin' (morale failure), to have developed to insolvency seen as a business risk (economic failure) (enhancement of a rescue culture), (iv) from a formal legal procedural approach to an openness for flexible and pragmatic choices ('deformalisation', sometimes

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[271] We have excluded research into areas as (international) tax law, e.g. (re)charaterising shareholder loans, at arm's length finance. We also excluded matters of competition law, including rules of State Aid.

[272] Jean-Charles Bricongne, Maria Demertzis, Peter Pontuch and Alessandro Turrini, 'Macroeconomic Relevance of Insolvency Frameworks in a High-debt Context: An EU Perspective', European Economy Discussion Paper 032, June 2016, available at http://ec.europa.eu/economy_finance/publications/eedp/pdf/dp032_en.pdf (p. 22 et seq.) submit, that the role of national authorities is twofold: (i) they should ensure that an effective insolvency framework is in place, and '… adapts where necessary both its legal and institutional elements to the magnitude of the challenges, and (ii) they need to put in place flanking policies to support and encourage the actual use of insolvency frameworks by private agents, explaining such measures, such as recapitalisation of banks, early warning mechnisms, tax incentives and social policy measures.

[273] See in the USA the call for reforming Chapter 11 US Bankruptcy Code. Similar developments are seen in Australia, japan and India.

[274] In each individual case the real issue in a rescue attempt is rebuilding trust amongst all parties involved. Legislation and financial restructuring are only to be considered means to reach this goal. See Jan Adriaanse, *The Uneasy Case for Bankruptcy Legislation and Business Rescue*, 2014 2 NIBLeJ 8.

‘contractualisation’ of insolvency, including a pushing back of the role of courts), leading to the development to the distinct body of business rescue and insolvency law. It is submitted that this law indeed can assist in the restructuring of the economy and the allocation of assets from within the private sector.[275] While the reporters are aware of the variety of different normative theories that have sought to explain the fundamentals of insolvency and – in the context of a restructuring framework relevant – company law, we do not ground our analysis on a specific theoretical concept. Instead, we will mention the influence of conflicting ideas anytime they have a practical relevance in evaluating practices or statutory rules, for instance when determining the role of shareholders in voting on a restructuring plan.

54. The way forward on the topics analysed and recommended upon in this ELI Business Rescue Report contains certain new departures. We do believe, however, that our proposals logically follow developments as described in the previous paragraphs. We cherish the belief that the report will assist in taking a next, decisive step in the evolutionary process of the European side of business rescue and insolvency law.

[275] We can only list a selection of these studies: Bob Wessels, ‘Europe Deserves A New Approach To Insolvency Proceedings’, in A. Bruyneel & Jean-Pierre Buyle, *Bicentenaire du Code de Commerce – Tweehonderd jaar Wetboek van Koophandel* (uitg. Larcier, Brussel 2007), 267 (also published in 4 European Company Law, December 2007, p. 253-258); H. Cousy, ‘Naar een nieuwe visie of het insolventierecht’, in H. Braeckmans, H. Cousy, E. Dirix, B. Tilleman en M. Vanmeenen (eds.), *Curatoren en Vereffenaars: Actuele Ontwikkelingen II* (Antwerpen-Oxford: intersentia 2010),p. 2-19; Vanessa Finch, ‘Corporate rescue: Who is Interested?’, Journal of Business Law 2012, Issue 3, 190 et seq.; Reinhard Bork, *Rescuing Companies in England and Germany* (Oxford University Press 2012) (Chapter 2 ‘Practical considerations’); Thomas H. Jackson and Davis A. Skeel, ‘Bankruptcy and Economic Recovery’, ILE Research Paper No. 13-27, available at http://ssrn.com/abstract=2306138; Oscar Couwenberg and Stephen J. Lubben, ‘Essential Corporate and Bankruptcy Law’, Seton Hall Public Law Research Paper No. 2238613, 2013, available at http://ssrn.com/abstract=2238613; Eric Dirix, ‘Het insolventierecht anno 2014’, in H. Braekmans, E. Dirix, M.E. Storme, B. Tilleman en M. Vanmeenen (eds.), *Curatoren en vereffenaars: actuele ontwikkelingen III* (Antwerpen – Cambridge: Intersentia 2014), p. 3-38.; Sarah Paterson, ‘Rethinking the Role of the Law of Corporate Distress in the Twenty-First Century’, LSE Law, Society and Economy Working Papers 27/2014, available at www.lse.ac.uk/collections/law/wps/wps.htm; Horst Eidenmüller, ‘Strategische Insolvenz: Möglichkeiten, Grenzen, Rechtsvergleichung’, Zeitschrift für Wirtschaftsrecht ZIP 2014, p. 1197-1205; Adebola, Bolanle, ‘A Few Shades of Rescue: Towards an Understanding of the Corporate Rescue Concept in England and Wales’ 2014, available at https://ssrn.com/abstract=2524488; Christoph Paulus, ‘§ 1 InsO und sein Insolvenzmodell’, Neue Zeitschrift für Insolvenz- und Sanierungsrecht (NZI) 2015, p. 1001-1006; Stephan Madaus, ‘Schulden, Entschuldung, Jubeljahre – vom Wandel der Funktion des Insolvenzrechts’, Juristenzeitung 2016, p. 548-556.

CHAPTER 1:
Actors and procedural design

1.1. Actors in restructuring and insolvency proceedings

55. This chapter covers the procedural foundation of restructuring processes and insolvency proceedings. It starts off with defining the roles of the key actors in such processes and proceedings (para. 55 et seq.) before setting out conditions for out-of-court workouts and supporting frameworks (para. 224 et seq.), the conditions for formal restructuring and insolvency proceedings (para. 264 et seq.), as well as termination of unsuccessful rescue attempts, including their conversion into another proceeding (para. 318 et seq.).

56. In 2012, reconfirming its commitment to be guided in its work by the rule of law '… as … the foundation of friendly and equitable relations between States and the basis on which just and fair societies are built', the General Assembly of the United Nations recognised '… the importance of fair, stable and predictable legal frameworks for generating inclusive, sustainable and equitable development, economic growth and employment, generating investment and facilitating entrepreneurship …'.[276] It is evident that in addition to a balanced and predictable restructuring and insolvency law, in the area of restructuring and insolvency the roles of all parties involved, including courts and insolvency practitioners, applying the law, are paramount.

57. In the literature it is widely acknowledged that the quality of these key players is of utmost importance, see for instance the Belgian author professor Dirix: 'The soundness of every insolvency legislation depends on the quality of its practitioners: their legal quality, their integrity and their effectiveness. In no single legal order is insolvency law perfect. It can be determined however that in those countries where insolvency law operates properly, this mainly is the result of the quality of its actors: judges, insolvency practitioners and liquidators …'.[277] Reference too is made to Austin (Texas) professor Westbrook: 'In the field of insolvency there are two actors whose integrity and experience are central to the functioning of the insolvency system: judges and administrators',[278] and Fletcher (England) and Wessels (the Netherlands) submitting that in each individual case the organisational structure should be assured, with which these authors mean '… a country's insolvency governance system in an individual case (the allocation of functions between courts and liquidators, including the legal and operational relationships between them, based on law and additional regulations) as well as a country's institutional system, merely related to the

[276] See Declaration of the High-level Meeting of the General Assembly on the Rule of Law at the National and International Levels, Sixty-seventh session, A/RES/67/1, 24 September 2012, para. 8, that adds '…, and in this regard we commend the work of the United Nations Commission on International Trade Law in modernizing and harmonizing international trade law.'
[277] See E. Dirix, 'Het insolventierecht anno 2014', in H. Braekmans, E. Dirix, M.E. Storme, B. Tilleman en M. Vanmeenen (eds.), *Curatoren en vereffenaars: actuele ontwikkelingen III* (Antwerpen – Cambridge: Intersentia 2014), p. 3-38.
[278] Jay Lawrence Westbrook et al., *A Global View of Business Insolvency Systems*, (The World Bank, Washington DC 2010), p. 203.

requirements to fulfil these actors' functions, including professional and ethical rules that apply to them.'[279]

58. International standard developing and setting agencies are emphasise the importance of qualified professionals, see e.g. World Bank[280] UNCITRAL Legislative Guide[281] and the European Bank for Reconstruction and Development (EBRD).[282]

59. In 2014, the EBRD confirmed once more the importance of a functioning insolvency and restructuring framework for businesses in financial difficulties and for transition countries' economies. In its Assessment report, it is stated: 'A sound legislative basis or set of laws governing insolvency is fundamental. Nevertheless, an insolvency system also requires professionals with specialist legal, financial and commercial expertise, who are able to perform the various tasks associated with managing a financially distressed or insolvent business. These professionals include judges, lawyers, accountants and insolvency office holders (IOHs), as well as a developing profession of turnaround experts.'[283]

60. Who sets the standards for a national system of insolvency law and the professionals involved in applying that system? Leaving aside specific European regulations[284], Member States are the main source for primary insolvency legislation. However, our National reports show that rules of practice and procedure are as important as substantive law. In several Member States rules of practice have been established by the court, sometimes after consulting e.g. the local bar. In the Netherlands, for instance, rules of practice and procedure have been set out in guidelines, established by an informal group of supervisory judges in

[279] See Ian F. Fletcher and Bob Wessels, *Harmonization of Insolvency Law in Europe, Preadvies 2012 uitgebracht voor de Vereniging voor Burgerlijk Recht* (Deventer: Kluwer 2012), 78 et seq. These authors make the following comparison: 'Where a solid contract or a smooth merger largely depends on the good work of a professional involved (a contract drafter or an M&A specialist), a successful insolvency proceeding is heavily dependent on a skilled and experienced insolvency office holder and court.' See too Lord Hacking, 'Arbitration is only as good as its arbitrators', in S. Kröll at al. (eds.), Liber Amicorum Eric Borgsten, International Arbitration and International Commercial Law: Synergy, Convergence and Evolution, Kluwer Law International 2011, p. 97-122.

[280] World Bank Principles (2016). See also Bob Wessels and Gert-Jan Boon, *Cross-Border Insolvency Law, International Instruments and Commentary*, (2nd Ed., Alphen aan den Rijn: Kluwer Law International 2015), para. 1.

[281] UNCITRAL Legislative Guide (2004); UNCITRAL Legislative Guide, Part Three: Treatment of Enterprise Groups in Insolvency (2010), and UNCITRAL Legislative Guide, Part Four: Directors' Obligations in the Period Approaching Insolvency (2013).

[282] EBRD IOH Principles (2007).

[283] EBRD, 'Assessment of the insolvency office holder, Review of the profession in the EBRD region', 2014, see http://assessment.ebrd.com/insolvency-office-holders/2014/report.html. The report presents the results of an in-depth study on insolvency office holders conducted by the EBRD across 27 jurisdictions. The assessment was carried out from 2012-2014. The following EU-Member States were included in the study: Latvia, Poland, Romania, Bulgaria, Croatia, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovak Republic and Slovenia. In its aim to support the transition of central and eastern European and Mediterranean countries to market economies, the EBRD has acknowledged the importance of solid insolvency laws. It considers that '… [m]odern insolvency systems and debtor-creditor regimes are the cornerstone of sustainable economic development and provide a safety valve for financial failures'. EBRD has developed two sets of non-binding set of principles, the Core Principles for an Insolvency Law (2004) and the Insolvency Office Holder Principles (2007), see Bob Wessels & Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming).

[284] Such as the EIR (2015), based on Article 81 of the Treaty on the Functioning of the European Union (TFEU) and the Proposal Restructuring Directive (2016), based on Articles 53 and 114 TFEU.

insolvencies (acting on a national level), as well as in detailed rules of proceedings, drafted by a national consultation of the Chairmen of the Civil departments of all (eleven) district courts.[285] Although Dutch courts – with some exceptions – follow these non-binding rules, this level of uniformity seems to be absent in Belgium where the president of each commercial court decides on the rules of practice in his/her district. Unfortunately, this entails differences between the (nine) districts in respect of insolvency proceedings. Also in Spain and Italy, in pre-/insolvency proceedings, specific rules of practice and procedure are usually and informally set by each insolvency court. As an example, the Court of Milan sets and updates rules concerning appointment of commissari giudiziali and other professionals operating with the court, as well as its costs, regularly.[286]

61. In England and Wales, the rules of practice and procedure governing pre-/insolvency procedures derive from a number of sources including: (i) primary legislation, enacted by the UK Parliament including the Companies Act 2006 (which governs schemes of arrangement) and the Insolvency Act 1986 (which governs CVAs and administrations), (ii) the Insolvency Rules 1986, which is subordinate legislation made by the Lord Chancellor under sections 411 and 412 of the Insolvency Act 1986 following consultation with the Insolvency Rules Committee appointed pursuant to section 413 of the Insolvency Act 1986[287], (iii) the common law, through which judges have developed additional rules of practice applicable to pre-/insolvency procedures (for example, certain common law conditions apply to the jurisdiction of the court to sanction a scheme of arrangement in respect of a foreign company), and (iv) guidance or statements of principle which fall outside the statutory framework but which impose standards of required practice that apply to licensed insolvency practitioners in parallel[288], and (v) the Civil Procedure Rules and Practice

[285] Recofa (*rechters-commissarisen in faillissement*) and LOVC (*Landelijk Overleg van de Voorzitters van de Civiele sectoren*). Such a national consultation is established at first instance level as well as appeal level.

[286] The updated instructions of the Court of Milan are available at http://www.ilfallimento.it/wp-content/uploads/2010/10/tribunale-milano-circolare-4-2010.pdf.

[287] The Insolvency Rules Committee is an advisory committee consisting of various members of the legal and accounting professions who volunteer their services in considering proposed amendments to the Insolvency Rules 1986. These Rules will be out of date from 6 April 2017 when the new Insolvency Rules 2016 enter into force, replacing the Insolvency Rules 1986. We felt that this does not change our overall analysis of the rules as subordinate legislation.

[288] These guidance and statements include (a) the Insolvency Code of Ethics, issued by the Insolvency Service (the executive agency of the Department of Business Innovation and Skills responsible for authorising and regulating the insolvency profession) and setting out the fundamental principles which should govern the conduct of all licensed insolvency practitioners; and (b) the Statements of Insolvency Practice (SIP), issued under procedures agreed between the insolvency regulatory authorities acting through the Joint Insolvency Committee (JIC), which set principles and key compliance standards with which licensed insolvency practitioners are required to comply. SIP seems to be a lively document. It is periodically changed, following new or desirable developments. In January 2016, it has been reported that JIC is working on renewing SIP as well as the Code of Ethics. Given the new statements are largely principles rather than practice-based the suggestion has been made that a new statement would be entitled Statements of Insolvency Principles and Practice (SIPPs). See See Philip Reynolds and Lee Manning, Pre-packaged Sales in Administrations: Statement of Insolvency Practice 16 ('SIP 16'), in 13 International Corporate Practice 2016, 1 et seq., and David Menzies, 'What's ahead for the insolvency profession in 2016?' ICAS 2016, available at https://www.icas.com/technical-resources/whats-ahead-for-the-insolvency-profession-in-2016. However, mention must be made of a critical assessment of the self-regulatory system that applies in Britain, leading to the submission that professional bodies have a dual role in promoting the profession and, at the same time, regulating it, with little effectiveness in pushing the highest standards and protecting affected stakeholders. Nevertheless, the latest reforms should '… greatly improve public confidence in the role of professional regulation playing a particular

Directions issued by the Ministry of Justice, which make up a procedural code that governs the way cases are in court are conducted in England and Wales.[289]

62. In order to design an effective and efficient national insolvency law, the UNCITRAL Legislative Guide (2004), in Recommendation 7, lists some twenty common features which should be considered. In Recommendation 7(a)-(c), it is provided that in such law the following should be considered:

> '(a) Identifying the debtors that may be subject to insolvency proceedings, including those debtors that may require a special insolvency regime;
> (b) Determining when insolvency proceedings may be commenced and the type of proceeding that may be commenced, the party that may request commencement and whether the commencement criteria should differ depending upon the party requesting commencement;
> (c) The extent to which the debtor should be allowed to retain control of the business once insolvency proceedings commence or be displaced and an independent party … appointed to supervise and manage the debtor, and the distinction to be made between liquidation and reorganization in that regard'.[290]

63. As to Recommendation 7(a), in this ELI Report we have focussed on 'business rescue', to be understood as encompassing both the rescue of the debtor (such that the entity itself survives) and the rescue of the debtor's business on a going concern basis (whether or not the business continues to be carried on in the same entity). It should be contrasted with the sale of the debtor's assets on a piecemeal or break-up basis. In this Report, references to debtors should be interpreted to exclude references to banking and insurance debtors, and references to consumer bankruptcies. Debtors do include sole traders and entrepreneurs as well as corporate entities.

64. The topic of Recommendation 7(b) will be addressed below (1.2 – 1.5).

65. Recommendation 7(c) serves as introduction to the allocation of roles for a debtor, an 'independent party' (such as an administrator or Insolvency Office Holder, IOH) and/or a court. Generally, formal (restructuring and insolvency) proceedings have two basic types: proceedings with a liquidation or winding-up character and (possibly) rescue-oriented proceedings.[291] Principle C6.2 of the World Bank Principles (2016) identifies three

effective part in their respective capacities', see Bo Xie, *Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue* (Edward Elgar Publishing 2016), 154 et seq.

[289] The applicability of these sources in each case depends on the nature of the procedure in question. For example, guidance for insolvency practitioners will only be relevant where an insolvency practitioner is involved. Generally, the Insolvency Service is responsible for authorising and regulating the insolvency profession and provides guidance in insolvency matters in that capacity. In other matters the role of the Insolvency Service in a business rescue is fairly limited. It may be involved in conjunction with other government departments or bodies, e.g. in matters of rescuing an airline or matters involving the environment or issues of pensions.

[290] Recommendation 112 adds: '112. The insolvency law should specify the role of the debtor in the continuing operation of the business during insolvency proceedings. Different approaches may be taken, including: […]
(b) Limited displacement, where the debtor may continue to operate the business on a day-to-day basis, subject to the supervision of an insolvency representative, in which event the division of responsibilities between the debtor and the insolvency representative should be specified in the law; […]'.

[291] See para. 1.2 regarding procedural design of a restructuring and insolvency framework.

approaches to rescue-oriented or reorganization proceedings in which allocation of roles is expressed: 'C6.2 There are typically three preferred approaches in reorganization proceedings: (i) exclusive control of the proceeding is entrusted to an independent insolvency representative; or (ii) governance responsibilities remain invested in management; or (iii) supervision of management is undertaken by an impartial and independent insolvency representative or supervisor. Under the second and third approaches, complete administrative power should be shifted to the insolvency representative if management proves incompetent or negligent or has engaged in fraud or other misbehaviour.'

66. As has been set out in the Introduction, revisions of many EU countries' national laws demonstrate several common tendencies in proceedings, which have the general aim of rescuing a company's business. Ongoing legislative developments in several Member States, inspired by the Recommendation of March 2014 or in their own right, will result in new or renewed proceedings in matters of insolvency or pre-insolvency. The underlying paradigm of a shift of focus to rescue of business, in legislation as well as in practice, will also mean that traditional roles (of a court or an Insolvency Office Holder) will be in transition. In their functioning, these players will reflect the legislative changes and the renewals introduced. In addition to the persons and bodies mentioned, others may function in (pre-)insolvency proceedings, e.g. a court appointed mediator or a court appointed supervisor or – in an early stage of general financial problems – a turnaround manager. All these actors in restructuring and insolvency play an important role, not only for the proper functioning of negotiations or efficiently handling of procedures for the benefit of creditors as well as other stakeholder, but also in protecting civil rights and the increase of general welfare.

67. The European Economic and Social Committee issued in 2014 its opinion on the role and future of the liberal professions in European civil society 2012.[292] The EESC is strongly of the opinion that the particular public interest of the liberal professions, and the associated requirements for the services they provide, 'need to be safeguarded through binding professional regulations and a raft of generally recognised standards of ethical behaviour for each profession. All the Member States therefore already have a minimum level of regulation'. The EESC therefore recommends that 'all liberal profession organisations and associations should have codes of conduct and ethical standards as well as commissions of ethics within the profession' (point 5.3). The ESSC continues to submit that … stringent ethical requirements on the liberal professions will, in future, also need to be guaranteed through practical guidelines and clearly defined ethical principles. This could involve both standardised and enforceable professional regulations and codes of ethical professional conduct. This will increase consumer confidence' (point 6.3). Where in a restructuring process certain roles may involve a strong influence from actors into each other, e.g. in those Member States where the continuous work of a mediator, supervisor of insolvency practitioner (selection, appointment, supervision of work, determining fees) is dependent on one (local) court, the basis for these rules should be provided for in primary law. Details can

[292] Opinion of the European Economic and Social Committee (EESC) on the role and future of the liberal professions in European civil society 2012, INT/687, issued 25 March 2014 (Rapporteur Mr Metzler), available at www.eesc.europa.eu. According to the Opinion the liberal profession includes tax advisors, bankruptcy advisors and mediators, see point 2.8. Mr Metzler participated in a 2 hour discussion on the role of professionals during the Annual Conference of ELI in Ferrara (Italy) in September 2016.

be arranged in rules of practice and/or by codes of conduct (by way of self-regulation by professional bodies).

68. In the EU, the landscape of these proceedings is well-nigh obscure. In 28 Member States over hundred insolvency proceedings are in place.[293] These nearly all have their own national identification names and differ many times in aim and scope, as well as who may initiate such proceedings, their conduct, their closure and what will be the rights and duties of all stakeholders involved in each of these proceedings.[294] Moreover, in the ongoing legislative developments in several Member States, inspired by the March 2014 Recommendation or in their own right, new or renewed proceedings in matters of insolvency or pre-insolvency have been or will be introduced. In addition, several of these proceedings are not listed in Annex A of the EIR (2015), such as the English Scheme of arrangement[295], in France Mandat ad hoc and Conciliation, in Italy Concordato preventivo, in Spain Procedimiento de homologación de acuerdos de refinanciación or in the Netherland what is called: pre-pack.[296] In this Report we must limit ourselves to providing just a general impression of how (pre-)insolvency proceedings, including its most important actors (or: role players) are supervised.

69. It is not only Member States' insolvency proceedings that have or are being reformed by the increased focus on rescue of business. Changes have also been made (or should be made) to the persons involved in these proceedings. Traditionally, in many European countries in insolvency proceedings these persons or bodies are: the court, the insolvency practitioners and, in several countries, a supervisory judge or, in some countries, a creditors' committee.[297] Evidently, reflecting legislative changes and the renewals introduced, also these players are in transition.[298] In addition to the persons and bodies mentioned, others

[293] See Annex A to the Insolvency Regulation 848/2015 (EIR (2015)) which provides for over 110 insolvency proceedings in the 27 Member States that are bound by it. Denmark is not bound by it

[294] Article 7 EIR (2015) ('Applicable law') lists 13 topics which many times are being differently regulated in the Member States.

[295] A scheme of arrangement is subject to the supervision of the court which is imposed through two court hearings: one to obtain a court order to convene the relevant scheme meeting(s) (Section 896 UK Companies Act) and one to obtain a court order sanctioning the scheme (Section 899 UK Companies Act).

[296] The proceedings mentioned may fall under the scope of Article 1 EIR (2015). What the Dutch call 'pre-pack' is a pre-insolvency proceeding in its own right, not to be confused with its name equivalent in England. See Stef Vullings, 'The Dutch Pre-Pack: An Alternative on the Rise', 4(1) NIBLeJ 2016, 6.

[297] From Principle 7 (Reporting and Supervision), under (b) of the EBRD IOH Principles (2007)), it can be taken that there can be a supervisory role for the committee of creditors: 'Creditors, the debtor and others with an interest in an insolvency case (for example, a court or regulatory body) are entitled to be regularly informed about the progress of the case and that relevant information is available to them. This may be best facilitated through reports. This also provides a basis upon which the work of an office holder and the progress of an insolvency case may be monitored. Accordingly, the law should provide: (b) for the appointment, in appropriate cases, of a committee of creditors who may 'oversee' the work of an office holder This is not to encourage interference in the performance of the work of an office holder, rather to enable a group of creditors to consider the progress and quality of the work. It can sometimes be achieved by close consultation between the office holder and the committee in relation to the more important matters that arise. A committee of creditors will not be appropriate in all cases. Factors to be considered in determining the need include the size of the estate relative to the expense of a committee, the number of creditors and so forth.' See for 'creditor committees' para. 4.4 on the governance role of creditors (Q4).

[298] For existing insolvency professionals with existing qualifications, it will be a challenge to change focus and invest in new qualifications, which in not easy, judging the contribution of Rolf Leithaus, 'Auf ein Wort', NZI Heft 1-2/2016, p. V.

may have a role or function in (pre-)insolvency proceedings, including court appointed mediators or court appointed supervisors or – in an earlier stage of general financial problems – a turnaround manager.[299]

70. This chapter begins with the parties involved in restructuring or insolvency, (1.1). It touches upon the role of the court, including the supervisory judge (1.1.1). In addition, two actors will be discussed, ie a court appointed mediator (1.1.2) or a court appointed supervisor (1.1.3).[300]

71. Whereas these actors generally are in the judicial domain, in insolvency and rescue practice four dominant actors may play a role in day-to-day practice: the insolvency practitioner (1.1.6), the debtor in possession (1.1.7), the turnaround manager (1.1.8), or a chief restructuring officer (CRO) (1.1.9). For all these actors, their status, power and supervision is addressed, including the status, powers and supervision of a 'debtor-in-possession' (or similar function), when the debtor itself (the companies' board) is in charge of a restructuring or insolvency, including the duties and liabilities of the debtor-in-possession.

72. In par. 1.1.10 generally the duties and liabilities of directors are surveyed, when an insolvency practitioner is involved in the whole process.

1.1.1. Role of the court

73. The rather traditional setting in many Member States' insolvency proceedings, especially those which have 'liquidation' or 'winding-up' as a goal, is that supervision over such proceedings is provided by a court, and national or international rules provide which court is competent to act in such a case. The competent court supervises a court appointed

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[299] As a reform priority from an economic perspective, Jean-Charles Bricongne, Maria Demertzis, Peter Pontuch and Alessandro Turrini, 'Macroeconomic Relevance of Insolvency Frameworks in a High-debt Context: An EU Perspective', European Economy Discussion Paper 032, June 2016, available at http://ec.europa.eu/economy_finance/publications/eedp/pdf/dp032_en.pdf (p. 22 et seq.) submit, that '… reforms could aim at enhancing institutional frameworks to ensure an efficient functioning of insolvency procedures. …, differences in the outcomes of insolvency frameworks can be very substantial across the EU, reflected inter-alia in the large variations in the indicators relating to recovery rates, and the time and cost to resolve debt. Such differences imply that in some countries room exists to make the institutional settings for insolvency more efficient. Reforms in this respect should aim, inter-alia, at increasing court capacity and creating specialised in-court resources for insolvency cases … Skills of extrajudicial practitioners should be enhanced. Their performance should be subject to supervision and monitoring, while their remuneration should be designed to strengthen the incentives for swift resolution. In parallel, the quality and availability of information about debtors (liabilities, assets, and income) should be improved in such a way to ensure proper functioning of the insolvency frameworks in place.'

[300] In Article 2(15) of the Proposal Restructuring Directive (2016) such an actor is defined as a 'practitioner in the field of restructuring', meaning '… any person or body appointed by a judicial or administrative authority to carry out one or more of the following tasks: (a) to assist the debtor or the creditors in drafting or negotiating a restructuring plan; (b) to supervise the activity of the debtor during the negotiations on a restructuring plan and report to a judicial or administrative authority; (c) to take partial control over the assets or affairs of the debtor during negotiations'. As an explanation to Article 5 ('Debtor in possession') it is provided: '… the debtor should be left in possession of its assets and affairs. Mediators or supervisors (practitioners in the field of restructuring) may have a role, but such practitioners should not be appointed by a judicial or administrative authority in every case.'

insolvency practitioner and it appoints – if national law so allows – a supervisory judge that supervises the day-to-day administration by the insolvency practitioner. The role for the court itself remains rather distant, and mostly dealing with issues of a legal nature and disputes (conflicts with creditors, hearings, termination of a practitioners' appointment or – if possible – converting a proceeding into a proceeding of another nature).[301] We found such settings e.g. in Austria, Belgium, Germany and the Netherlands. A court's role can also be further limited: in England, for instance, a Company Voluntary Arrangement (CVA) is subject to the supervision of a licensed insolvency practitioner (or any other person who has been authorised to act as nominee or supervisor of a voluntary arrangement) appointed for this purpose. He or she will deal with the proposal, file reports at the court but, absent a specific application to the court in relation to the CVA, the court is not otherwise involved. Also certain types of procedures – such as Individual Voluntary Arrangements (IVA) and Debt Relief Orders (DRO) – are commenced out of court, but the court always has 'oversight' in the sense that there can be a reference or an appeal to the court if contested issues arise.

74. In Germany, the standard insolvency procedure is under the direction of an insolvency professional, even if the proceedings aim at restructuring, and his powers are broad. He is 'master of the proceedings' and can order any measures necessary for the restructuring of the business to the point of asset-deal restructuring, and he can carry these actions out autonomously. However, this insolvency practitioner is supervised in two ways. Generally, he will be under the supervision of the court. In addition, it is the task of the creditors' committee to monitor the insolvency practitioner's execution of his office. Also in other EU Member States courts have similar supervisory roles, e.g. in Greece where the bankruptcy court serves as the basic organ supervising insolvency procedures and pre-insolvency procedures (recovery procedure and special administration procedure). For courts, other countries have reported similar roles and functions.[302]

75. It is noticeable that in several Member States the court uses an 'extended judicial official'. For instance, in Belgium during judicial reorganisation, the main task of such a supervisory judge is reporting and advising. The supervisory judge is supposed to follow the debtor closely and he will advise the commercial court on all important decisions to be taken during the reorganisation procedure. However, in Belgium, such a supervisory judge does not take decisions in respect of the debtor, nor can he give binding instructions to the debtor.[303] The concept of the supervisory judge exists in several Member States (albeit in different proceedings and with different powers), e.g. France, Greece and the Netherlands.

[301] For an overview of the differing powers and responsibilities of judges in a selection of 12 EU Member States, see Judicial Wing of INSOL Europe, *The Role of the Judge in the Restructuring of Companies Within Insolvency* (Nottingham-Paris 2013).

[302] See Bob Wessels & Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming).

[303] In 2013, the Belgian legislator enlarged the competence of the supervisory judge in order to increase the control on debtors and avoid abuses. The supervisory judge can initiate an early termination of the procedure, whenever the debtor does not comply with any requirement provided for in the Belgian Act on Continuity of Business. In case the debtor does not cooperate or withholds relevant information, the judge may initiate the early termination procedure. However, the actual decision to terminate the pending proceedings is taken by the commercial court.

76. Principle C9.1 of the World Bank Principles (2016), states the following role for the court during an insolvency proceeding: 'C9.1 The business should be permitted to operate in the ordinary course. Transactions that are not part of the debtor's ordinary course of business activities should be subject to court review.' Principles D1.4 ('Exercise of Judgment by the Court in Insolvency Proceedings') and D1.5 ('Role of Courts in Commercial Enforcement Proceedings') of the World Bank Principles (2016) determine the following: 'D1.4 … The court should have sufficient supervisory powers to efficiently render decisions in proceedings in line with the legislation without inappropriately assuming a governance or business management role for the debtor, which would typically be assigned to management or an insolvency representative', and 'D1.5 … The general court system must include components that effectively enforce the rights of both secured and unsecured creditors outside of insolvency proceedings. If possible, these components should be staffed by specialists in commercial matters. Alternatively, specialized administrative agencies with that expertise may be established.' Finally, Principle D1.2 ('Role of Courts in Insolvency Proceedings') of the World Bank Principles (2016) provides: 'D1.2 … Insolvency proceedings should be overseen and impartially disposed of by an independent court and assigned, where practical, to judges with specialized insolvency expertise. Non-judicial institutions playing judicial roles in insolvency proceedings should be subject to the same principles and standards applied to the judiciary.'[304]

1.1.1.1. Requirements for judges

77. Generally, the foregoing suggests that a court / a judge has to fulfil a set of five criteria: (i) a general understanding of business management (so as not to assume managerial tasks), (ii) understanding what it needs to effectively enforce the rights of both secured and unsecured creditors outside of insolvency proceedings (as for instance a stay may influence pre-insolvency enforcement rights, (iii), preferably, be a specialist in commercial matters, (iv) be impartial and independent, and (v) where practical, have specialized insolvency expertise.

78. As far as the Reporters have seen, in insolvency law literature the question about the requirements for a court/a judge to deal with insolvency matters professionally has seldom be posed. That is rather different for the insolvency practitioner. In November 2011, the European Parliament[305] suggested harmonisation of general aspects of the requirements for the qualification and work of a 'liquidator'. For our analysis of the requirements that may be applied to a judge, we follow here the grouping of the requirements set by the EP for a liquidator (insolvency practitioner). An insolvency practitioners (i) must be approved by a competent authority of a Member State or must be appointed by a court of competent jurisdiction of a Member State, must be of good repute and must have the educational background needed for the performance of his/her duties, (ii) must be competent and qualified to assess the situation of the debtor's entity and to take over management duties for the company, (iii) must be independent of the creditors and other stakeholders in the

[304] Two other World Bank Principles are worth mentioning:
'D5.1 Judicial Decision Making. Judicial decision making should encourage consensual resolution among parties where possible, and should otherwise undertake timely adjudication of issues with a view.
D5.2 Enforcement of Orders. The court must have clear authority and effective methods of enforcing its judgments.'
[305] Proposal Restructuring Directive (2016).

insolvency proceedings, and (iv) in the event of a conflict of interest, he/she must resign from his/her office.

79. In a report of 2012, Fletcher and Wessels queried why the European Parliament did not make a similar suggestion for the introduction of common (minimum) standards for insolvency judges. The question was motivated by the system of recognition that was introduced in 2002 by the European Insolvency Regulation (2000).[306] In the field of (international) insolvency, in accordance with the 22nd Recital of the European Insolvency Regulation (2000), the rule that insolvency proceedings opened in one Member State are to be recognised in all the Member States from the time that they produce their effects in the State of the opening of proceedings, is based on the principle of mutual trust. The Court of Justice of the EU, in 2006, held that it is that mutual trust which has enabled a compulsory system of jurisdiction to be established, to which it is inherent that the court of a Member State hearing an application for the opening of main insolvency proceedings checks ex officio that it has jurisdiction having regard to Article 3(1) of the European Insolvency Regulation (2000), i.e. examine whether the centre of the debtor's main interests is situated in that Member State. The Court emphasised that such an examination must take place in such a way as to comply with the essential procedural guarantees required for a fair legal process.[307] From this it may be inferred that for European courts dealing with civil law and commercial law matters, two of the requirements identified above ((ii) understanding what it needs to effectively enforce the rights of both secured and unsecured creditors outside of insolvency proceedings; (iv) be impartial and independent) should be assumed to be met. What about the other three? In short (i) a general understanding of business management, (iii), preferably, be a specialist in commercial matters, and (v) were practical, have specialized insolvency expertise?

80. In Europe, it is only in the last decade that useable (albeit limited) data have become available to sketch the general European procedural landscape, revealing that there is no common European definition of 'court', that there are 'radically different' court budgets and that the professional status of judges is not harmonised'.308 Regarding the state of affairs of the developments of insolvency procedures in 12 transition economies, it was concluded some ten years ago, that there remained shortcomings of the legal institutions (generally: courts and insolvency practitioners) necessary for the efficient operation of insolvency laws. As to the judiciary it was concluded: 'A continuing problem is the poor system of legal education which produces judges with insufficient knowledge of economic and financial matters', from which a decade ago, it was concluded: 'These limitations lead us to the conclusion that, in transition economies in general, the involvement of courts in insolvency proceedings should be kept to the minimum'.[309]

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[306] Council Regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings, [2000] *OJ* L 160/1, in legal force since May 2002. It has been repealed by Article 91 EIR (2015).

[307] ECJ 2 May 2006, Case No. C 341/04 (*Eurofood IFSC*) ECR I 3813. Ex officio examination of jurisdiction has now been included in Article 4 EIR (2015).

[308] See Alan Uzelac, Harmonised Civil Procedure in a World of Structural Divergences? Lessons Learned from the CEPEJ Evaluations, in X.E. Kramer and C.H. van Rhee, *Civil Litigation in a Globalising World* 9T.M.C. Asser Press 2012), p. 175 et seq.

[309] See Ewa Balcerowicz, Iral Hashi, Jens Lowitzsch and Miklós Szanyi, in Jens Lowitzsch (ed.), *The Insolvency Law of Central and Eastern Europe. Twelve Countries Screening of the New Member and Candidate Countries of the European Union and Russia: A Comparative Analysis* (Insol Europe, Volume 2/2007).

81. Within the EU, the further development of the area 'Freedom, Security and Justice' requires a proper functioning of the internal market on the basis that cross-border insolvency proceedings should operate efficiently and effectively. Any (soft law) tools should actively aim to further build mutual trust between Member States, which includes the strengthening of confidence in the European judicial area. This is a challenge. In a report published in 2015, 45 large questionnaires were responded to by five European insolvency judges, acknowledging that in some Member States the quality of judges is in need for improvement, the court's infrastructure and available means are poor, the knowledge of the European Insolvency Regulation (2000) is insufficiently developed, the experience to deal with international insolvency cases or the mastering of a second language (for instance English, German or French) is lacking[310], whilst the awareness of the impact of international business or the interests involved in a business rescue plan is not often fully understood.[311]

82. Recently, in June 2016, the Nordic-Baltic Insolvency Network recommended (under section XI ('Administration of insolvency proceedings'), 13 and 14) that:

> 'The court's qualifications and role in the management
>
> 13. Insolvency proceedings, as well as other cases and matters with strong insolvency law implications, should be handled by insolvency courts, commercial courts with special qualifications in the area of insolvency law, or by a division of a court or certain judges who are specialised in or equipped with special qualifications in insolvency law.
>
> 14. If the qualification requirements in the previous section's conditions cannot be met, the insolvency law should not give the court a central or an active role in the management of liquidation or reorganisation proceedings. In particular, the court in that event should not make decisions regarding business matters.'[312]

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[310] See in general on this subject: Astrid Sadler, 'Practice Obstacles in Cross-border Litigation and Communication between (EU) Courts', Erasmus Law Review 2012, Vol. 5, Issue 3), available at www.erasmuslawreview.nl. Steve Parker and Nick Hood, Reform mania: why is the whole world upgrading its insolvency regimes? Parts 1-3, in 9 Corporate Rescue and Insolvency 2016, nrs. 1, 2 and 3, 18, 62, and 107 respectively: '*In many countries judicial capacity, expertise and experience is severely restricted. This despite the excellent work carries out by INSOL International, the American Bankruptcy Institute, INSOL Europe …*'. Insufficient mastering of legal English was one of the key outcomes of a self-assessment of 66 judges from 22 EU Member States (see Gert-Jan Boon, Joran Tromp & Bernard Santen, 'Grensoverschrijdende rechterlijke samenwerking in insolventies', Nederlands Juristenblad 2016/199. Some of these judges were critical on the use of sworn translators, for reason of money, speed and the experience that not all translators can stick to an objective questioning.

[311] Bob Wessels (ed.), *EU Cross-border Insolvency Court-to-Court Cooperation Principles* (European and International Insolvency Law Studies 1, The Hague: Eleven International Publishing 2015), p. 24. Note though that several respondents also criticized the quality of persons acting in a role as insolvency office holder, their understanding of the Insolvency Regulation, their lack of expertise and their awareness of the importance in cross-border insolvency cases to deal with foreign insolvency office holders and/or courts.

[312] See Nordic-Baltic Insolvency Network, *Nordic-Baltic Recommendations on Insolvency Law* (Sweden: Wolters Kluwer 2016). For the text of these Recommendations, available at http://www.sccl.se/wp-content/uploads/2017/04/Nordic-Baltic-Recommendations-Final-Version-bok-rotated.pdf. This Network includes Sweden, Finland, Estonia, Latvia and Lithuania as well as Non-EU Member States Norway and Denmark.

Although not all these data are exhaustive and recent, they allow us to conclude that understanding of business (including economic and financial) matters and specialisation in insolvency law are essential and up for improvement.

83. Looking at a general tableau of 'courts' in the EU, in many civil law countries insolvency cases are not dealt with by specialised courts (like the bankruptcy courts in the USA), but by a court that has general competence in civil matters and disputes. These countries include Austria, Belgium, Czech Republic, Estonia, France, Germany, Greece, Hungary, Italy, Latvia, the Netherlands, Poland, Spain and Sweden. In some countries (supervisory) judges could be non-professional lay judges, such as in Belgium and France.[313] Courts in all countries mentioned are involved in a large number of decisions, ranging from assessing whether opening criteria have been met, selection, appointment or dismissal of an insolvency office holder, ordering interim measures, arranging or instructing certain notifications or publications, approving certain (essential) actions (such as the initiation of civil proceedings by the IOH, approve a plan to continue or discontinue the debtor's business, admitting claims against the insolvent estate, termination of the proceedings, initiating liability actions against management). As a consequence, in almost all countries mentioned nearly all judicial decisions and actions from a court are reviewable, although across countries there will be differences in e.g. the parties with standing in appeal, the grounds for appeal and the time for appeal.

84. The Reporters are not aware of any systematic research about whether the judges in these courts are specialised enough (in applying rather complicated insolvency law matters, often in a rather short time frame) and possess sufficient commercial experience. In their report of 2012, Fletcher and Wessels submit: 'The fundamental principle in cross-border insolvency matters within the EU is that recognition of judgments delivered by the courts of the Member States is automatic', see Article 16 EIR (2000), as it '… should be based on the principle of mutual trust,' see Recital 22 to the European Insolvency Regulation (2000). This principle serves as the cornerstone for confidence in the Member State's judicial capacity'.[314] In the Proposal Restructuring Directive (2016), the Commission picked up the topic of judicial qualification in Article 24 stating that 'Member States shall ensure that the members of the judiciary and administrative authorities dealing with restructuring, insolvency and second chance matters receive initial and further training to a level appropriate to their responsibilities.' The Commission adds in a second paragraph that 'without prejudice to judicial independence and differences in the organisation of the judiciary across the Union, where restructuring, insolvency and second chance matters are dealt with by judicial

[313] This would be possible in the Netherlands (and occurred for supervisory judges in the last century). Presently in the Netherlands only judges have a supervisory role. A result from comparative research in general commercial law cases demonstrate that lay judges only in exceptional cases have a role in appeal cases, see Holger Fleischer and Nadja Danninger, 'Die Kammer für Handelssachen: Entwicklungslinies and Zukunftperspectiven', ZIP 5/2017, p. 205-214.

[314] Fletcher and Wessels suggest that systematic examination should take place in this specific field in an aim to obtain accurate and comparative data on aspects of the functioning of courts in insolvency matters, see Ian F. Fletcher en Bob Wessels, *Harmonisation of Insolvency Law in Europe, Preadvies uitgebracht voor de Vereniging voor Burgerlijk Recht* (Deventer: Kluwer 2012), p. 123 et seq. For studies beyond the traditional judicial values, such as judicial independence, see Richard Devlin and Adam Dodek, *Regulating Judges. Beyond Independence and Accountability* (Cheltenham, UK / Northampton, MA, USA: Edward Elger Publishing 2016); Sandra Taal, *Working separately together: A quantative study into the knowledge sharing behaviour of judges* (Diss. Utrecht, Stämpli Verlag AG 2016).

authorities, Member States shall ensure that these matters are dealt with in an efficient manner which ensures expeditious treatment of the procedures and that the members of the judiciary in charge have the necessary expertise and specialisation'.[315]

85. Although generally (commercial or civil) courts are involved in pre-/insolvency matters, several National Reports refer to certain forms of specialization. In England, only about twenty High Court judges are assigned to the Chancery Division which is why it can be considered quite specialised in the matters of its jurisdiction, including insolvency and company proceedings. In Belgium commercial courts may be composed with both professional judges and lay judges. The lay judges are businessmen, independent company chairmen and chief executives, accountants, bankers, etc. When not serving as a lay judge one day per week, they carry on professional activities outside the court. In France, only lay judges (businessmen) hear insolvency cases at the commercial court level. In several countries, commercial courts may have, as a form of specialization, one or more 'insolvency chambers'. In the commercial courts in France insolvency cases will be dealt by the insolvency divisions of the court, as in Belgium also composed with lay judges.[316] The phenomenon of an internal unit or department within the general (first instance) court can also be seen in Germany, Greece, Hungary, Italy, Latvia, the Netherlands, Sweden, and – to a lesser extend – Spain.

86. In France, as from 1 March 2016, specific commercial courts will have exclusive jurisdiction over conciliation, safeguards, reorganisation and liquidation proceedings, when the debtor meets certain criteria. This is one of a group of changes made in August 2015 to the French insolvency law system. These include (i) the specialization of certain commercial courts, (ii) changes to the applicable rules to administrators and judicial officers, and (iii) various other amendments provisions of direct relevance to the conduct of insolvency proceedings. The law 2015-990 of 6 August 2015 for the growth, activity and equal economic opportunities (called: Loi Macron) introduces the specialization of some commercial courts. These provisions will apply to collective proceedings opened on 1 March 2016 or later (Article 231) and must be supplemented by a decree listing these specialized commercial courts. Article L. 721-8 of the Code of Commerce specifies that these courts will be competent to deal with certain French insolvency proceedings ('les procédures de conciliation, de sauvegarde, de redressement judiciaire et de liquidation judiciaire, lorsque le débiteur exerce une activité commerciale ou artisanale') and in the case the debtor is (a) a company whose number of employees is greater than or equal to 250 and where the debtor is a company whose net turnover is at least 20 million euros, or (b) when the debtor is a company whose net turnover is at least 40 million euros. Most notably, the same specially designated commercial courts will be competent for the procedures for the opening of

[315] We leave aside the idea of a (gradual) introduction of European courts, as suggested by Diego Valiante, *Europe's Untapped Capital Market: Rethinking financial integration after the crisis* (CEPS Paperback, London: Rowman & Littlefield 2016), concluding (p. 226): 'Therefore, it is reasonable to expect that a full-fledged EU bankruptcy regime would not emerge soon, but a fragmented system of bankruptcy laws can be damaging for cross-border financial transactions. In this respect, there are important areas in which harmonisation can be achieved without putting into question the different legal systems currently coexisting in Europe, leaving the counterparties of a cross-border financial transaction to price these differences (measurable ex ante) in the final price. There are two important areas *vis-à-vis* insolvency proceedings that deserve more attention: the regulatory framework and the judicial review by dedicated courts.'
[316] As in the English High Courts these are not necessarily specialised in rescue or insolvency matters.

insolvency proceedings in accordance with acts of the European Union relating to insolvency proceedings (which seems more extended than the European Insolvency Regulation (2015)) or for procedures which arise from the presence within its jurisdiction of the centre of main interests (COMI) of the debtor. Companies facing an insolvency proceeding with subsidiaries in a similar position will be subject to the same court, which will enable the negotiation of a workout much more efficiently. If the specialised commercial court has jurisdiction over the parent company, it will also have jurisdiction over the subsidiaries.[317]

87. In the UK in 2015 the 'Financial List' procedure has been introduced as special court and a 'market test procedure' when parties – without an actual legal dispute – are seeking guidance on a point of English law. As from 1 October 2015 in the UK the Financial List is in operation. It is a joint initiative of the Chancery Division and the Queen's Bench Division and builds on the expertise of the judges of the Commercial Court and the Chancery Division. Judges from both jurisdictions have been nominated to sit as 'Financial List judges'. The financial markets play an important role nationally and internationally, and are continually developing. Many parties in the financial markets choose for English law to govern their relationships. In recognising that the UK serves as a global hub for financial law, a new court has been set up in London to deal with disputes between them. The Financial List primarily intends to meet the needs of the international financial community and to make sure that cases are dealt with by judges with particular relevant expertise and to provide users of the Financial List fast, efficient and high-quality dispute resolution of their claims or disputes. Disputes that are eligible for inclusion are those that principally relate to financial disputes of over £50m or equivalent, or which require particular market expertise, or '... raise issues of general market importance'. It also includes restructuring and insolvency matters, such as schemes of arrangement. The procedure is intended to fit seamlessly with existing procedure. Parties issue proceedings in either the Commercial Court or the Chancery Division. Before judge allocation, the parties will have the opportunity to indicate any particular feature of expertise that may be advantageous. The so-called the 'market test case' procedure is a procedure to facilitate the resolution of '... market issues to which immediately relevant authoritative English Law guidance is needed', without the need for a present cause of action between the parties to the proceedings. The parties with interest should be '... actively in business in the relevant market', whilst in appropriate cases, a relevant trade body or association may be joined to ensure that the arguments of all interested parties are properly put before the court. The 'market test case' procedure wishes to ensure that markets are most efficient when their actors have mechanisms to resolve uncertainties quickly and definitively.[318]

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[317] See http://www.legifrance.gouv.fr/affichLoiPubliee.do?idDocument=JORFDOLE000029883713&type=general&legislature=14. Catherine Ottaway and Fanny Seroke, 'The Impact of the "Macron" Law on French Insolvency Procedure' International Corporate Rescue 2016, p. 48 et seq.; Paul Omar, 'IP regulation in France set for a shake-up!', eurofenix Winter 2015/16, 30 et seq.

[318] It is a pilot for two years and it provides a mechanism for the court to grant declaratory relief on the grounds that it is in the public interest to do so. Further info available at https://www.judiciary.gov.uk/you-and-the-judiciary/going-to-court/high-court/financial-list/. Until November 2016 some 22 cases have been dealt with, see the speech by The Chancellor of the High Court Sir Geoffrey Vos, 'A Look at the Future for Insolvency and Business Litigation in London', 9 November 2016, available at https://www.judiciary.gov.uk/announcements/speech-by-the-chancellor-of-the-high-court-a-look-at-the-future-for-insolvency-and-business-litigation-in-london/.

88. Another form of concentration takes place in the Netherlands, through the Enterprise Chamber (*Ondernemingskamer*), a division within the Court of Appeal of Amsterdam. Its jurisdiction is not 'insolvency', but rather adjacent: internal corporate disputes. Generally, the Enterprise Chambers (EC) has jurisdiction in specific disputes arising within legal persons, ie those that around thirty Dutch acts have assigned to it. By far most cases are placed in the context of the right of inquiry (recht van enquete)[319] and workers' co-determination law[320]; other cases typically relate to the area of corporate litigation.[321]

The right of inquiry entitles shareholders (a group of at least 10% of the shareholders in a B.V. or an N.V., or the holder(s) of shares or depositary receipts with a total nominal value of at least € 225.000) and trade unions, to request the Enterprise Chamber an investigation into the affairs of the company. These proceedings are divided in two phases. In first phase of inquiry proceedings, the EC decides whether indeed an investigation (inquiry) shall be held. The EC can order such investigation if there are '… well founded reasons to doubt the correctness of the course of action followed by the corporation'. If the EC, having balanced the involved interests, including that of the corporation, orders an investigation, it shall appoint one or more investigators. The company shall (in first instance, at least) bear the costs of the investigation. The investigators are rather free in how to organise and conduct the investigation. This phase ends when the investigators file their report with the court.
The proceedings come to an end, unless the plaintiffs are of the opinion that the report shows mismanagement (i.e. some incorrect course of action). Usually, management board and/or the supervisory board are held responsible for misconduct. In order to have determined that misconduct has taken place, the plaintiffs have to file a new request, initiating the second phase. If the EC establishes mismanagement indeed, it can take one or more measures to put an end to it, such as the dismissal of directors, the suspension of annulation of any decision of any body of the company. The EC can even order the dissolution of the corporation. The EC therefore possesses a range of powerful instruments. It can, at the request of the parties that requested for the inquiry, also order immediate temporary relief measures (to be applied for the duration of the proceedings), which include the suspension of a director, the appointment of a director or supervisory director with special authorities, the suspension of certain authorities of any body of the company, and the (temporary) transfer of shares. It is clear that the Enterprise can deeply intervene within legal entities and enterprises, aiming at the creation of a corporate environment in which a healthy balance within the company and its bodies can be restored.

The Enterprise Chamber has nationwide jurisdiction. In most of her allotted procedures it is the only court at first instance. The proceedings before the Enterprise Chamber are characterized by flexibility, an informal character, competence and speed, the latter whenever possible, especially where necessary. Its expertise is strong, also because the Enterprise Chamber uses councils (raden). These are laymen from the perspective of the law

[319] Article 2:344 and following Dutch Civil Code.
[320] Especially Articles 25 and 26 of the Works Councils Act.
[321] E.g. first instance actions for squeeze-out of minority shareholders, requests for correction of the financial statements, the annual report or by adding other data of companies and certain other entities, claims on appeal under the rules of settlement of disputes between shareholders and resisting the withdrawal of unilateral statements containing residual liability of for instance a holding company towards a subsidiary.

in the strict sense, but they have in the areas where the Enterprise Chamber has jurisdiction over quality knowledge and experience, including expertise on financial matters and corporate governance. The Enterprise Chambers generally treats and decides on complaints submitted in multiple compositions: three professional judges and two councils.

89. In as far as corporate restructurings or insolvencies have a cross-border dimension, the following points related to the court's role must be mentioned. As of 26 June 2017 the role of a court dealing with insolvency matters (and the role of an insolvency practitioner) in cross-border insolvency cases will be notably increased.[322] The Recast of the EU Insolvency provides in Articles 41 – 44 for cooperation and communication where there are multiple insolvency proceedings relating to a single debtor. The existing mutual duty to cooperate has been extended in several ways. Whereas in Article 31 EIR (2000) these duties are limited to insolvency practitioners (in the EIR (2000) defined as 'liquidators'), Articles 41 – 44 EIR (2015) will impose duties of cooperation and communication as between courts (Article 42), and between insolvency practitioners and courts (Article 43 EIR (2015)), as well as between insolvency practitioners (Article 41 EIR (2015), the successor to Article 31 EIR (2000)). These provisions not only extend the number of parties subject to the European Insolvency Regulation (2015)'s duties of cooperation and communication, but also provide more detail as to the content of these duties, and (in the case of Article 43 EIR (2015)) provide a rule to regulate the costs of such cooperation and communication (Article 44 EIR (2015)).[323] Parallel provisions to Articles 41 – 44 EIR (2015) can be found in Chapter V of the Regulation, which governs cooperation, communication and coordination in corporate group insolvencies. In cross-border insolvency cases courts will therefore encounter new challenges[324] and quality, professionalism and integrity will be of uppermost importance.[325]

[322] See EIR (2015).

[323] See Bob Wessels, 'Commentary on Articles 41-44 EU Insolvency Regulation (Recast)', in Reinhard Bork and Kristin van Zwieten (eds.), *Commentary on The European Insolvency Regulation* (Oxford University Press 2016), p. 457-506.

[324] See Heinz Vallender, 'Neue Herausforderungen für Richter und Insolvenzverwalter durch reformierte EuInsVO', NZI 2015/18. In 2015 a set of 26 EU Cross-Border Insolvency Court-to-Court Cooperation Principles ('EU JudgeCo Principles (2015)') accompanied by 18 EU Cross-Border Insolvency Court-to-Court Communications Guidelines ('EU JudgeCo Guidelines (2015)') have been developed. The EU JudgeCo Principles (2015) include principles on their non-binding status and their objectives, case management of courts and the equal treatment of creditors and principles about the judicial decisions itself, on its reasoning and for instance on providing a stay or moratorium. Several principles relate to the course of the proceedings, such as notifications and authentication of documents, and principles on the outcome of judicial cooperation, for instance cross-border sales, assistance to a reorganisation or rules for binding creditors to an international reorganisation plan. The EU JudgeCo Guidelines (2015) represent a set of very practical guidelines to facilitate communications in individual cross-border cases. See Bob Wessels (ed.), *EU Cross-border Insolvency Court-to-Court Cooperation Principles* (European and International Insolvency Law Studies 1, The Hague: Eleven International Publishing 2015). Visit www.eujudgco.eu for the full text of the EU JudgeCo Principles (2015) and EU JudgeCo Guidelines (2015).

[325] See on the subject, related to courts, also para. 1.6.1.3. See – from the angle of an IOH – for instance Bob Wessels, *De onafhankelijkheid van de faillissementscurator* (Preadvies Christen Juristen Vereniging 2013, Zutphen: Uitgeverij Paris 2013), p. 84, submitting: 'The core question of every insolvency judge will be: how will I know when someone approaches my court and says she/he is the insolvency practitioner appointed in a proceeding in Cyprus, in France or in Finland, that she/he is sufficiently honorable and incorruptible? More substantial is to down-to-earth question: how will I know as a Dutch judge that I communicate with, cooperate with or sometimes provide information to someone whose profession and work is assessed continuously on professionality and integrity?'

1.1.1.2. Impetus for recommendations

90. We submit that the greater number of the aspects of the deontology displayed for a 'liquidator' by the European Parliament (being (i) competency; appointment; good repute; educational background needed for the performance of his/her duties, (ii) must be competent and qualified to assess the situation of the debtor's entity, (iii) independent, (iv) in the event of a conflict of interest, he/she must resign from his/her office) will for a judge or a court be regulated in any way or form in the Member States' constitution and/or its procedural legislation. In any EU Member State, the function of judges is a prerogative of the sovereign state.

91. Still, Member States should use their regulatory powers to secure a degree of specialisation within the court system and ensure that judges are appropriately qualified to handle every-day liquidation cases as well as complex rescue procedures or cross-border cases.

92. Member States should evaluate their court systems against certain key factors which can indicate which alternative seems the best, given the circumstances of the case, respectively introduce a framework that allows these factors to be balanced in a particular case. Key indicators include:

(i) the avoidance of heavy costs for courts;
(ii) the general need to decide in insolvency matters with urgency and speed;[326]
(iii) the general preference of disputants for confidentiality and to limit court involvement;
(iv) the wish to save resources for the insolvent estate; and
(v) ensuring easier implementation (e.g. of a cross-border rescue plan) or (vi) streamlining notices to creditors, as well as general business considerations, such as gaining time and efficiency and tapping on available expertise.[327]

93. Considering the great diversity of restructuring and insolvency cases, Member States should not only provide for specialised insolvency courts or chambers. They should also introduce a further specialised subsection or jurisdiction for (bigger) rescue and/or cross-border-cases because such cases require a specific set of qualification and experience that should be concentrated with specific judges in much more specialised courts. The design of the High Court in England or the latest reforms in France provide excellent examples of a possible structure.

94. Judges appointed to hear insolvency cases should have a special set of qualification while judges in specific restructuring or cross-border chambers should receive additional training. Every judge at an insolvency court should:

1. be impartial and independent in any case;

[326] We leave aside another method for achieving speed, namely technology or a per case digital forum, see Chaz Rainy, 'Finding a Forum for Insolvency: Using Digital Forums to Improve Due Process in Insolvency Proceedings While Preserving Speed, Certainty, Discretion, and Cost Considerations', 10 July 2015, available at https://ssrn.com/abstract=2657473.

[327] These indictors in general also reflect a more recent trend in many Western legal systems to reduce the problem of excessive and expensive resort to court proceedings, see Neil Andrews, *The Modern Civil Process* (Mohr Siebeck 2008).

2. in general understand business management issues;
3. understand what it needs to effectively enforce the rights of both secured and unsecured creditors outside of insolvency proceedings;
4. have specialised in commercial law matters; and
5. have acquired insolvency expertise.

95. Member States should reflect these preconditions when appointing judges to insolvency courts or chambers. People appointed can have a legal, but also a business education – depending on the judicial tasks in the respective jurisdiction for an insolvency judge. Experiences with lay judges handling cases at the local level in France have proven that such appointments are an option. If suitable candidates are not available, Member States must provide for respective training. In addition, Member States should ensure the required level of experience and expertise by requiring and guaranteeing a judge's term for a minimum number of years in the field of insolvency and restructuring. When appointing judges for further specialised chambers for restructuring or cross-border cases, Member States must safeguard the expertise necessary for the task by choosing from judges with experience in commercial and insolvency law that receive additional training in restructuring and international insolvency law. The establishment of national and international organisations of insolvency judges (e.g. BAKInsO in Germany, Judicial Wing at INSOL Europe or at the International Insolvency Institute (III), or the network of judges (and other experts) at the IEEI (International Exchange of Experience in Insolvency) has proven the potential of educating judges on a non-mandatory level while also organising their influence in the political process in Member States or at the EU level.

96. Courts themselves may wish to improve their level of quality and effectiveness. They could commit themselves to the development of a professional standard, a benchmark to continuously test the level of the key components of being 'a good judge'. The initiative on a national level could be taken by a national conference of judges or by certain courts themselves. In addition to a national standard a professional standard in matters of restructuring and insolvency could be developed. Elements of this standard would focus on the substance of a judicial decision, that such decisions would be on time, the flexibility of the organisation of persons involved (judges as well as supporting staff) and their expertise.[328]

97. Where such qualification requirements cannot be met, Member States should not give the court a central or an active role in the management of liquidation or reorganisation proceedings. In particular, the court in that event should not make decisions regarding business matters.

[328] We note, with appreciation, Recital 39 of the Proposal Restructuring Directive (2016): 'Finally, given the enhanced cooperation mechanisms between courts and practitioners in cross-border cases set up by Regulation (EU) 2015/848, the professionalism of all actors involved needs to be brought to comparable high levels across the Union … Member States should ensure that members of the judicial and administrative bodies are properly trained and have specialised knowledge and experience in insolvency matters. Such specialisation of members of the judiciary should allow making decisions with potentially significant economic and social impacts within a short period of time and should not mean that members of the judiciary have to deal exclusively with restructuring, insolvency and second chance matters. For example, the creation of specialised courts or chambers in accordance with national law governing the organisation of the judicial system could be an efficient way of achieving these objectives.' See Article 24 of the Proposal Restructuring Directive (2016).

1.1.1.3. Recommendations

Recommendation 1.01: The EU as well as Member States should recognise that the success of any restructuring or insolvency system is very largely dependent upon those who administer it. Such a system can only function well when all stakeholders, including the general public, have confidence and respect in the courts and insolvency practitioners, and the way the roles of all parties involved are guaranteed and executed.

Recommendation 1.02: The EU as well as Member States should ensure that any restructuring and insolvency system includes transparent rules in the law for legal powers and duties, appointment, licensing, supervision, education and work standards and ethics for the key actors in that system. Such rules can be further elaborated in more depth and detail in European or national rules, including rules of practice. In setting professional and ethical standards, the EU and Member States should ensure that the relevant professional bodies are consulted and involved in the creation of such standards and that they take into account best practices for appropriately regulated professional parties as set out in principles and guidelines on regulation of the restructuring and insolvency profession developed or adopted by European and international non-governmental organisations active in the area of restructuring and insolvency.

Recommendation 1.03: Member States should provide for specialised courts or chambers to handle restructuring and insolvency cases. In addition, Member States should introduce a further specialised subsection for hearing rescue and cross-border-cases which require a specific set of qualifications and experience that should be concentrated with specific judges specialised in these matters.

Recommendation 1.04: Member States and courts should recognise that the performance of restructuring and insolvency tasks by courts and its judges requires the continuous strengthening of judicial independence, and the appearance of such independence.

Recommendation 1.05: Member States should ensure the proper qualification of judges at such specialised courts when making appointment decisions. Member States should also ensure the further education of appointed judges by supporting further training and by setting mandatory minimum terms of judges within these courts to incentivise the acquisition of the requisite expertise and experience. They should also encourage and support judges to actively participate in national and international networks of insolvency judges.

Recommendation 1.06: The EU, Member States and courts should actively develop methods to effectively improve judges' performances by either

(i) concentration of courts with jurisdiction to decide in matters of restructuring and insolvency;

(ii) selecting certain matters in which courts can be addressed to provide their view in certain matters of market uncertainties;

(iii) developing specific education beyond the boundaries of general legal competence;

(iv) developing and applying professional insolvency standards to assess performance; or
(v) by a combination of these.

1.1.2. Role of a mediator

98. The Recommendation of March 2014 introduces two rather new actors in the area of reconstruction and insolvency, ie the mediator and the supervisor. [329] The relevant Recital in the Recommendation provides: '(17) To promote efficiency and reduce delays and costs, national preventive restructuring frameworks should include flexible procedures limiting court formalities to where they are necessary and proportionate in order to safeguard the interests of creditors and other interested parties likely to be affected. For example, to avoid unnecessary costs and reflect the early nature of the procedure, debtors should in principle be left in control of their assets and the appointment of a mediator or a supervisor should not be compulsory, but made on a case-by-case basis.'

99. Section II B ('Facilitating negotiations on restructuring plans') then provides:

> 'Appointment of a mediator or a supervisor
> 8. Debtors should be able to enter a process for restructuring their business without the need to formally open court proceedings.
> 9. The appointment of a mediator or a supervisor by the court should not be compulsory, but rather be made on a case by case basis where it considers such appointment necessary': adding with an eye to a mediator '… (a) in the case of a mediator, in order to assist the debtor and creditors in the successful running of negotiations on a restructuring plan;'[330]

100. The Recommendation is further silent on these two functions. The Assessment Report is a bit more forthcoming: 'A mediator's role is to assist the parties in reaching a compromise on a restructuring plan. A mediator may be appointed ex officio or on request by the debtor or creditors where the parties cannot manage the negotiations by themselves. The role of supervisors is to keep an eye on the actions of the debtor and creditors and ensure they are fair to the body of creditors and comply with the law. He does not take over the day-to-day operation of the business of the debtor. A supervisor may be appointed on a case-by-case basis, e.g. where there is a risk of abuse of the stay of enforcement of actions, or of certain high-risk transactions being undertaken by the debtor. The possibility to appoint a supervisor must however be exceptional.'[331]

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[329] Confirmed in Recital 18 and Article 5 of the Proposal Restructuring Directive (2016).
[330] Of importance for mediation is also a provision with regard to the coordination of the insolvency of groups of companies in Article 72 EIR (2015) ('Tasks and rights of the coordinator'), para. 2: '2. The coordinator may also: (a) be heard and participate, in particular by attending creditors' meetings, in any of the proceedings opened in respect of any member of the group; (b) mediate any dispute arising between two or more insolvency practitioners of group members.'
[331] Commission's Recommendation (2014) 32.

1.1.2.1. Mediation in civil and commercial law matters

101. In Europe, the Directive on certain aspects of mediation in civil and commercial matters entered into force in 2008.[332] The Directive had to be implemented in the national laws of the Member States before 21 May 2011.

102. The Directive concerns mediation not in national cases, but in cross-border disputes, in which at least one party is a domiciled or habituate resident in a Member State other than that of any other party on the date on which e.g. the parties agree to use mediation after the dispute has arisen.[333] In the Directive mediation is seen as a category of Alternative Dispute Resolution (ADR) which is defined as '… a range of procedures that serve as alternatives to litigation through the courts for the resolution of disputes, generally involving the intercession and assistance of a neutral and impartial third party.'[334]

103. Mediation is different from the other ADR procedures, such as arbitration, because the parties ultimately make their own decision. There is a third party, a mediator, but s/he only guides the parties and their discussions and negotiation towards an agreement. Another difference is that mediation is a voluntary process, while arbitration often is imposed and its result (an arbitral award) is enforceable.[335] Although 'arbitration' in insolvency matters has occurred in Europe, we do leave it aside in the Report.[336]

104. In the European Union there has been attention on mediation since 1998. The European Commission made a Recommendation about alternative dispute resolution in consumer disputes.[337] In 2001, the Commission published a second Recommendation about consensual resolution of consumer disputes.[338] Subsequently, a Green Paper on ADR has

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[332] Directive 2008/52/EC of the European Parliament and of the Council of 21 May 2008 on Certain Aspects of Mediation in Civil and Commercial Matters ('Mediation Directive').

[333] Article 2(1) Mediation Directive.

[334] H.J. Brown & A.L. Marriot, *ADR Principles and Practice* (London: Sweet & Maxwell 1999), p. 12.

[335] Some six years since its adoption, mediation in civil and commercial matters is – despite its proven and multiple benefits – still used in less than 1% of the cases in the EU. For a general overview of the differences in regulation mediation in Europe, see Manon Schonewille and Fred Schonewille (eds.), *The variegated landscape of mediation* (The Hague: Eleven International Publishing 2014). For an in depth study, compare Guiseppe De Palo, Leonardo D'Urso, Mary Trevor, Bryan Branon, Romina Canessa, Beverly Cawyer & L. Reagan Florence, 'Rebooting' the Mediation Directive: Assessing the Limited Impact of its Implementation and Proposing Measures to Increase the Number of Mediations in the EU, Report to the European Parliament 2014, available at http://www.europarl.europa.eu/RegData/etudes/etudes/join/2014/493042/IPOL-JURI_ET(2014)493042_EN.pdf. In May 2016 the European Commission has to report on the application of the Directive and, if necessary propose amendments to the Directive. The consultation process started late September 2015. See http://ec.europe.eu/justice/newsroom/civil/opinion/ 150910_en.htm.

[336] See e.g. Girsberger, 'Die Stellung der gesicherten Gläubiger in der internationalen Insolvenz' 70 Rabels Zeitschrift für ausländisches und internationales Privatrecht 2006, 535. For an illustration, see Chancery Division 8 April 2004 (*Dobb White & Co*). The English liquidator sought the sanction of the court pursuant to section 168(3) of the Insolvency Act 1986 for a cooperation agreement between himself and a US appointed receiver of a company incorporated in the Bahamas. Both companies were understood to have been involved in a worldwide pyramid fraud scheme. As there was scope for dispute between the two office holders as to over which assets they had jurisdiction, the agreement aimed to avoid potential disputes by pooling all assets wherever located outside the US with any disagreements to be resolved by arbitration, followed by further sanction of the court.

[337] Commission Recommendation 98/275/EC, 30 March 1998.

[338] Commission Recommendation 01/310/EC, 4 April 2001.

been delivered[339] a Code of Conduct for Mediators was designed[340] and in 2008 the Mediation Directive entered into force.

105. The European Commission stated the objective of securing better access to justice, as part of the policy of the EU in further establishing an area of freedom, security and justice, which should encompass access to judicial as well as extrajudicial dispute resolution methods. The Mediation Directive should contribute to the proper functioning of the internal market, in particular as concerns the availability of mediation services. In the Directive 'mediation' is defined as '… a structured process, however named or referred to, whereby two or more parties to a dispute attempt by themselves, on a voluntary basis, to reach an agreement on the settlement of their dispute with the assistance of a mediator. This process may be initiated by the parties or suggested or ordered by a court or prescribed by the law of a Member State.'[341] It is clarified in Recital 6 why mediation should be promoted: 'Mediation can provide a cost-effective and quick extrajudicial resolution of disputes in civil and commercial matters through processes tailored to the needs of the parties. Agreements resulting from mediation are more likely to be complied with voluntarily and are more likely to preserve an amicable and sustainable relationship between the parties. These benefits become even more pronounced in situations displaying cross-border elements.'

106. Where in the EU the institution of mediation has received much support in the form of the Mediation Directive 2008/52/EC, a recent study submits that its implementation generates only mixed feelings. The study shows that the Directive's minimum common legal framework for mediation in the Member States has not been enacted in Belgium, in Finland only in relation to court-annexed mediation, whilst the Netherlands and the UK only have implemented the Directive in relation to cross-border mediation. Fully international implementation has been achieved in e.g. Spain and Portugal. According to the said study well developed and broad mediation frameworks are available in Bulgaria, Croatia, Italy and Spain, whereas Sweden and the Netherland only provide a minimum set of rules, mainly related to the enforcement of settlements.[342] Although in the genesis of the Mediation Directive, the study mentioned does not reveal, and the Reporters have not found evidence that the Commission also had in mind disputes in matters of restructuring or insolvency, it is submitted that 'civil and commercial matters' include matters of 'rescue and insolvency'.[343] However, in some countries, including Belgium and Spain mediation in rescue and insolvency occurs. Before describing these national efforts, some words on international and comparative sources relating to the topic.

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[339] COM (2002) 196, April 2002 (Green Paper on alternative dispute resolution in civil and commercial law).

[340] The Code contains principles to which mediators can commit. Mediators can do this voluntarily and under their own responsibility. The Code can be used in all civil and commercial matters. The Code describes the expertise, the impartiality and independence of the mediator, the basic principles of a settlement agreement and the confidentiality. See http://ec.europa.eu/civiljustice/adr/adr_ec_code_conduct_en.pdf.

[341] Article 3(a) Mediation Directive.

[342] Carlos Esplugues Mota (ed.), *Civil and Commercial Mediation in Europe* (Volume II: Cross-Border Mediation, Cambridge-Antwerp-Portland: intersentia 2014), 769 et seq.

[343] In a similar vein too: Horst Eidenmüller and David Griffiths, 'Mediation in Cross Border Insolvency Procedures', 2009, available at http://www.gforensics.com/resources/CrossBorderMediation.pdf.

1.1.2.2. International developments in insolvency mediation

107. At the global level 'mediation' in the pre-insolvency, informal workout period is encouraged.[344] See for example the World Bank Principles for Effective Insolvency and Creditor Rights Systems, Principle B4 ('Informal Workout Procedures'):

> 'B4.1 An informal workout process may work better if it enables creditors and debtors to use informal techniques, such as voluntary negotiation or mediation or informal dispute resolution. While a reliable method for timely resolution of inter-creditor differences is important, the financial supervisor should play a facilitating role consistent with its regulatory
> duties as opposed to actively participating in the resolution of inter-creditor differences.
>
> B4.2 Where the informal procedure relies on a formal reorganization, the formal proceeding should be able to quickly process the informal, pre-negotiated agreement.
>
> B4.3 In the context of a systemic crisis, or where levels of corporate insolvency have reached systemic levels, informal rules and procedures may need to be supplemented by interim framework enhancement measures in order to address the special needs and circumstances encountered with a view to encouraging restructuring. Such interim measures are typically designed to cover the crisis and resolution period without undermining the conventional proceedings and systems.'
>
> It seems to follow from its wording and context that the informal workout process envisaged would be assisted via voluntary negotiation or mediation conducted by a country's financial supervisor.[345] It seems too that the Principle does not address corporate insolvency cases that does not '… have reached systemic levels.'

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[344] For a preliminary study, see Bob Wessels, 'Mediation in restructuring and insolvency', Tijdschrift voor Arbitrage 2016/03, p. 59 et seq.

[345] The Asian Development Bank developed principles regarding informal workouts, including references to mediation, which should be adopted and applied as banking and financial industry standards, e.g. Principle 15 ('In endeavouring to determine disputes between creditors or between a debtor and its creditors, regard should be given to the possibility of referring such disputes, with the consent of those involved, to mediation'). The informal approach with a role of the financial supervisor acting as a mediator or providing access to independent mediators that create the conditions for negotiation among all the parties involved has been named 'The London Approach', see P. Kent, 'The London Approach', 33 Bank of England Quarterly Bulletin 1993, p. 110; P. Kent, 'Corporate Workouts – A UK Perspective, International Insolvency Review 1997, p. 165; J. Armour and S. Deakin, 'Norms in private insolvency: the 'London Approach' to the resolution of financial distress, Journal of Corporate Law Studies, 2001-1, p. 251 et seq; Ira Lieberman, Maria Gobbo, William P. Mako & Ruth L. Neyens, 'Recent International Experiences in the Use of Voluntary Workouts under Distressed Conditions', in Michael Pomerleano and William Shaw (ed.), *Corporate Restructuring: Lessons from Experience* (The World Bank 2005), p. 59. See also Bo Xie, Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue, Edward Elgar Publishing 2016, p. 22 et seq., describing the four phases in process. This special approach taken by the financial supervisor in stimulating or organizing a 'corporate workout' has been introduced or followed in Indonesia in 2000 ('Jakarta Initiative'), Turkey ('Istanbul Approach'), Korea and several other countries, see José M. Garrido, *Out-of-Court Debt Restructuring, A World Bank Study* (Washington: International Bank for Reconstruction and Development / International Development Association or The World Bank 2012). In 2005, in the Netherlands a plea was made, with reference to the London Approach, for a 'Dutch Approach' to out-of-court corporate reorganizations in the Netherlands. See J.A.A. Adriaanse, *Restructuring in the Shadow of the Law. Informal Reorganisation in the Netherlands* (Doctoral thesis, University Leiden, Deventer: Kluwer 2005). It should be noted, however, that due to the changes in (international) lending and finance (stronger capital rules for banks, the rise of hedge funds) the 'London Approach' largely has lost its original function. See Bob Wessels, *International Insolvency Law Part I. Global*

108. INSOL International, the worldwide federation of national organizations of accountants and lawyers, specializing in the broad field of insolvency, has published in 2000 a Statement of Principles for A Global Approach to Multi-Creditor Workouts (which was revised in 2017). The statement comprises eight principles indicating 'best practice' for a company experiencing financial difficulties and which has a large number of (foreign) creditors.

109. The Principles are jurisdiction-neutral and are therefore in principle applicable, irrespective of the legal system in that specific country.[346]

110. In the UNCITRAL Practice Guide (2009) suggestions are made for specific clauses to be included in cross-border insolvency agreements ('Protocols'). After having divided resolution of disputes in such cross-border agreements into two groups[347], the Practice Guide – on the basis of an assessment of cross-border protocols used in international practice – explains how continued cooperation between the proceedings in different states can be ensured and the framework established by the agreement upheld.

111. The Practice Guide has found that some dispute resolution clauses used are those in which the appointment of a third-party to resolve disputes is included: '… The agreement can particularize the mediation procedure to be followed, addressing issues such as commencement; opting-out; timetable; choice and appointment of the mediator; compensation; immunity; as well as the confidentiality of the process.'[348]

112. In the USA mediation is frequently used in insolvency procedures, including Chapter 11 cases.349 As an alternative to bankruptcy court litigation in personal bankruptcy cases mediation has been used in disputes in relation to recovering assets from third parties for the benefit of the estate, disputes relating to claims against a debtor and inter-creditor disputes about distribution of the assets of the estate.[350] In 2015 it has been contended that in the USA for complex multi-party restructurings '… the use of mediation to reach consensual plans of reorganisation, while not standard protocol in cases, has become

Perspectives on Cross-Border Insolvency Law (Wessels Insolvency Law Volume X) (4th ed., Deventer: Kluwer 2015), para. 10107. See also Sarah Paterson, 'Bargaining in Financial Restructuring: Market Norms. Legal Rights and Regulatory Standards', 14 Journal of Corporate Law Studies 2014-2, p. 333 et seq.: '… particularly the arrival of distressed debt investors in the London market, weakened and ultimately destroyed the effectiveness of the London Approach.'

[346] The publication demonstrates that the Principles are endorsed by the World Bank, the Bank of England and the British Bankers Association. For the text of the principles see Bob Wessels and Gert-Jan Boon, *Cross-Border Insolvency Law, International Instruments and Commentary*, (2nd Ed., Alphen aan den Rijn: Kluwer Law International 2015), para. 18.

[347] 'The first kind refers to disputes, which may arise with respect to the intent, interpretation, implementation or enforcement of the agreement. Other disputes may address certain kinds of (potential) conflict in the insolvency proceedings and provide special rules regarding the resolution. An example of the second kind of dispute resolution device is establishing a scheme for the submission of special claims (e.g. warranty claims) to a special tribunal, or an arbitration panel for handling issues that could otherwise involve difficult and uncertain questions of conflict of laws or choice of forum.' See UNCITRAL Practice Guide (2009), para. 74 et seq.

[348] UNCITRAL Practice Guide (2009), para. 68.

[349] I. Meier, 'Mediation and Negotiation in a Court or in an Out-of-Court Reorganization Procedure' in H. Peter, *The Challenges of Insolvency Law reform in the 21st Century: facilitating Investment and Recovery to enhance Economic Growth* (Zürich: Schulthess 2006), p. 292 et seq.

[350] See Jacob Aaron Esher, Lisa Hill Fenning, Erwin I. Katz*, The ABI Guide to Bankruptcy Mediation* (2nd ed. 2009).

common and is no longer controversial'.[351] Areas of deployment of mediation include creditors' meetings (to have creditors negotiate and agree regarding their voting on a restructuring plan – plan of arrangement) or structured negotiating to manage and resolve a large number of claims. A much talked-about mediation concerns the Lehman Brothers liquidation Chapter 11 cases to negotiate and mediate hundreds of disputes arising from derivative contracts due to Lehman's filing for bankruptcy.

113. From a report of January 2016 follows in the case of Lehman Brothers Holding Inc and its affiliates that 495 ADR-processes have resulted in a sum passing the $3 billion mark for the various estates. Settlements have been achieved in 424 ADR matters involving 541 counterparties. Until 13 January 2016 245 ADR matters that have reached the mediation stage and been concluded, 232 have been settled in or subsequent to mediation; only 13 mediations have terminated and remain unsettled.[352] So recently, in the USA, mediation has been used in larger, multi-party reorganisations. The costs of the mediation, including the compensation of the mediator, were paid by the estate.[353] The purpose of these mediations is for all parties to discover a way to find common ground while protecting their interests: 'Its ultimate success in large and complex chapter 11 cases stems from facilitating parties' goals rather than simply evaluating the merits of their positions … and the interests of all creditors for an expeditious resolution, rather than years of deadlocked litigation.'[354] Esher submits that in the EU mediation in insolvency '… may be problematic without some form of court or regularly compulsion.'[355]

114. In December 2014, the ABI Commission on the reform of Chapter 11 reports that the commission has discussed a proposal for a more structured process for exchanging information and establishing the parameters of bargaining, as well as whether the court should be involved in the process from the outset. The Commission perceived value in the mediator's role, but expressed concerns regarding costs and a 'one-size-fits-all' approach to

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351 Jack Esher, 'Recent Use of Mediation for Resolution and Effective Management of Large Case Insolvencies', International Corporate Rescue 2015-6, p. 349 et seq.

352 Letter to Honorable Shelley C. Chapman Regarding Seventy-third ADR* Status Report, see https://www.americancollegeofbankruptcy.com/file.cfm/31/docs/Mediation%20in%20restructuring%20and%20insolvency%20-%20Tijdschrift%20voor%20Arbitrage.pdf.

353 Cases included Residential Capital LLC, Cencage Learning Inc., Nortel Networks, Radio Shack and Energy Future Holdings Corp. See Jack Esher, 'Recent Use of Mediation for Resolution and Effective Management of Large Case Insolvencies', International Corporate Rescue 2015-6, at 350/351, and Benjamin D. Feder and David Hahn, 'Mediation in Large Chapter 11 Cases', available at http://www.abi.org/committee-post/mediation-in-large-chapter-11-cases. Many bankruptcy judges are appointed as mediators, see e.g. in Residential Capital: Hon. James M. Peck, 'Settlement Talks in Chapter 11 After "WAMU": A Plan Mediator's Perspective', 22 American Bankruptcy Law Review 2014, p. 65 et seq. For reasons to involve judges in mediation, see Janice Miller Karlin, 'The "M" Word: Mediation Musings', ABI Journal 26 November 2015, 26 et seq. The American Bankruptcy Institute (ABI) has established its Bankruptcy Court Local Mediation Rule (Rule 9019), to assist courts in setting up standards for organisation of court assigned mediation, see e.g. for the U.S. Bankruptcy Court District of Delaware, 'Rule 9019-5 Mediation', http://www.deb.uscourts.gov/content/rule-9019-5-mediation. Since some five years the American Bankruptcy Institute/St. John's Bankruptcy Mediation training of forty hours is open for all interested in insolvency mediation.

354 Benjamin D. Feder and David Hahn, 'Mediation in Large Chapter 11 Cases', available at http://www.abi.org/committee-post/mediation-in-large-chapter-11-cases.

355 Jack Esher, 'Recent Use of Mediation for Resolution and Effective Management of Large Case Insolvencies', International Corporate Rescue 2015-6, at p. 351.

a mediator. It concluded that a mediator likely would be an asset in many cases, but believed it would be a more effective tool if invoked based on the facts of the particular case.[356]

1.1.2.3. Insolvency mediation in the EU

115. In the EU mediation in matters of insolvency are dealt with in some Member States, but at its development appears to remain in its infancy. In many Member States, mediation is a tool used in restructuring negotiations without specific provisions in the respective insolvency or law[357] while a number of jurisdictions actually provide for a type of mediator. In Belgium, for matters of insolvency, a schuldbemiddelaar' or 'mediateur de dettes' is mentioned in Annex B to the EIR (2015). As of its entry into force in 2009, the Belgium Act on the Continuity of Companies Wet Continuiteit Ondernemingen (WCO)) contains an article about a company intermediary ('ondernemingsbemiddelaar') who can help reorganise the company.[358] The WCO does, however, not clarify its specific role. In the UK, the Chancery Court Guide 2016 stated that 'where appropriate the court will encourage the parties to use alternative dispute resolution (on which see Chapter 17) or otherwise help them settle the case.'[359] In particular, the court will readily grant a short stay at allocation or at any other stage to accommodate mediation or any other form of settlement negotiations. The court will not, however, normally grant an open-ended stay for such purposes and if, for any reason, a lengthy stay is granted it will be on terms that the parties report to the court on a regular basis in respect of their negotiations. In the French legal system of mandataire ad hoc and règlement amiable/conciliation an out-of-court workout is enhanced. It is typically initiated by the debtor.

116. Specific mention should be made of a pilot project 'mediation in bankruptcy liquidation cases', running in the Netherlands and initiated by the District Court in Amsterdam in 2012. The aim is to investigate whether procedures initiated by or against the insolvency practitioner ('*curator*') can be solved more quickly and at lower cost through mediation, so as to preserve a greater proportion of the debtor's estate for the benefit of the creditors.[360] The pilot is in line with the declared intention of the Minister of Justice and Security to promote dispute resolution through mediation. The mediation processes are supervised by experienced mediators. The (supervisory) judge does not participate in the mediation, but, in the context of its supervisory role to agree with it in a solution reached through mediation. A protocol has been prepared for the procedure and the court has established a Mediation Bureau and compiled a list of professional mediators who are familiar with insolvency. Although still early to draw conclusions, the first impressions (after some two years, based

[356] ABI Report (2014), at 161. In the report, at 181, the deployment of a mediator is suggested in valuation matters.

[357] See, for instance, Uwe Kassing, 'Mediation im Insolvenzrecht – Sanierungsmediation', in Fritjof Haft and Katharina Gräfin von Schlieffen (eds), *Handbuch Mediation* (3rd ed. Beck 2016) for Germany.

[358] Section 13 of the Act on Continuity of Companies, available at http://www.staatsbladclip.be/staatsblad/wetten/2009/02/09/wet-2009009047.html. See Bart de Moor, 'Gegevensverzameling, de handelsonderzoeken en de ondernemingsbemiddelaar', in Stan Brijs Yves Brulard, Bart De Moor, Charles Gheur, Sophie Jacmain, *De wet betreffende de continuïteit van de ondernemingen* (Louvain-la-Neuve, Anthemis 2010), p. 48 et seq.

[359] See Article 18.2 of the Guide, available at https://www.judiciary.gov.uk/wp-content/uploads/2016/02/chancery-guide-feb-2016.pdf.

[360] C.H. Lankhorst, 'Mediation ook in faillissementszaken?' Bedrijfsjuridische berichten 2012/32.

on some 20 cases) have been regarded as positive[361], although more recent impressions demonstrate that other courts in the Netherlands (apart from the District Court in Rotterdam) seem reluctant to fully support mediation.[362] In the light of the Recommendation of March 2014, in the Netherlands further study of the weaving of ADR methods into (threatening) insolvency has been called for.

117. In 2013 the Spanish Insolvency Act has included a new chapter regulating the 'insolvency mediator' and the extrajudicial settlement of payments ('ESP') as a form of negotiating the debts of the entrepreneurs. The goal of an ESP is to guarantee that a business failure does not result in impoverishment and frustration to the extent of inhibiting an entrepreneur from starting a new venture, but rather as a means to learn and progress. This process is supervised by an independent professional, an insolvency mediator. S/he promotes and coordinates the entrepreneur's process by carrying out different tasks and applying procedures as stated in the Act. The insolvency mediator has the authority to summon the creditors and the debtor to a meeting and put in place a payment plan for all debts to be paid. S/he will be named by the commercial registrar or by a public notary of the debtor's place of residence, from among the mediators included in the list of Spanish Mediators and Mediation Institutions. The parties will inform the insolvency administrator of the commencement of the ESP. Within the first ten days of being appointed, the insolvency mediator will make a list of all debts and, within the following two months, will convene a meeting with the debtor and their creditors to negotiate a binding agreement. The insolvency mediator is responsible for assisting the parties in reaching an ESP and in supervising its compliance. The insolvency mediator also has the right to request the start of the insolvency proceedings before a judge, if the negotiations are not moving forward, if the payment plan is not accepted or if the ESP is breached. In the event that the insolvency mediator refers the insolvency proceeding to a judge for determination, the judge will appoint the insolvency mediator as the insolvency administrator, giving rise to the so-called 'consecutive insolvency'.[363] In other EU Member States mediation in insolvency has not yet become a specified tool.[364]

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[361] Annet Draaijer and Toni van Hees, 'Pilot mediation in faillissementszaken', Tijdschrift voor Insolventierecht 2013/40; J.A.A. Adriaanse and E.J.M. van Beukering-Rosmuller, 'ADR/Mediation bij (dreigende) insolventie', Tijdschrift voor Arbitrage 2014/51. For an initial impetus for a method to prevent (international) insolvencies – also using psychological methods – see Jan A.A. Adriaanse, Ellen J.M. van Beukering and Jean-Pierre I. van der Rest, 'Een aanzet voor een methodiek tot het voorkomen van (internationale) insolventies', Nederlands-Vlaams tijdschrift voor Mediation and conflictmanagement 2015 (19) 1, p. 45 et seq., concluding that Harvard negotiation principles and the INSOL Principles for a Global Approach to Multi-Creditor Workouts (see para. 1.1.2.2) fulfil a useful contribution for a structured process of financial restructuring, in which the involvement of a neutral/mediator with specific knowhow and conflict-management techniques will be essential for a solution which is acceptable for all parties.

[362] See http://www.innovatierechtsbestel.nl.

[363] The ESP allows to cram down dissenting creditors (also secured creditors) if certain majorities are achieved. The ESP is only open for individuals (entrepreneurs or not) or small companies (i.e., companies with less than 50 creditors, estimated liabilities or estimated appraisal of assets that do not exceed EUR 5 million) which are in an insolvent situation may resort to this refinancing mechanism. During negotiations by way of a Pre-insolvency Notice, the debtor may file for a three-month additional period to carry out the out-of-court negotiations, without having to file for insolvency. Such a notice may be filed by the debtor, the trade registrar or the notary public in charge of appointing the mediator. If, after this period, the insolvency situation persists the debtor will have to file for insolvency in the following month. See Augustín Bou, 'Too Many Ineffective Amendments to the Spanish Insolvency Law', International Corporate Rescue 2015, p. 162 et seq.; Laura Ruiz, 'Spanish Insolvency Act: the legislation created by the crisis', Insolvency and Restructuring International,

1.1.2.4. Impetus for recommendation

118. Positive experience in a few jurisdictions where mediation is actively used to resolve restructuring and insolvency related disputes should prompt legislators to recognise that introducing a mediator can avoid unnecessary costs and delay from litigation or deadlock about unresolved disputes. Mediation can also effectively assist parties in reaching a compromise on a restructuring plan, provided that a mediator acts independently. A careful balance should be applied in that an increasing role for mediators will only make sense where there are mediator-suitable disputes. For instance, where the business is simply to be sold on a going concern basis to a new owner, there does not seem any room for a mediator. Moreover, making mediation mandatory might be risky given they will charge costs to the estate, for which reason there needs to be checks and balances (e.g. creditor control over decision to appoint a mediator).

119. To further the idea of mediation, European institutions should support a comparative and empirical study on the (desired) use of mediation in restructuring and insolvency matters. Such a study should encompass a focused approach on the status of ‘mediation in restructuring and insolvency’ in the EU Member States and the role and professional qualification of an ‘insolvency mediator’ in a national setting. It would include study and proposals regarding the general civil/procedural framework necessary to function fully satisfactory as such a mediator, such as the criteria under which a court should appoint a mediator, the basics of a mediation agreement, the professional qualifications of a mediator, rules on confidentiality, rules on referral of courts to mediation, who initiates mediation, legal effect of mediation (prescription terms; pending proceedings). Such a study should be comparative in nature (EU Member States), should include the USA as well and should also concentrate on the question which topics should be subject to of form of regulation on EU level and which ones can be left to the EU Member States.[365]

September 2015, p. 25 et seq; Alberto Núnez-Lagos Burguera, ‘Recently Enacted Spanish Out-of-Court Debt Restructuring Laws Join the Current European Trend for Efficient Restructuring and lead Innovation for Restructuring Solutions’, in International Corporate Rescue 2015, p. 216 et seq. In 2015 some amendments to the mechanism of the ESP and the role of the mediator have been introduced. See Pilar Galeote, ‘Mediación Concursal El acuerdo extrajudicial de pagos y el mediador concursal’, 2015, available at http://ssrn.com/abstract=2659255.

[364] In Germany, in a proposal for legislation to deal with group insolvencies a group coordinator (*Koordinationsverwalter*) can be appointed, an independent person, who could align proceedings and also can act as a mediator to mediate between the individually appointed insolvency office holders, see Deutscher Bundestag, 18. Wahlperiode, Drucksache 18/407, p. 23.

[365] For further study, see e.g. Richard Heuser, *Schiedsgerichtbarkeit und Mediation im Insolvenzverfahren* (Frankfurt am Main: Peter Lang 2011); Luise Graf-Schlicker, ‘Mediation in Deutschland: Auf dem Weg zu gesetzlichen Regelungen’, in Andreas Büchler, Markus Müller-Chen, Ingeborg H. Schwenzer (eds.), *Private Law – national – global – comparative, Festschrift für Ingeborg Schwenzer zum 60. Geburtstag* (Stämpfli Verlag AG Bern/intersentia 2011), p. 609-622; José M. Garrido, *Out-of-Court Debt Restructuring, A World Bank Study* (Washington: International Bank for Reconstruction and Development / International Development Association or The World Bank 2012), para. 94 et seq.; Maximilian Gimbel, *Mediation in Unternehmenskrise und Insolvenz* (Bremen: EHV Academic GmbH 2014); Sarah Paterson, ‘Bargaining in Financial Restructuring: Market Norms. Legal Rights and Regulatory Standards’, 14 Journal of Corporate Law Studies 2014-2, p. 333 et seq.; Remo Caponi, ‘”Just Settlement” or “Just About Settlement”? Mediated Agreements. A Comparative Overview of the Basics‘, 79 Rabels Zeitschrift für ausländisches und internationales Privatrecht 2015, p. 117.

1.1.2.5. Recommendations

Recommendation 1.07: Member States should consider making more explicit provision for the involvement of mediators to resolve restructuring and insolvency disputes. Member States should recognise that the performance of a task in matters of restructuring and insolvency by a mediator could avoid unnecessary costs and could effectively assist parties in reaching a compromise on a restructuring plan, under the condition that a mediator acts independently.

Recommendation 1.08: In Member States where mediation is, or will soon be, an accepted form of dispute resolution in commercial cases, professional organisations should be encouraged to include mediators in restructuring and insolvency matters into a system of adherence to requisite standards of performance necessary for a fit and proper exercise of their task, where there is a dispute for which a mediator could usefully play a role and subject to controls designed to avoid unnecessary costs.

Recommendation 1.09: The European Commission or other European institutions should support a comparative and empirical study on the (desired) use of mediation in restructuring and insolvency matters.

1.1.3. Role of a Supervisor

120. With a similar background as the introduction of a mediator, the Recommendation of March 2014 opens the doors of the market of restructuring and insolvency laws for a 'supervisor'.[366] Such a supervisor should be appointed by a court on a case by case basis with the rationale to limit court formalities and to promote efficiency and reduce delays and costs. Under the heading of 'facilitating negotiations on restructuring plans', and the subheading 'Appointment of a mediator or a supervisor', recommendations 8 and 9 determine (as far as a supervisor concerns):

> 8. Debtors should be able to enter a process for restructuring their business without the need to formally open court proceedings.
> 9. The appointment of … a supervisor by the court should not be compulsory, but rather be made on a case by case basis where it considers such appointment necessary: … (b) in the case of a supervisor, in order to oversee the activity of the debtor and creditors and take the necessary measures to safeguard the legitimate interests of one or more creditors or another interested party.'[367]

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[366] Confirmed in the explanation to Article 5 of the Proposal Restructuring Directive (2016). The Recommendation of March 2014 provides: '(17) To promote efficiency and reduce delays and costs, national preventive restructuring frameworks should include flexible procedures limiting court formalities to where they are necessary and proportionate in order to safeguard the interests of creditors and other interested parties likely to be affected. For example, to avoid unnecessary costs and reflect the early nature of the procedure, debtors should in principle be left in control of their assets and the appointment of a mediator or a supervisor should not be compulsory, but made on a case-by-case basis.'

[367] With a similar role in the Proposal Restructuring Directive (2016) a 'practitioner in the field of restructuring' is introduced, see Bob Wessels, 'If you're the IP, I'm the Pifor', Global Restructuring Review December 2016, p. 26-27.

1.1.3.1. International developments regarding a supervisor

121. The term ‘supervisor’ is not unknown in the land of insolvency. The UNCITRAL Legislative Guide, in recommendation 156, provides:

> ‘(156) The law may establish a mechanism for supervising implementation of the plan, which may include supervision by the court, by a court-appointed supervisor, by the insolvency representative, or by a creditor-appointed supervisor.’

Compared to the Recommendation, it is immediately clear from the text that the latter ‘supervisor’ has a much more limited task (supervising the implementation of a plan), whilst an appointee also could be another person or body than a court. In the Guide[368] the starting point is that in practice many plans can be executed by the debtor without the need for further intervention or supervision by the court or the insolvency representative. The Guide has found that especially in the case of a debtor-in-possession reorganization. However, under other laws that provide for the proceedings to conclude when the plan has been fully implemented, it may sometimes be necessary for the implementation to be supervised or controlled by an independent person. The UNCITRAL Legislative Guide expresses: ‘Under several insolvency laws the court has an ongoing role in supervision of the debtor after approval of the plan, pending completion of its implementation. This may be important where issues of interpretation of the performance or obligations of the debtor or others arise. Some countries provide for the court to authorize continued supervision of the affairs of the debtor, to varying degrees, by a supervisor or insolvency representative after approval of the plan. A further approach permits creditors to appoint a supervisor or representative to oversee implementation of the plan.’[369]

122. As part of the overall governance structure, the ABI Commission suggesting revisions to the Chapter 11 proceedings[370] recommends the introduction of a new phenomenon, the ‘estate neutral’, which will replace any reference in the U.S. Bankruptcy Code’s text to an ‘examiner’. Under existing American bankruptcy law, next to the relatively rare figure of a chapter 11 ‘trustee’, a supplement to the debtor in possession is an examiner, which may be appointed to investigate the affairs of the debtor. Regarding its legal powers it is noted that an examiner does not displace the debtor in possession or its management.[371] The ABI Commission presents research from which it follows that since the early 1990s an examiner was appointed in some 7 percent of the larger cases, mainly in ‘huge’, contentious cases. Allegations of corporate fraud and misconduct by a debtor’s insiders or affiliates are often cited as reasons for appointing an examiner so that the examiner may investigate such allegations. The Commission mentions as examples the examiner’s reports in the chapter 11

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[368] UNCITRAL Practice Guide (2009), para. 69.

[369] The UNCITRAL Legislative Guide (2004) then continues (para. 70) for these cases where the debtor defaults in performing its obligations under the plan or implementation of the plan breaks down for some other reason. It has found that some insolvency laws provide that the court can terminate the plan and convert the proceedings to liquidation, other laws laws provide that the plan will only be terminated in respect of the specific obligation breached (it otherwise remains valid) or sometimes the plan itself contains provisions regarding default.

[370] See ABI Report (2014), Chapter 1 Introduction, para. 22.

[371] Examinership is only available if no trustee has been appointed and only upon request of a party in interest or the U.S. Trustee and after notice and a hearing. See Clifford J. White III and Walter W. Theus, Jr., ‘Chapter 11 Trustees and Examiners after BAPCA’, 80 American Bankruptcy Law Journal 2006, p. 289 et seq.

cases of Lehman Brothers, Residential Capital, and Tribune Company. These reports assessed the merits of claims asserted by parties in the case, identified additional potential claims and causes of action, and provided parties in interest with substantial information concerning the debtor and its case that otherwise likely would have been undiscovered or unavailable.[372] Notwithstanding the merits of the current role of an examiner, the Commission determined that the new concept of an 'estate neutral' should replace examiners under the Bankruptcy Code. The task of such an estate neutral would be very flexible and would depend very much on the case at hand. The tasks or role would therefore not be clearly outlined or demarcated in the Code. An estate neutral could be appointed particularly in cases when, for example, stakeholders found value in leaving the debtor in possession in control, but certain matters in the case needed an independent assessment either because it was difficult for a debtor to investigate itself or because the debtor and stakeholders were too vested in their respective positions to identify areas of potential compromise. In general, an estate neutral could have a more extensive role from that of a traditional examiner in chapter 11 cases, including roles such as facilitating dispute resolution and reducing information asymmetries.[373]

1.1.3.2. Court appointed supervisors in the EU

123. The function of a supervisor has been reported in two EU Member States. In Austria in certain cases, the supervision of the performance under a reorganisation plan is conducted by a trustee (Treuhänder). The supervision over the Reorganisation Proceedings with Self-Administration is divided between the insolvency court, the reorganisation administrator (Sanierungsverwalter) and the creditors' committee (Gläubigerausschuss). In certain cases, however, the supervision of the performance under a reorganisation plan is also conducted by a trustee (Treuhänder). In France, both Mandat ad hoc and conciliation proceedings are conducted under the supervision of a court-appointed practitioner (mandataire ad hoc or conciliateur) to help the debtor reach an agreement with its creditors. In French practice this would typically involve negotiations to reduce or reschedule the debtor's indebtedness.

1.1.3.3. Impetus for recommendation

124. Considering that a number of actors can assume the task of supervision the administrator of the estate, there may not be any additional value in adding another supervisor to a legal framework. Hence, Member States should assess carefully whether a supervisor could be useful, possibly for the quality and effectiveness of the execution and

[372] Report of Kenneth N. Klee, Examiner, *In re Tribune Co*., No. 08-13141 (July 26, 2010); Report of Anton R. Valukas, Examiner, *In re Lehman Bros. Holdings, Inc.*, No 08-13555 (Bankr. S.D.N.Y. Mar. 11, 2010); Report of Arthur J. Gonzalez, Examiner, *In re Residential Capital, LLC,* No. 12-12020 (Bankr. S.D.N.Y. May 13, 2013). The Report discloses that Kenneth N. Klee and Arthur J. Gonzalez are Commissioners.

[373] See Michelle Harner, 'Creating Right Tools for Distressed Companies and Their Creditors', ABI Journal 8 November 2015, p. 8 et seq., explaining that inspiration for the concept of 'estate neutral' also was provided by the report on an international working group. That group was chaired by Wessels and De Weijs, see Bob Wessels and Rolef J. de Weijs, 'The Reform of Chapter 11: Its Process and the Recommendations Made', in Bob Wessels and Rolef J. de Weijs (eds.), *International Contribution to the Reform of Chapter 11 U.S. Bankruptcy Code* (European and International Insolvency Law Studies 2, The Hague: Eleven International Publishing 2015), p, 3 et seq. The book contains reports of 13 countries all over the globe.

implementation of a restructuring plan or in safeguarding a moratorium for the protection of pre-insolvency negotiations, in their framework. If a supervisor is introduced, Member States should put in place legal and professional rules providing a supervisor with a legitimate basis in national law and a set of rights, obligations and professional rules that guarantee a proper functioning in its activities. In any case a supervisor must act independently and should be accountable for its performance to its appointee, be that a court or a committee of creditors.

1.1.3.4. Recommendations

Recommendation 1.10: Member States should assess whether a supervisor would bring additional value to their legal framework. If they conclude so, Member States should put in place legal and professional rules including rules on the independence and accountability of supervisors.

1.1.4. Insolvency practitioners

125. In the EU, for matters of restructuring and insolvency the most important actors in nearly any insolvency proceeding are the courts and the respective insolvency practitioners. Their authorities and roles are based on or limited to the provisions of domestic law. In cases where a role of an actor extends beyond the implementation of mandatory rules of insolvency law, it will be determined – generally – by contract, for instance the services of a turnaround advisor. The status, power and supervision of such an advisor will be regulated by contract and, as the case may be, by applicable professional or ethical rules which apply to the actors concerned.

1.1.4.1. Significant elements from National Reports

126. A limited set of questions concerning an insolvency practitioner has been posed to the National Reporters. The responses to these questions are being ordered in a general way below. It should be stressed that this ordering does not assess matters that are of indirect or direct influence on the performance of insolvency practitioners, such as the strength or the weakness of a national insolvency system, the openness towards (or the reluctance to) changes in insolvency legislation or the overall professionalism of an association of insolvency practitioners, whilst also no research has been done to the efficiency and effectiveness of the functioning of IPs in their day-to-day work. The responses serve to demonstrate the heterogeneity of the manner in which principle and practical issues concerning IPs have been worked into a national legal framework. These questions posed were the following.

Who may be appointed to act as an insolvency practitioner?

127. In the 13 countries reviewed, an IP could be:

(i) a (bar-registered) lawyer (in Belgium in bankruptcy cases; Greece; in Italy the commissari giudiziali; common practice in the Netherlands);

(ii) a specifically designated professional (in England and Wales: a licenced insolvency officeholder, licence to be provided by one of seven professional bodies, including accountancy and law; in France: a mandataire judiciare; Latvia; in Greece: a licensed statutory auditor or A' class accountant/tax consultant); or
(iii) an expert with business knowledge of experience (with a variety of requirements: Austria, in Belgium in a non-bankruptcy case, Germany; Sweden).

128. In all these cases, national specific eligibility criteria apply, such as age, level of knowledge, reputation, certain amount of years of experience, independence, impartiality, mandatory training, a 'clean slate' (no criminal convictions, not having been declared bankrupt, no outstanding debts etc.). Only individuals can be appointed (Germany, England and Wales, Sweden), not companies (as is however the requirement in Hungary).[374] In Spain a company can be appointed, when at least one of its members is a registered lawyer and another of its members is an economist or an auditor.

How are they appointed?

129. The results of our survey generally lead to five models:
(i) IP selection and appointment by the court, e.g. France, Germany (unless preliminary creditors' committee is established), Greece, Netherlands, Poland, Spain, Sweden);
(ii) creditors' influence on the selection of the IP (Belgium, Bulgaria, England, Estonia, Romania);
(iii) debtor's influence or debtor itself (Belgium);
(iv) selection without involvement of a court or of creditors (e.g. via drawing by lot or an electronic system) (Hungary, Lithuania, Slovak Republic, Slovenia); or
(v) selection and appointment by a state agency (Latvia, in case the debtor and the creditors cannot agree on a particular candidate). In Latvia, the insolvency administrator is supervised by government agency and the court. The agency supervises the performance of the insolvency administrator and is entitled to issue binding resolutions (for instance to oblige the administrator to request the

[374] For a fundamental view, see the German Constitutional Court (*Bundesverfassungsgericht*), 12 January 2016, deciding: '36: [T]he work of insolvency practitioners cannot be regarded any more as a mere activity on the side when working as a lawyer, tax advisor, business advisor or accountant … It is beyond any doubt, that the function of an insolvency practitioner should be based of the requirements of an independent autonomous profession …', and '62: [T]he exclusion of legal persons from the position of insolvency administrator is to ensure the proper conduct of insolvency proceedings, which serves a legal value of high rank (*dient einem Rechtsgut von hohem Rang*). As has been demonstrated, the insolvency procedure aims as part of the foreclosure law directly the protection and enforcement of constitutionally protected private interests and is an essential element in the judicial guarantee owed by the State (*der vom Staat geschuldeten Justizgewähr*) ... Given this high importance of insolvency proceedings for the rights, protected by the constitution, the exclusion of a legal person is not un-proportional in relation to the goal of ensuring effective insolvency proceedings, which is laid down in the Act by the assurance that follows from the personal trust in the person of the insolvency administrator, who is supervised by the insolvency court', ZIP 7/2016, 321, with commentary of Römermann; EWiR 5/2016, with commentary of Flöther. See Beck, 'Wann – endlich – kommt das Berufsrecht für Insolvenzverwalter?', NZI 5/2016; Hanns Prütting, 'Eigenständiges Berufsrecht für Insolvenzverwalter?', Marie Louise Graf-Schlicker, Wilhelm Uhlenbruck, Hanns Prütting (eds), *Festschrift für Heinz Vallender zum 65. Geburtstag* (Köln: RWS Verlag Kommunikationsforum GmbH 2015), p. 471-488.

termination of particular procedure because the debtor does not comply with the plan).[375]

What powers do they have in each relevant procedure?

130. As the National Reports indicate, nearly all laws the insolvency practitioner's powers flow directly from the applicable law. National law allows an insolvency practitioner to take measures or intervene in legal positions that he would not be allowed to without such laws. Across countries the powers of an IP are tailored to specific proceedings, but in as far as they relate to the debtors' assets they are generally broad, e.g. to manage the debtor's business, enter into new contracts on its behalf, sell its assets, decide on the executory contracts, collect outstanding claims of the debtor, preserve all rights and claims of the debtor, decide on pending law suits or payment of creditors. There are differences across countries as to how certain important actions the IP wishes to take are regulated, such as whether the IP needs prior approval of a supervisory judge, the court or a creditors' committee for e.g. the continuation of the business activities, the immediate sale of perishable goods, the continuation of pending proceedings, concluding a settlement with creditors, an interim payment to creditors, the initiation of liability proceedings against management, payment of the secured creditor against release of the collateral or a private (non-auction) sale of certain property. Certain powers of an IP directly relate to or flow from the execution of the powers mentioned, such as (again differently ordered depending on the country and specific proceeding in issue) (a) gathering of the estate and its assets, among which also actions to 'reconstruct' the estate, for example via an action of setting a previous transaction aside, (b) drawing up an inventory list of the assets and the preservation of the estate and ensure that there are no assets being dissipated, (c) describing the estate, as well as valuate its components and (d) drawing up a statement of assets and liabilities, showing the nature and amount of the assets and the debts of the estate show, and the identity of the creditors and the amount of their claim (including, where relevant, a verification of claims process).

What duties do they owe, and to whom? What sanctions apply for breach of duty, and do they include any risk of personal liability?

131. The variety of responses in this section continue. In nearly all countries where it applies a distinction is made between formal proceedings and actions of practitioners outside a formal scope. Duties of a practitioner exist based on a general norm (e.g. to supervise the business, Austria in URG proceedings; duty is to ensure a fair balance between the interests of the company, the creditors and any other parties involve, in an English CVA), with a general content (e.g. the diligence required by a 'good' office holder; the professional standards and conduct expected from an authorised insolvency officeholder; he must act as

[375] In Germany the debate is fierce on topics as whether the limitation of the appointment as Verwalter is justified (Christopher Seagon, 'Beschränkung des Verwalteramts auf natürliche Personen: Ungleichbehandlung aus gutem Grund!', NZI 2015, p. 825 et seq.) and whether professional rules lawyers apply to the autonomous function of IOH, as accepted by AGH Munich 17 February 2014, ZIP 17/2014, 830, with critical commentary by Römermann, and Federal Supreme Court 6 July 2015, ZIP 2015, 1546. Against that e.g. the Verband Insolvenzverwalter Deutschlands (VID), the German Association of IOHs. See also Thorsten Graeber, 'Die Entwicklung der Verwalterauswahl under der Insolvenzordnung', in Marie Louise Graf-Schlicker, Wilhelm Uhlenbruck, Hanns Prütting (eds), *Festschrift für Heinz Vallender zum 65. Geburtstag* (Köln: RWS Verlag Kommunikationsforum GmbH 2015), p. 165-182, and Frank Pollmächer and Klaus Siemon, 'Der Bunderinsolvenzverwalter für die InsO oder die unverbindliche Vorauswahlliste', NZI 4?2017, p. 93-99.

is reasonably expected of an administrator with due understanding and experience, who fulfils his task with punctiliousness and commitment), sometimes reflecting a light benchmark (light negligence), either to specific persons or towards all persons within the realm of the interests the IOH is to protect. In Sweden the Company Reorganisation Act does not include any provisions regarding liability to pay for damages for the administrator, but in literature it is submitted that the same liability as under the Bankruptcy Act shall apply also to administrators in a company reorganization, but this is still an open question. Specific duties may exist based on specific norms (e.g. to report, to convene a meeting) and the French report also mentions a criminal liability for the office holder. In matters of civil liability either specific rules apply or often general principles of a countries' civil law. In Greece for instance, the insolvency administrators (syndicos), the special administrator under L. 4307/2014 and the special agent are liable towards the debtor and the creditors for any fault, whereas towards any third party they are liable only for malice or gross negligence.

132. Liability itself can be attached to the function of an IOH (in its quality as IOH) as well as personal, e.g. for the total amount of losses and has to be established within the formal insolvency proceeding or in general civil proceedings. In Poland for instance the receiver, court supervisor and administrator appointed in the respective proceedings act in their own name but on account of the bankrupt debtor; they are not liable for obligations contracted in matters concerning the bankruptcy estate, but can be liable for any damage resulting from improper performance of their duties. In nearly all countries, in formal proceedings, an IOH can be dismissed or replaced, either at the request of all parties, of a specific party, at its own request of by the court ex officio. In some a court can order that the administrator carries out a specific act or does not carry out a specific act or that the administrator call a creditors' meeting to consider a specific resolution.

133. Some countries possess a disciplinary process when violating general norms (e.g. any violation of professional ethics, and any failure of integrity or honour, even relating to facts unconnected with professional practice), can be sanctioned (e.g. in France, England, Hungary).The Spanish report notes that there are no specific duties set forth for the insolvency mediator apart of the general powers he has, whilst there is no sanction regime for the insolvency mediators, as opposed to what happens with insolvency administrators.

What reporting obligations do they come under?

134. A great variety of matters are published or notified in several ways (internet, official gazette, general notices) towards a variety of addressees: the general public (available information of any practitioner making his potential services known), all creditors or to specific addressees, such as a registration of companies (in Hungary online submission), shareholders, an employees' representative or a public prosecutor (Belgium, France). In Germany the creditors' meeting (which is bound by confidentiality) may require the insolvency practitioner to give specific information. In case of notices certain forms are prescribed and certain periods should be obeyed, e.g. the fact of being appointed, the date certain proceedings have started, the aim of the proceedings, notifications for creditors' meetings, whether the proceeding involves creditors from other countries. A central duty in nearly all countries is the requirement to notify all (known) creditors to submit their claims

for verification purposes. Reporting duties may be related to the specific goal of the involved expert (an opinion of a third person to the court, filing of certain documents), regarding specific matters of the estate or the intention to initiate certain proceedings (in case of transaction avoidance or directors' liability), regarding certain transactions (e.g. exceeding a certain amount). Information or reporting duties also may relate to the continued performance of the business after a restructuring process has started or related to the mandatory involvement of a creditors' committee. Many times interim or progress reports to a court, a company registration (Italy)[376] or a creditors' committee are mandatory, as is full and detailed reporting (on managing the affairs of the debtor, including financial accountability, the causes of the company's troubles) may be related to the finalization of a restructuring process or the termination or conversion of certain proceedings. In Poland periodically and yearly reporting duties exit to tax and social security authorities. Many times (interim) reports are accessible by the general public, but in some countries access is limited to certain persons in interest, such as the creditors, in some cases access is possible only after the approval of the (supervisory) judge. Availability may differ (and overlap): the office of the IOH or a bailiff's office (in Germany reports are part of the court's files and may be inspected by creditors without further prerequisites) or a website. In France progress reports shall not become public. In Greece the insolvency administrator (syndicos) is obliged to submit to the creditors' meeting a report on the financial situation of the debtor and the causes that led to bankruptcy, the prospects of preserving the business as a whole or in part, its potential viability and the possibility of the debtor's entering into a reorganization plan, as well as the projected consequences regarding the satisfaction of creditors. Also, the insolvency administrator is obliged to submit a report describing his work progress to the supervisory judge every six months. In special administration procedure, the administrator is responsible for all publications relating to the public auction (publication of invitation to potential investors, publication of the court decision that accepts the selection of the highest bidder etc), and for the publications relating to the distribution of the auction proceeds. Moreover, the administrator is responsible to notify all the auction's participants on the selection of the highest bidder. In Spain, for the insolvency mediator there is no particular information obligation.

How are they remunerated?

135. In theory, the remuneration of an insolvency office holders could be arranged in several ways. It could be a 'salary' in these instances in which an IOH is a public official, employee of the State or a state's agency. In the countries in our survey we have not seen examples. The remuneration could be based on an hourly rate (in the Netherlands calculated per six minutes time units; in Belgium the system mandates a fee quote to the court's approval; in England and Wales since 1 October 2015 administrators, liquidators and trustees in bankruptcy also have the duty to provide fee estimates to creditors), a fixed rate, a percentage of realisations from the debtor's estate, a combination of the foregoing or (as in Latvia) an agreement with the debtor (in case there is no agreement the remuneration is

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[376] In Article 161, VIII co. of Italian insolvency law it is stated that "after filing of the application for a concordato preventivo proceeding and before the filing of the plan and the proposal to creditors, the debtor has to file, on a monthly basis, a financial situation of its activity. Such situation is published in the companies register by the court's clerk ('cancelliere')."

one minimal wage per month).[377] The sum received may include certain costs, including costs for third party advice. Such a general rate is related to a described basis (value of the assets; results achieved during trading of business) and could be adjusted by a regressive percentage calculated by referring to the value of the assets or progressively based on, for example, the experience of the insolvency practitioner and the complexity of the case. Another model – in some countries supplying the basic remuneration system – is that remuneration is affected by the outcome of the procedure (for example, through payment of a 'bonus' for the realisation and distribution or maximisation of recoveries or rescue of the debtor's business).

136. In all models it might be possible that any outcome is limited to a maximum amount of remuneration that can be charged by an insolvency practitioner. In many models the final determination – in formal proceedings – is in the hands of a court, sometimes pre-advised by the supervisory judge. In France a creditor's representative is entitled to a fixed fee per case and a fixed right on the basis of a certain action (e.g. realisation of assets). In pre-insolvency proceedings, not surprisingly, fees are the result of the agreement concluded between the debtor and the practitioner.

137. The National Reports describe national remuneration systems in quite some detail. Nearly all national systems are characterised by meticulous regulation, in the primary law and in secondary law. No mention is made of the fact that certain remuneration schemes could be an obstacle in true cross-border cooperation, e.g. in the case that remuneration in country A is based on value of sales of assets, whilst it would objectively be more efficient to include these assets in a sale of all the assets, initiated out of country B. In nearly all remuneration systems fees and costs are borne by the debtor. As a consequence, problems arise in cases where an estate has hardly any assets or even is asset-less.

138. All of the above seem to confirm the outcomes of a geographically much more limited (nutshell) research in 2013 on the topic of the independence of a court appointed insolvency practitioner.[378] A comparison of selected topics in Belgium, Germany and England resulted in the rather incomparability of the rules and regulations of insolvency office holders (in formal proceedings), as well as the incommensurability of the IOH's positions. Both are strongly connected to the national system of insolvency (procedural) law. In Belgium, in principle, an exclusive monopoly for the attorney exists, with legal rules on selection and appointment, and (according to some) an implicit requirement of integrity. The Belgian Faillissementwet requires the IOH to take an oath and that at the beginning of his work, any kind of conflict of interest or appearance of bias is communicated to the presiding judge. In addition, the Belgian Act contains a fairly comprehensive system for conflict of interest. Germany, however, mentions impartiality ('Unabhängigkeit') explicitly in its Act, assumes the appointment of a 'business consultant ('Geschäftskundige', which does not have to be a lawyer), and provides a mechanism for judicial review of that independence if that person has been appointed by creditors or by the debtor. In Germany, the issue of selection and appointment is to a large extent left to the judiciary. How it is carried out, is seen in practice

[377] For England and Wales, see Stephan Leslie,' Changes made to insolvency legislation on 1 October 2015', Corporate Rescue and Insolvency October 2015, p. 210 et seq.
[378] Bob Wessels, *De onafhankelijkheid van de faillissementscurator*, (Preadvies Christen Juristen Vereniging (CJV), Zutphen: Uitgeverij Paris 2013), p. 47 et seq.

and legal literature as very unsatisfactory.[379] The same sentiment exists in the Netherlands. In England, there are some five procedures and there are seven organizations that are authorized to provide licenses to an IOH. These organisations all have their own system for (dis)qualification. The English administrator is an 'officer of the court', a figure that is unknown in many continental legal systems.

1.1.4.2. Significant international tendencies

139. Compared to some fifteen years ago, insolvency practitioners now have a key role in coordination insolvency proceedings with cross-border elements within the EU, to which since 2002 the European Insolvency Regulation (2000) applied[380] and as of 26 June 2017 the European Insolvency Regulation (2015).[381] The model on which the European Insolvency Regulation (2000) is based may result in one main insolvency proceeding with the insolvency practitioner dealing with assets located in any other Member State, or it may result in a split of insolvency proceedings opened against the debtor, who has assets or operations in two or more jurisdictions of the EU. In these situations, Article 31 EIR (2000) obliges the insolvency practitioners involved in these proceedings to coordinate these proceedings to '… contribute to the effective realisation of the total assets'. They '… must cooperate closely, in particular by exchanging a sufficient amount of information …'.[382] Their roles require certain specific qualities and skills.

140. As of 26 June 2017 the role of an insolvency practitioner (and of a court) in cross-border insolvency cases will be notably increased.[383] The Recast of the EU Insolvency provides in Articles 41 – 44 for cooperation and communication where there are multiple insolvency proceedings relating to a single debtor. The existing mutual duty to cooperate has been extended in several ways. Whereas in Article 31 EIR (2000) these duties are limited to insolvency practitioners (in the EIR (2000) defined as 'liquidators'), Articles 41 – 44 EIR (2015) will impose duties of cooperation and communication as between courts (Article 42), and between insolvency practitioners and courts (Article 43 EIR (2015)), as well as between insolvency practitioners (Article 41 EIR (2015), the successor to Article 31 EIR (2000)). These provisions not only extend the number of parties subject to the Regulation's duties of cooperation and communication, but also provide more detail as to the content of these duties, and (in the case of Article 43) provide a rule to regulate the costs of such cooperation

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[379] Compare Frank Frind, 'Die Unabhängigkeit des (vorläufigen) Insolverwalters/Sachwalters nach Inkrafttreten des '"ESUG"', in Hugo Grote, Manfred Obermüller, Gerhard Pape (eds.), *Insolvenz und Sanierung – auf der Dauerstelle geht es weiter, Festschrift für Hans Haarmeyer zum 65. Geburtstag,* (Carl Heymans Verlag 2013), p. 39-63.

[380] Council Regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings, [2000] *OJ* L 160/1, which entered into force 31 May 2002. The Insolvency Regulation does not apply to Denmark.

[381] Regulation (EU) 2015/848 of the European Parliament and the Council of 20 May 2015 on insolvency proceedings (recast), [2015] *OJ* L 141/19, it does not apply to Denmark.

[382] Recital 20. Regarding Article 31 EIR (2000), or see Pannen/Riedemann, in Klaus Pannen(ed.), *European Insolvency Regulation* (Berlin: Walter de Gruyter 2007), Article 31; Bob Wessels, *International Insolvency Law* (3rd ed., Deventer: Kluwer 2012), para. 10845 et seq.; Christoph Paulus, *Europäische Insolvenzverordnung. Kommentar* (4th ed., Verlag Recht und Wirtschaft, Frankfurt am Main 2013), Article 31; Christian Wenner / Michael Schuster, 'EuInsVO', in Klaus Wimmer (Hrsg.), *FK-InsO. Frankfurter Kommentar zur Insolvenzordnung* (8th ed., C.H. Beck Verlag: München 2015), Article 31 EuInsVO.

[383] See EIR (2015).

and communication (Article 44).[384] Parallel provisions to Articles 41 – 44 EIR (2015) can be found in Chapter V of the Regulation, which governs cooperation, communication and coordination in corporate group insolvencies. In cross-border insolvency instances quality, professionalism and integrity will be of uppermost importance.[385]

141. For the topics addressed, we limit ourselves to four sets of (non-binding) international norms which are relevant, namely those of the World Bank, the United Nations Commission on International Trade Law (UNCITRAL) and those of the European Bank for Reconstruction and Development (EBRD).[386] The last source to use has its limits to a large part of Northern Europe, the Nordic-Baltic Recommendations on Insolvency Law (December 2015).

142. In the 2016 Principles for Effective Insolvency and Creditor/Debtor Regimes[387] the World Bank is firm in its opinion that in an insolvency liquidation proceeding the existing management should be replaced by an insolvency practitioner. Principle C6.1 provides:

> ‘In liquidation proceedings, management should be replaced by an insolvency representative with authority to administer the estate in the interest of creditors. Control of the estate should be surrendered immediately to the insolvency representative. In creditor-initiated filings, where circumstances warrant, an interim administrator with limited functions should be appointed to monitor the business to ensure that creditor interests are protected.’

143. This approach is more nuanced in reorganisation proceedings. In Principle C6.2 it is stated:

> ‘There are typically three preferred approaches in reorganization proceedings:
> - exclusive control of the proceeding is entrusted to an independent insolvency representative; or
> - governance responsibilities remain invested in management; or
> - supervision of management is undertaken by an impartial and independent insolvency representative or supervisor.
>
> Under the second and third approaches, complete administrative power should be shifted to the insolvency representative if management proves incompetent or negligent or has engaged in fraud or other misbehaviour.’

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[384] For its increase with the effect that duties to cooperate and communicate cross-border to courts too, see para. For a discussion see Bob Wessels, ‘Commentary on Articles 41-44 EU Insolvency Regulation (Recast)’, in Reinhard Bork and Kristin van Zwieten (eds.), *Commentary on The European Insolvency Regulation*, (Oxford University Press 2016), p. 457-506.

[385] See for instance Bob Wessels, ‘De onafhankelijkheid van de faillissementscurator’, (Preadvies Christen Juristen Vereniging (CJV), Zutphen: Uitgeverij Paris 2013), 84, submitting: ‘The core question of every insolvency judge will be: how will I know when someone approaches my court and says she/he is the insolvency practitioner appointed in a proceeding in Cyprus, in France or in Finland, the she/he is sufficiently honorable and incorruptible? More substantial is to down-to-earth question: how will I know as a Dutch judge that I communicate with, cooperate with or sometimes provide information to someone whose profession and work is assessed continuously on professionality and integrity?’

[386] For seven other sets of recommendations, see Ian F. Fletcher en Bob Wessels, *Harmonisation of Insolvency Law in Europe, Preadvies uitgebracht voor de Vereniging voor Burgerlijk Recht* (Deventer: Kluwer 2012), p. 32 et seq.

[387] See Bob Wessels and Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming)

144. The emphasis on the role and powers of an 'insolvency representative', leads, we believe, to a rather weak recommendation in Principle D8 ('Competence and Integrity of Insolvency Representative'), providing:

> 'The system should ensure that:
> - Criteria as to who may be an insolvency representative should be objective, clearly established and publicly available;
> - Insolvency representatives be competent to undertake the work to which they are appointed and to exercise the powers given to them;
> - Insolvency representatives act with integrity, impartiality and independence; and
> - Insolvency representatives, where acting as managers, be held to director and officer standards of accountability, and be subject to removal for incompetence, negligence, fraud or other wrongful conduct.'[388]

145. The United Nations Commission on International Trade Law (UNCITRAL) has published, in 2004, its Legislative Guide on Insolvency Law: '… a comprehensive statement of key objectives and core features for a strong insolvency, debtor-creditor regime, including considerations of out-of-court restructuring, and a legislative guide containing flexible approaches to the implementation of such objectives and features, including a discussion of the alternative approaches possible and the perceived benefits and detriments of such approaches'.[389] The goal of the Legislative Guide is: '… to assist the establishment of an efficient and effective legal framework to address the financial difficulty of debtors. (…) The advice provided in the Guide aims at achieving a balance between the need to address the debtor's financial difficulty as quickly and efficiently as possible and the interests of the various parties directly concerned with that financial difficulty, principally creditors and other parties with a stake in the debtor's business, as well as with public policy concerns.' UNCITRAL stresses the key role of an 'insolvency representative': 'The insolvency representative plays a central role in the effective and efficient implementation of an insolvency law, with certain powers over debtors and their assets and a duty to protect those assets and their value, as well as the interests of creditors and employees, and to ensure that the law is applied effectively and impartially. Accordingly, it is essential that the insolvency representative be appropriately qualified and possess the knowledge, experience and personal qualities that will ensure not only the effective and efficient conduct of the proceedings but also that there is confidence in the insolvency regime.' Contrary to the statement of the World Bank, the Legislative Guide contains over twenty pages with ten recommendations on the role of the insolvency representative.[390] Recommendations are related to:

- Qualifications (115);
- Conflict of interest (116 and 117);
- Appointment (118);
- Remuneration (119);
- Duties and functions of the insolvency representative (120);

[388] Footnote omitted.

[389] The United Nations General Assembly has stated '… that all States give due consideration to the Legislative Guide when assessing the economic efficiency of their insolvency regimes and when revising or adopting legislation relevant to insolvency', Resolution 59/40 of 2 December 2004.

[390] UNCITRAL Legislative Guide (2004), p.174 et seq, including recommendations 115-125. See Bob Wessels and Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming).

- Right to be heard (see 137);
- Confidentiality (see 111);
- Liability (121);
- Removal and replacement (122 – 124); and
- Estates with insufficient assets to meet the costs of administration (125).

146. The goal of EBRD's set of Insolvency Office Holder Principles, published in 2007, is: '… to add detail to the World Bank and UNCITRAL guidance. They are designed to help law reformers identify issues to be resolved and to ensure that critical elements are not overlooked. They are intended to advance the integrity, fairness and efficiency of the insolvency law system by ensuring that only appropriately qualified professionals hold office in insolvency cases'.[391] The following principles are mentioned:

Principle 1: qualification and licensing
Principle 2: appointment in an insolvency case
Principle 3: review of an office holder appointment
Principle 4: removal, resignation and death of an office holder
Principle 5: replacement of an office holder
Principle 6: standards of professional and commercial conduct
Principle 7: reporting and supervision
Principle 8: regulatory and disciplinary functions
Principle 9: remunerations and expenses
Principle 10: release of office holder
Principle 11: insurance and bonding
Principle 12: code of ethics.[392]

147. The Nordic-Baltic Insolvency Network Recommendations formulate a similar requirement for a person handling liquidation ('trustee') or a reorganisation ('administrator') for '… insight, experience and suitability for handling the proceedings in question'[393], as well as '… for independence and impartiality in relation to both the debtor and the creditors', whereas the persons mention '… should be obligated to declare if there exists any threats to

[391] See Jay Allen and Neil Cooper, 'EBRD insolvency office holder principles' EBRD Law in transition online, October 2007, p. 12 et seq.

[392] EBRD has cooperated with Serbia and, together with the Bankruptcy Supervisory Agency of Serbia (BSA), it has developed standards on all aspects of the deontology of the insolvency practitioners. In 2010 with force of law a Manual on the National Standards and Code of Ethics for Bankruptcy Administrators has been introduced in Serbia. It also contains eight Technical Guidance Notes on National Standards, a Technical Guidance Note on Code of Ethics, and a Code of Ethics for Bankruptcy. The National Standards are related to: (1) Bank accounts and monetary assets of the bankrupt debtor and accounting for the bankrupt debtor's estate, (2) Inventory and evaluation of assets of the bankrupt debtor and the Initial bankruptcy balance sheet, (3) Compiling the report of the bankruptcy administrator on economic and financial position of the bankrupt debtor, (4) Supervision Agency, (5) Manner and procedure of realising assets of the bankrupt debtor, (6) Information to be contained in the reorganization plan, (7) Final account of the bankruptcy administrator, and (8) Manner of keeping and preserving records of the bankrupt debtor and the bankruptcy administrator. See http://www.ebrd.com/pages/sector/legal/insolvency.shtml. Evidently, the reporters are aware of the difference there may exist between 'law in the books' and 'law in action', but the approach deserves certainly attention.

[393] It adds in Recommendation XI:4 '… that in most jurisdictions this would normally be a lawyer, but the network does not consider whether requirements for certain formal qualifications, a specific title, certification or license should be made in addition to the general suitability requirement.'

independence or any conflict of interest.'[394] Compared to the other three soft law sources, the Nordic-Baltic Recommendations are limited to two topics: (i) the appointment and dismissal of the trustee and the administrator[395] and (ii) the trustee and administrator's liability for damages.[396]

148. Although differences exist in impetus, structure and detail, the four sets of non-binding guidance of the World Bank, UNCITRAL, EBRD and the Nordic-Baltic Insolvency Network demonstrate that in the first fifteen years in this century insolvency law has evolved to a key part of (international) commercial law, and that a solid system of insolvency law contributes to clear relationships between the debtor and its creditors as well as the powers of insolvency practitioners and courts. All four have as their central mission to assist legislators, policy makers, associations of practitioners with efficient and effective insolvency legislation.

1.1.4.3. INSOL Europe Statement of Principles and Best Practice for Insolvency Office Holders in the EU

149. The lack of further legislative action and the revisions to be expected to be made to the European Insolvency Regulation (2000) has led to an initiative taken in 2012 by the largest insolvency practitioners association in Europe, INSOL Europe. In December 2012, the European Commission (EC) submitted a report on the application of the EIR (2000) to the European Parliament (EP), the Council and the Economic and Social Committee.[397] In accordance with article 46 EIR (2000), this report was accompanied by a proposal to adapt

[394] See Recommendation XI:5. The question whether the administrator could be appointed trustee in a subsequent liquidation is answered negatively in Recommendation XI:6: '…the clear main rule should be that a person other than the former administrator is to be appointed. Exceptions should only be made in special circumstances when, for example, the reorganisation has been underway for just a few days and nothing of significance has occurred.'

[395] 'XI:7. Both the trustee or the administrator should be appointed by the court.

XI:8. There should not be a requirement, but an option, in the application to put forward a proposal for a specific person to be appointed liquidations trustee. The trustee should in principle always be appointed irrespective of any proposals. If it is evident from the application that a person who has been proposed fulfils the suitability requirement, and there is no noteworthy objection to this, the court should be able to approve the proposal without further consideration.

An administrator in reorganisation should be appointed after a proposal by the applicant. However, as in liquidations, the court should not be bound by the proposal, but should be able to approve it under the same guidelines as for liquidations.

XI:9. The trustee and the administrator could be dismissed by the court at the request of a creditor, a creditors' meeting, a creditors' committee, the debtor, the trustee or administrator him or herself or ex officio. In cases where the proceedings are subject to public supervision; such a request could also be made by the supervisory authority. The reason for the dismissal should be that the requirements under sections XI:4 and 5 are not met or that the trustee or administrator for some other reason should be dismissed from the assignment.'

[396] 12. A trustee and an administrator should have a duty to compensate for damage that he or she intentionally or negligently caused with regard to either the estate, a creditor or the debtor whilst performing his or her duties.

According to the first paragraph there should also be liability against third parties provided the trustee or the administrator has disregarded a written or unwritten insol-vency law rule laid down for the protection of third parties.'

[397] European Commission, Report from the Commission to the European Parliament, the Council and the European Economic and Social Committee on the application of the Council Regulation (EC) No. 1346/2000 of 29 May 2000 on insolvency proceedings, COM(2012) 743 final.

the European Insolvency Regulation (2000). The focus of the EC Proposal[398] is on (a) enhanced restructuring possibilities, and (b) intensification of communication and cooperation between liquidators, between courts, and between each other. The proposal – after discussion and amendment – led to the EIR (2015) to be effective as of 26 July 2017.

150. On the intensification of communication and cooperation, the last line of Recital 20 of the Proposed EIR (2015) reads: '… In their cooperation, liquidators and courts should take into account best practices for cooperation in cross-border insolvency cases as set out in principles and guidelines on communication and cooperation adopted by European and international associations active in the area of insolvency law.' In the adopted EIR (2015), now in Recital 48, the wording has slightly changed and, at the end a reference is made to UNCITRAL: '… When cooperating, insolvency practitioners and courts should take into account best practices for cooperation in cross-border insolvency cases, as set out in principles and guidelines on communication and cooperation adopted by European and international organisations active in the area of insolvency law, and in particular the relevant guidelines prepared by the United Nations Commission on International Trade Law (UNCITRAL).'

151. The cited Recital opens the door to already existing 'best practices', such as the European Communication and Cooperation Guidelines for Cross-border Insolvency (also termed: 'CoCo Guidelines (2007)'), which were endorsed by INSOL Europe during its Annual Congress in October 2007 in Budapest, Romania. The CoCo Guidelines (2007) initiative was jointly chaired by professors Miguel Virgós (University Autonomá, Madrid, Spain) and Bob Wessels (now emeritus of Leiden University, the Netherlands). These Guidelines have received attention both in legal literature as well as from judges and practitioners, and were for instance taken into account in the June 2009 Global Cross-Border Insolvency Protocol for the Lehman Brothers Group of Companies and in the agreements used in the Nortel Network case, which led to the decision of the Court of Justice of the EU of EU of June 2015.[399]

[398] European Commission, Proposal for a regulation of the European Parliament and of the Council amending Council Regulation (EC) No 1346/2000 on insolvency proceedings, COM(2012) 744 final, available at http://ec.europa.eu/justice/civil/commercial/insolvency/index_en.htm.

[399] CJEU 11 June 2015, Case C-649/13 (*Comité d'entreprise de Nortel Networks SA and Others v Cosme Rogeau and Cosme Rogeau v Alan Robert Bloom and Others*). See Bob Wessels and Miguel Virgós, *European Communication and Cooperation Guidelines for Cross-Border Insolvency* (INSOL Europe 2007). See www.insol-europe.org, or www.bobwessels.nl, weblog, document 2007-09-doc1. These Guidelines are explained in e.g. Bob Wessels and Miguel Virgós, 'Accommodating Cross-border Coordination: European Communication and Cooperation Guidelines for Cross-Border Insolvency', International Corporate Rescue, Vol. 4, Issue 5, 2007, 250 et seq. The European Communication & Cooperation Guidelines for Cross-border Insolvency of 2007 aim to provide rules to be applied by insolvency administrators within their duties to communicate and cooperate in cross-border insolvency instances to which the EU Insolvency Regulation is applicable. Their reception has been welcomed by scholars (e.g. Mario Hortig, *Kooperation von Insolvenzverwaltern,* (Schriften zum Insolvenzrecht Diss. Köln, Band 25, Baden-Baden: Nomos 2008): '… it is to be expected that the Guidelines will develop to the European standard of cooperation', at 258), and insolvency practitioners (Stephen J. Taylor, 'The Use of Protocols in Cross Border Insolvency Cases', in Klaus Pannen (ed.), *European Insolvency Regulation* (Berlin: De Gruyter Recht 2007), 678 et seq ('highly laudable initiative', at 681); Lars Westpfahl, Uwe Goetker, Jochen Wilkens, *Grenzüberschreitende Insolvenzen* (Köln: RWS Verlag, 2008) ('extremely helpful', p. 125); Louise Verrill, 'The INSOL Europe Guidelines for Cross Border Communication', in Bob Wessels and Paul Omar (eds.), *Crossing (Dutch) Borders in Insolvency* (Nottingham, Paris: INSOL Europe 2009), 39 et seq ('[it is] important for the professions to be aware of and understand the need to adopt the CoCo Guidelines', at 45). See also

152. In 2013 and 2014, at the request of INSOL Europe, researchers of Leiden Law School have designed a set of Principles and Best Practices for Insolvency Office Holders in Europe. The founding idea is that by designing this set of Principles and Best Practices the general quality of IOHs in Europe would improve and the mutual trust between IOHs as well as the trust in the IOHs' work by courts as well as the general public would be enhanced. In addition, IOHs would be able to work more efficient, which once again would enhance the trust in the IOH profession on the market.[400] The study led to a set of non-binding statement of professional and ethical guidelines for insolvency office holders, presented during the Annual Congress on Insol Europe in Istanbul, mid October 2014, including seven Principles and over thirty Best practices. These principles concern:

Principle 1. Insolvency Office Holder
Principle 2. Professional Standards
Principle 3. Ethical Standards
Principle 4. Administration of the Estate
Principle 5. Communication
Principle 6. Coordination and cooperation
Principle 7. Insolvency governance[401]

153. A Leiden Law School master thesis of 2014 by Fidder, comparing Belgium, Germany and England) as well as relevant international sources drafted by organizations such as UNCITRAL, the World Bank and EBRD, suggests that harmonization of a rule on conflict of

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Andreas Geroldinger, *Verfahrenskoordination im Europäischen Insolvenzrecht. Die Abstimmung von haupt- und Sekundärinsolvenzverfahren nach der EuInsVO* (Veröffentlichungen des Ludwig-Boltzmann-Institutes für Rechtsvorsorge und Urkundenwesen, Manzsche Verlags- und Universitätsbuchhandlung, Wien 2010), p. 31, qualifying the CoCo Guidelines as a first and by all means very promising attempt (*Ein erster durchaus vielversprechender Versuch*). See also Paul H. Zumbro, 'Cross-border Insolvencies and International Protocols – an Imperfect but Effective Tool', 11 Business Law International no. 2, May 2010, 157 et seq, at 167 ('The CoCo Guidelines reflect best practices both inside and outside Europe'); Patrick E. Mears and Timothy S. McFadden, 'Court-to-Court Communications, Reform of European Regulation', ABI Journal, October 2012, at 33 et seq. For an in depth analysis of the CoCo Guidelines (2007), see Olaf Benning, *International Prinzipien für grenzüberschreitende Insolvenzverfahren* (Schriften zum Verfassungsrecht, Band 45, Frankfurt: Peter Lang 2013), stressing another aspect, in that the CoCo Guidelines (2007) also can be used to trace European or even global principles for cross-border insolvency proceedings ('… um Europaweit oder sogar weltweit geltenden Principien für grenzüberschreitende Insolvenzverfahren zu ermittlen'), at 83. For the Nortel Network case, see Bob Wessels, *International Insolvency Law Part II. European Insolvency Law (Wessels Insolvency Law Volume X)* (4th ed., Deventer: Kluwer 2017), para. 10640 et seq. (forthcoming).

[400] The Leiden Law School research has as its members for this IOH-project prof. Jan Adriaanse (professor of Turnaround Management), prof. Iris Wuisman (professor of Company Law), and Dr Bernard Santen, Senior Researcher, all at Leiden Law School (www.tri-leiden.eu). Wessels acted as a consultant to this IOH-project.

[401] The Leiden Law School developed a framework for the uniform analysis of the existing rules for IOHs. It deducted four main categories of subjects: (1) IOH selection and appointment (regarding the question how to become an IOH), (2) Professional standards (covers professional and ethical standards for an IOH, (3) Roles and responsibilities (relates to what an IOH should do once appointed in an individual case), and (4) Insolvency governance (the various monitoring functions on the IOH's work. During the whole process assessments and discussions have taken place with a group of around 20 consultants, from at least 10 EU Member States, covering academic scholars, judges and insolvency practitioners. Further explained in Bob Wessels, 'Harmonisation of Requirements for Insolvency Holders on a European Level', in *Festschrift für Bruno M. Kübler zum 70. Geburtstag* (München: Verlag C.H. Beck oHG 2015), p. 757 et seq.

interest at the level of the European Union is desirable and provides seven recommendations to the European Union legislator on the substance of such a rule.[402]

1.1.4.4. Impetus for recommendations

154. The reporters adhere to the views that have been developed for over thirty years: 'The success of any insolvency system … is very largely dependent upon those who administer it. If they do not have the confidence and respect, not only of the courts and of the creditors and debtors, but also of the general public, then complaints will multiply and, if remedial action is not taken, the system will fall into disrepute and disuse'.[403] Fletcher and Wessels, fully accepting this view, have in addition stressed '… that it is not only the creditors' confidence, but the trust the market puts in the insolvency office holders' actions, which may translate in her/his ability to exercise a transparent process, e.g. for unsecured creditors to be informed in a clear way about any process and to be able to influence any administration, to understand the way the profession is regulated, which would include a mechanism to maintain trust in any regulatory regime, such as a post-action review or a complaints procedure'.[404]

155. The organisation of the profession on insolvency practitioner is organised in a variety of ways in all EU Member States. On all aspects of the insolvency practitioners' professions' deontology there are some similarities, but many times there are differences and diversities in a large proportion of its details. These aspects concern what EBRD in its 2014 report has called '… seven core elements (benchmarks) for the development and performance of the IOH profession', these being (i) licensing and registration, (ii) regulation, supervision and discipline, (iii) qualification and training, (iv) appointment system, (v) work standards and ethics, (vi) legal powers and duties, and (vii) remuneration.[405] We provide a few examples of this research.

156. In 2006, a review of 12 EU jurisdictions was conducted, with the result that in all jurisdictions reviewed for the selection of insolvency administrators it is necessary to possess the appropriate training and that '… it is either expressly or implicitly stated that persons

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[402] Wessels supervised Mr Fidder's thesis together with Hannover attorney Volker Römermann, also a professor at Humboldt University Berlin. See for the thesis and the recommendation: www.bobwessels.nl, weblog, at 2014-09-doc1.

[403] Cork Report, Insolvency Law and Practice – Report of the Review Committee (Chairman, Sir Kenneth Cork) (June 1982, Cmnd. 8558), London, HMSO ISBN 0 10 185580, at para. 732. The Cork Report has served as the basis for the reform of insolvency law in the UK, centred on the Insolvency Act 1986.

[404] Ian F. Fletcher and Bob Wessels, *Harmonization of Insolvency Law in Europe, Preadvies uitgebracht voor de Vereniging voor Burgerlijk Recht* (Deventer: Kluwer 2012), p. 82. See also Christoph G. Paulus, Stathis Potamitis, Alexander Rokas and Ignacio Tirado, 'Insolvency Law as a Main Pillar of Market Economy – A Critical Assessment of the Greek Insolvency Law', 24 International Insolvency Review 2015, p. 1 et seq., stressing the need of education and qualification for courts and insolvency practitioners, also to '… foster and nurture a rescue culture, as it is indispensable in order for the beneficial effects of a modern insolvency law with its emphasis on restructuring of companies to be fully realized.'

[405] EBRD, 'Assessment of the insolvency office holder, Review of the profession in the EBRD region' 2014, available at http://assessment.ebrd.com/insolvency-office-holders/2014/report.html. See para. 5. On these varieties generally: Jay Lawrence Westbrook et al., *A Global View of Business Insolvency Systems* (The World Bank, Washington DC 2010), p. 208 et seq.

who may be selected must, at least, possess the necessary mental and physical health and be able to prove that they have no relevant criminal record.'[406]

157. In 2009 a comparison was made between the German system of supervision with the English system.[407] For Germany the author distinguishes preventive and repressive ('information-repressive') supervision, performed either by the State ('staatlich') or privately ('privat'). For the UK he explains that 'the State' can be a Court or the Secretary of State and 'privately' contains creditors and the recognised professional bodies (RPBs).[408] Such (governmental) agencies are also operational in the Czech Republic, Latvia and Sweden, but non-existent in e.g. Belgium, France, Germany, Poland, Spain and the Netherlands.

158. In 2010, the International Association of Insolvency Regulators (IAIR)[409] has conducted a comparative study into a similar list of topics as mentioned under para. 85. From its study, which was limited to commercial insolvency, the main results of the nineteen organisations that participated are three of a kind: (i) in all jurisdictions represented insolvency professionals play a role in administering insolvency proceedings, (ii) in the majority of jurisdictions insolvency professionals are private sector professionals (17), (iii) in 55% of the jurisdictions insolvency professionals are licensed, most often licences are renewable and there is a register of insolvency professionals, whilst (non licensed) registration in a register of insolvency professionals is available in 'some' jurisdictions.

159. In the EU, the prevailing view is that the most important general exclusion criterion is that the insolvency practitioner is exposed to any conflict of interest, e.g. an accountant

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[406] Christian Köhler-Ma, 'Insolvency Administrator Selection and Quality Criteria in International Comparison', 2006, (on file with authors). See also Christian Köhler-Ma, 'Verwalterauswahl und Qualitätskriterien im internationalen Vergleich', Deutsche Zeitschrift für Wirtschafts- und Insolvenzrecht (DZWiR), 2006, 228 et seq.

[407] Johannes Henke, *Effektivität der Kontrollmechnismen gegenüber dem Unternehmensinsolvenzverwalter. Eine Untersuchung des deutschen und englishen rechts* (Studien zum ausländischen und internationalen Privatrecht, nr. 229, Mohr Siebeck 2009).

[408] The recognised professional bodies that regulate the practice of insolvency in Great Britain are: The Association of Chartered Certified Accountants; The Insolvency Service; Insolvency Practitioners Association; The Institute of Chartered Accountants in England and Wales; Chartered Accountants, Ireland; The Institute of Chartered Accountants of Scotland; The Law Society of Scotland; Solicitors Regulation Authority. See Insolvency Act 1986, s.391, together with S.I.1986/1764: the Insolvency Practitioners (Recognised Professional Bodies) Order 1986. These seven RPBs regulate around 1300 insolvency practitioners. Since 26 May 2015, the Small Business Enterprise and Employment Act 2015 has come into legal effect in the United Kingdom. The Act is designed to make the UK a more attractive place to start, finance and grow a business and reduce the barriers that many small businesses face in their drive to innovate, grow and compete. Regarding matters of insolvency the Act introduces, in Part 10 of the Act, the power the Secretary of State to issue directions to Recognised Professional Bodies (RPBs), commence an investigation into individual Insolvency Practitioners (IPs) and control individual enquiries. The Act also allows the Secretary of State to establish a single regulator of insolvency practitioners, if the reforms in the Act to strengthen the regulatory regime do not build confidence. For its text, see http://www.legislation.gov.uk/ukpga/2015/26/contents/enacted.

[409] The International Association of Insolvency Regulators (IAIR) is an international body with around 25 members, being government departments, agencies or public authorities (further: 'agencies') which have responsibility in their country for insolvency regulation, practice, policy and/or legislation. Among its members are agencies of Australia, Canada, China, India, Mexico, Russian Federation and the USA. EU Member States represented are Czech Republic, Finland, Ireland, Romania, UK: England & Wales (The Insolvency Service), UK Northern Ireland (The Insolvency Service) and UK Scotland - Accountant in Bankruptcy.

previously involved in preparing a financial statement or a previous attorney-client relationship that gives rise to similar objections.[410]

160. The 2014 study of EBRD was preceded by a report of 2007.[411] Aware of the relatively young and rather untested legal regimes related to insolvency in these countries in transition, the drafters' main conclusions are: (i) that in all the topics mentioned a variety of approaches have been chosen in a country's laws and regulations, (ii) that there is a clear need for appropriate detailed standards to guide office holders in their work and to improve the basis on which their work can be measured and assessed, and that (iii) in general there is an inadequate disciplinary system for insolvency office holders (either related to the vague ground for disciplinary action or the limited type of available sanctions). In the first phase leading to the EBRD 2014 assessment study in the countries of operation involved, EBRD found that the main distinction that has emerged is between countries that take an active approach to the development and regulation of the profession (examples of EU Member States being Romania and to a lesser extend Latvia) and those that adopt a more passive approach (the report mentions Poland). Another conclusion is that whilst some countries follow similar practices, there are substantial differences of approach towards the IOH profession within the jurisdictions surveyed. EBRD submits that this may lead to differences amongst IOHs themselves and the state of comparative development of the profession in a particular jurisdiction. On the topic of licensing or registration of IOHs, EBRD notes that this area has proved to be closely '… interlinked with regulation, supervision and discipline, since these functions are often, although not exclusively, performed by the same regulating entity, which is often responsible for the separate area of higher qualification and training.'[412]

161. The EBRD's assessment study of the IOH profession with the aim of evaluating both the profession's relative development and the legal and regulatory framework applicable to IOHs has led to a valuable source of information on insolvency office holders and may serve as a reference point for policy makers and stakeholders with an interest in further development of the profession.[413]

162. The European Parliament in November 2011, in its call for harmonisation of certain aspects of insolvency law also addresses general aspects of the requirements for the qualification and work of 'liquidators'. The EP sets forth, without suggesting a certain harmonisation instrument, the following (numbers have been added by the reporters):

1. the liquidator must be approved by a competent authority of a Member State or appointed by a court of competent jurisdiction of a Member State, must be of

[410] See Reinhard Bork, 'Die Unabhängigkeit des Insolvenzverwalters – ein hohes Gut', Zeitschrift für Wirtschaftrecht (ZIP), 2006, p. 58 et seq.; Björn Laukemann, *Die Unabhängigkeit des Insolvenzverwalters. Eine rechtsvergleichende Untersuchung* (Heidelberger Rechtswissenschaftliche Abhandlungen, Tübingen: Mohr Siebeck 2010).

[411] Jay Allen, Neil Cooper, Ron Harmer, 'A Regional Report on Insolvency Office Holders in South-East Europe', June 2007, available via www.ebrd.com. These eight countries are Albania, Bosnia and Herzegovina, Bulgaria, FYR Macedonia, Montenegro, Romania, Serbia, and Slovenia.

[412] We just mention a few items from this interesting report, see EBRD, 'EBRD Insolvency Office Holder (IOH) Performance, 2013 Pilot Assessment Report', 2013, available via www.ebrd.com.

[413] Reference is made to Bob Wessels and Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming).

good repute and must have the educational background needed for the performance of his/her duties;

2. the liquidator must be competent and qualified to assess the situation of the debtor's entity and to take over management duties for the company;
3. when main insolvency proceedings are opened, the liquidator should be empowered for a period of six months to decide on the protection of assets with retroactive effect in cases where companies have moved capital;
4. the liquidator must be empowered to use appropriate priority procedures to recover monies owing to companies, in advance of settlement with creditors and as an alternative to transfers of claims;
5. the liquidator must be independent of the creditors and other stakeholders in the insolvency proceedings;
6. in the event of a conflict of interest, the liquidator must resign from his/her office.[414]

163. Klaus Lehne, the reporter for the EP, stated that for insolvency practitioners: '… he would … like to propose some common requirements. Some harmonisation in this area would support the idea of closer cooperation between the liquidators and enhance the comparability in the profession.' The EP recommends harmonisation of certain elements of the profession of an insolvency office holder, and topics 1, 2, 5 and 6 (mentioned above) typically constitute elements for the deontology of nearly any profession in the commercial area.[415] It should be noted, however, that INSOL Europe (having been invited by the EP to provide background for the matters that could be a subject for harmonisation) in its study concluded that '… there is no merit in seeking to harmonise these issues until a further harmonisation of substantive insolvency law and company law has been achieved'.[416]

164. Following our earlier observations, the reporters regard it as an essential element in and insolvency framework that there should be no doubt whatsoever about an insolvency practitioner's inherent professional and personal qualities, both in an international as well as in a national context.[417] With the automatic recognition of an opening judgment, the powers of any appointed IP can be exercised – within the rules set by Article 21 EIR (2015) – in 26 other Member States. The specific way of coordinating cross-border insolvency proceedings, including communication with (foreign) courts requires certain specific qualities and skills.

[414] European Parliament resolution of 15 November 2011 with recommendations to the Commission on insolvency proceedings in the context of EU company law (2011/2006(INI)), at 1.4.

[415] Topics 3 and 4 relate to certain powers which, when executed, will have an immediate effect on third parties. From the Lehne reports follows that he thought it was too early to harmonise such powers.

[416] INSOL Europe's Note displays some eight EU Member State reports, from which it follows that the laws of EU Member States have different rules on the qualifications and eligibility for the appointment, licensing, regulation, remuneration, supervision and professional ethics and conduct of liquidators. Where the drafters of the Note have not experienced that the use of different systems in the EU Member States have caused any difficulties in practice, they came to the conclusion quoted. The Note is published as: European Parliament, 'Harmonisation of insolvency law at EU level, note', European Parliament 2010, PE419.633, at 23.

[417] Uncertainty regarding how to ascertain whether a person from abroad is indeed a qualified and professionally regulated IOH was expressed as one of the four concerns, flowing of a self-assessment of 66 judges from 22 EU Member States, see Gert-Jan Boon et al., 'Grensoverschrijdende rechterlijke samenwerking in insolventies', Nederlands Juristenblad 2016/199.

165. Insolvency law can only function with the assistance of experienced and knowledgeable actors, such as the insolvency office holder. Where he or she has a crucial role in the efficient administration of insolvency proceedings to which the European Insolvency Regulation (2015) is applicable, it is evident that IPs should have the appropriate know how to play that role.[418] From the sources mentioned above, it follows that a variety of solutions is found on basic matters such as appointment, supervision, education or remuneration. Of utmost importance is that IOHs work on the basis of trust, which is not so much the believe that a professional may have in its own ethical behaviour, integrity and know how, but how third parties in the market see IOHs, or better: the perception of these third parties in the market.[419]

1.1.4.5. Recommendations

Recommendation 1.11: Member States should lay down explicitly in their laws that the professional performing restructuring and insolvency tasks is impartial, independent and competent. Being regulated as a lawyer or an accountant does in itself not sufficiently guarantee the standards of performance necessary for the proper exercise of the restructuring and insolvency tasks.

Recommendation 1.12: The European and national legislators should set professional and ethical standards for insolvency practitioners and ensure that the relevant professional bodies are consulted and involved in the creation of such standards and that they take into account best practices for appropriately regulated professional parties as set out in principles and guidelines on regulation of the restructuring and insolvency profession developed or adopted by European and international non-governmental organisations active in the area of restructuring and insolvency. Such standards should at least contain rules on licensing and registration, supervision and discipline, qualification and training, an appointment system, work standards during administration, legal powers and duties, remuneration, reporting and communication and ethical working standards (including rules on conflict of interests and a complaint procedure).

Recommendation 1.13: Member States should safeguard the independence and competence of insolvency practitioners by providing for a transparent and predictable process of appointment and resignation/removal as well as adequate means of supervision and an appropriate, timely remuneration in each individual case.

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418 Therefore CoCo-Guideline 4.2 reads: 'A liquidator is required to act with the appropriate knowledge of the EC Insolvency Regulation and its application in practice.'

419 We note, with appreciation, Recital 40 of the Proposal Restructuring Directive (2016): Member States should also ensure that the practitioners in the field of restructuring, insolvency and second chance which are appointed by judicial or administrative authorities are properly trained and supervised in the carrying out of their tasks, that they are appointed in a transparent manner with due regard to the need to ensure efficient procedures and that they perform their tasks with integrity. Practitioners should also adhere to voluntary codes of conduct aiming at ensuring an appropriate level of qualification and training, transparency of the duties of such practitioners and the rules for determining their remuneration, the taking up of professional indemnity insurance cover and the establishment of oversight and regulatory mechanisms which should include an appropriate and effective regime for sanctioning those who have failed in their duties. Such standards may be attained without the need in principle to create new professions or qualifications.' See Articles 25 – 27 of the Proposal Restructuring Directive (2016).

1.1.5. Debtor in possession

166. The phenomenon of the 'debtor in possession' is for over a century a fundamental feature of US bankruptcy law. The UNCITRAL Legislative Guide is helpful in providing a description for a debtor in possession, which is a debtor in reorganization proceedings which are so structured that the debtor him- or herself, or itself, (especially the board of a company) retains full control over the business, with the consequence that the court does not appoint an insolvency representative.[420] The concept therefore basically means that the debtor keeps control over the day-to-day operation of its business during restructuring or liquidation proceedings, taking on a role that in other countries would have been performed by a court (or creditors') appointed third party.

167. In Europe, the concept of the debtor in possession is not as common as it is in the US.[421] The term was firstly defined in the EIR (2015). Furthermore, the European Commission referred to the concept of debtor in possession in its Recommendation of March 2014. According to the Commission, a debtor should stay in possession in case of a restructuring plan to avoid unnecessary cost and to reflect the early nature of the procedure. In most EU Member States a distinction is made though between reorganisation proceedings and liquidation proceedings. In those Member States, the debtor only remains in possession during reorganisation-oriented proceedings. Thus, in liquidation(-only) proceedings the debtor does not remain in charge. In Member States with an insolvency procedure that does not ex ante define the intended outcome (unified proceedings), like e.g. in Germany, leaving the debtor in possession is more or less a general procedural option. Some have a DIP option in all types of proceedings. In Greek bankruptcy proceedings, for instance, the court may permit the debtor to remain in control of its corporate affairs always along with the insolvency administrator's cooperation until when the liquidation of the property starts if a petition was filed by the debtor and if this is to the benefit of the creditor. In Greek recovery proceedings, the special agent may take over the management of the debtor's assets and affairs, and in special administrations no DIP option exists as the management is taken over by the special administrator.

The debtor in possession concept has several benefits. First of all, the existing knowledge, knowhow, expertise and network of business contacts of the debtor's directors concerning the debtor's business and financial affairs can continue without disturbances which may be detrimental for the business' prospects. The company's management will therefore continue to be available which will have its relationships and know-how that could benefit the debtor's restructuring efforts. In addition, the right to stay in control may also work as a powerful incentive for debtors to initiate formal restructuring proceedings voluntarily and, thus, timely. On the other hand, leaving a debtor or manager in control of a business that has failed under their management may hinder other stakeholders to trust the restructuring efforts of the debtor. Often, failure is caused by bad management decisions and stakeholder

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[420] UNCITRAL Legislative Guide (2004), para. 12, under B, 'Glossary, Terms and definitions'. UNCITRAL Practice Guide (2009), under B 'Glossary', in '2. Terms and explanations'.

[421] The ALI NAFTA Principles (2003), Annex A, Definitions, provide: 'Debtor in possession' refers to the person or persons entitled to operate the affairs of a debtor under either Chapter 11 reorganization in the United States or a concurso mercantil in Mexico, and includes a Mexican debtor in conciliation in Mexico.'

may wish to investigate a possible director's liability rather than see the management remain in control. A well-balanced debtor-in-possession (DIP) regime would have to address all these factors.

1.1.5.1. Significant elements from National Reports

168. The term debtor in possession was firstly defined in the EIR (2015) as '… a debtor in respect of which insolvency proceedings have been opened which do not necessarily involve the appointment of an insolvency practitioner or the complete transfer of the rights and duties to administer the debtor's assets to an insolvency practitioner and where, therefore, the debtor remains totally or at least partially in control of its assets and affairs'. Several EU Member States indeed have included the concept of a debtor in possession in their legislation. However, in most Member States a distinction is made between reorganisation proceedings and liquidation proceedings. This is for example the case in Belgium, the United Kingdom, Hungary, the Netherlands, and Sweden.

169. In Belgium, the debtor remains in possession during the formal judicial reorganisation proceedings. Belgian law provides for an optional appointment of an advisor (gerechtsmandataris/mandataire de justice) whose task it is to assist the debtor in possession during the proceedings. However, in a bankruptcy (liquidation) proceeding the debtor loses all his powers over his estate. These powers vest in one or more bankruptcy trustees appointed by the court. From that moment on the debtor itself is no longer entitled to dispose of his assets and to conclude agreements.[422] In the United Kingdom the debtor remains in possession during the out-of-court workout,[423] the scheme of arrangement procedure,[424] and the company voluntary agreements.[425] During the administration procedure the debtor does not remain in possession. An administrator will take over the management of the company's business and affairs.[426] In Hungary the debtor remains in possession during a reorganisation procedure. In a liquidation procedure, however, the debtor's external management is taken over by the insolvency practitioner.[427] In the Netherlands the debtor remains in possession during the suspension of payments procedure. However, the debtor in suspension may only perform acts of administration and disposition with respect to the estate, insofar he acts in cooperation with, or with permission or assistance of, the administrator.[428] In order to facilitate possibilities to effectively restructure those companies, the Dutch legislator has proposed an Act on the Continuity of

[422] Article 16 Bankruptcy Act.
[423] This workout is purely contractual in nature.
[424] A scheme of arrangement is a compromise between a company and its creditors or members or any class of them under Part 26 of the Companies Act 2006.
[425] A company voluntary arrangement is also a compromise between the company and its creditors for a composition in satisfaction of its debts or a scheme of arrangement of its affairs. An important difference with the scheme of arrangement is that under a company voluntary arrangement, the secured and preferential creditors cannot be bound by the scheme.
[426] Paragraph 59, Schedule B1 Insolvency Act 1986.
[427] Cstv. 34. Paragraph 1-2.
[428] Article 228 DBA.

Companies I on pre-pack proceedings[429] and an Act on the Continuity of Companies II on the scheme of arrangement outside bankruptcy proceedings.[430] In both the pre-pack procedure and the scheme of arrangement procedure the debtor will remain in possession. During a bankruptcy liquidation procedure, the directors lose the right to dispose of and to administer the assets of the company.[431] It is the Insolvency Practitioner who is charged with the administration and winding-up of the company's estate.[432] In Sweden, the debtor remains in possession during a company reorganisation procedure. During a bankruptcy procedure, the debtor does not remain in possession.

170. Some Member States allow for a debtor in possession in all types of proceedings. The German insolvency law only provides for a unified insolvency procedure and allows to avoid the appointment of an administrator in favour of a DIP under the supervision of a insolvency practitioner.[433] The debtor in possession may manage and dispose of his assets, having more or less the same powers as the insolvency practitioner in ordinary insolvency proceedings. Generally, in bankruptcy proceedings a liquidator is managing the debtor's assets after the commencement of the bankruptcy proceedings, unless the court permits the debtor to remain in possession and administration of its assets, but always along with the liquidator's co-operation.

Limitations to DIP powers

171. In case the law permits a debtor to remain in possession, there are some limitations to such a debtor's powers. In most Member States, the powers of the debtor in possession are 'limited' by the supervision of or cooperation with a court officer or insolvency practitioner.

In some Member States, those limitations consist in respect of certain transactions. This is for example the case in Austria during a reorganisation proceeding with self-administration. While the debtor in possession is entitled to carry out all legal acts in connection with the ordinary course of business, legal acts which fall outside this scope require prior approval of the reorganisation administrator. Furthermore, certain acts, such as (i) the voidance of legal acts and transactions which occurred prior to the opening of the proceedings, (ii) the review and acceptance of claims filed by the creditors, (iii) all transactions requiring the approval of the creditors' committee and of the insolvency court and all transactions required to be reported to the insolvency court, (iv) the sale of assets by way of court proceedings, and, (v) the sale of assets subject to a right for preferential treatment, may only be carried out by the reorganisation administrator. In Belgium, a transfer in part or in whole of the business to a third party has to be concluded by the court representative. In France, the powers of the debtor in possession are limited for acts exceeding day to day activities. This is also the case in Germany, where no obligations exceeding the range of his ordinary business may be entered into by the debtor without the consent of the insolvency monitor. In Latvia it is an

[429] *Kamerstukken II* 2014/15, 43 218, nr. 2. The Dutch 'pre-pack' is not similar as the English 'pre-pack'.
[430] Voorontwerp voorstel van wet tot wijziging van de Faillissementswet in verband met de invoering van de mogelijkheid tot het algemeen verbindend verklaren van een buiten faillissement gesloten akkoord ter herstructurering van schulden. The Dutch 'scheme of arrangement' should not be confused with the English proceeding with a similar name.
[431] Article 23 Bankruptcy Act.
[432] Article 68 Bankruptcy Act.
[433] Section 270 InsO.

option to set specific transactions and amounts of transactions that have to be approved by the insolvency administrator.

DIP liability under insolvency law

172. Where the debtor is a corporate entity, the question arises whether - once pre-/insolvency proceedings are commenced - special sources of liability for directors who act as a debtor in possession exist. In most Member States - e.g. in Austria, Belgium, the United Kingdom, France, Greece, Italy, Latvia, Poland, Spain, and Sweden - those special sources of liability do not exist. In most of those Member States the key triggering element is whether directors have timely filed for insolvency.[434] However, the Belgian Business Continuity Act provides for criminal sanctions to ensure transparency with regard to the debtors' estate and to ensure that creditors receive correct information, as well as to ensure a fair voting procedure.[435]

The German, Hungarian, and Dutch legislation do provide for special sources of liability for directors who act for a debtor in possession. In Germany, the directors face the liability of an insolvency practitioner.[436] In Hungary, the liability for directors who act as for a debtor in possession depends on the procedure. In a reorganisation procedure, the directors may be fined up to HUF 500.000 (some € 1575) if they fail to cooperate with the insolvency practitioner.[437] In a liquidation procedure the fine may be of an amount up to 50% of the debtors' income in the year preceding the commencement of the insolvency procedure or HUF 2.000.000 (some € 6300). This fine may be imposed even after the termination of the employment or other contractual relationship between the director and the debtor.[438] In the Netherlands, a director of a company subject to the suspension of payments procedure faces liability if acts without the cooperation of the administrator.[439]

Replacing individual directors of a debtor in possession

173. Where the debtor is a corporate entity, the question arises, once pre-/insolvency proceedings are commenced, whether the law does allow individual directors of a debtor in possession to be replaced by creditors, special advisors and/or the insolvency practitioner, and if so in what circumstances. In most Member States, it is not possible to replace individual directors by creditors or special advisors, but by the court. Replacement of individual directors by the court is for example possible in Austria, Belgium, Germany, Poland, and Spain. In Austria, the insolvency court has to revoke the self-administration and appoint a bankrupt receiver if:

i. circumstances arise which give reason to expect that the self-administration would result in disadvantages for the creditors;
ii. the reorganisation plan is not approved by the creditors within 90 days after the opening of the proceedings; or

[434] This is the case in Austria, Belgium, France, Greece, Italy, Latvia, Poland and Spain.
[435] Article 72 and 73 BCA.
[436] Section 60 and 61 InsO.
[437] Cstv. 13. Paragraph 3.
[438] Cstv. 33. Paragraph 1.
[439] Article 442 Dutch Criminal Code.

iii. such is applied by the debtor.

In Belgium, such provisions exist for judicial reorganisation proceedings. If the debtor or its directors have committed a manifestly gross error or lack good faith, an interim administrator can be appointed who will replace the directors.[440] In case of manifest negligence by the debtor or its administrators, the court may appoint a court representative in charge of performing a specific task for the duration determined by the court.[441] In Germany, the court may repeal its decision ordering debtor in possession management if the directors turn out to be negligent or incompetent if requested by the majority of the creditors' meeting, by a creditor with a right to separate satisfaction or by an ordinary insolvency creditor or by the debtor himself.[442] In Poland the court will ex officio recall the directors of a debtor in possession in a bankruptcy proceeding and nominate an administrator if:

i. the debtor has violated the law; or
ii. the manner in which he exercises management of the business of the debtor does not guarantee the performance of the arrangement (if accepted).[443]

In Spain, at the request of the insolvency officer, the court can decide to replace the directors for the insolvency officer in the exercise of administration and disposition over the assets of the debtor, for example in case of a lack of confidence of the clients or suppliers in the directors or in case of the existence of a conflict between the shareholders that is affecting the management of the company.

174. In some Member States, e.g. in Austria, Hungary, and Sweden, only the shareholders may replace the directors. In the United Kingdom, how a director can be replaced during an out-of-court workout, scheme of arrangement procedure or company voluntary arrangement procedure is a matter of the company's constitution.

Debtor not remaining in possession

175. In case the debtor does not remain in possession, the question arises which residual powers are enjoyed by directors and if their exercise is subject to any special approval requirements. In most Member States, the directors of companies in insolvency do not have any residual powers. The powers related to the assets are exercised by the insolvency practitioner. In some Member States, e.g. in Austria and Germany, the directors have the right to make dispositions with respect to assets not belonging to the insolvency estate. In Sweden, during a bankruptcy procedure, the directors are still able to represent the company alongside the administrator. Some Member States allow directors to retain their powers related to the internal activities of the debtor (e.g. to convene the general meeting of shareholders). This is for example the case in Hungary and Spain.

1.1.5.2. Significant international tendencies

[440] Article 28 (2) BCA.
[441] Article 28 (1) BCA.
[442] Section 272 InsO.
[443] Article 76 BRL.

176. Over the last years, several international initiatives are taken in the field of the phenomenon 'debtor in possession'. The debtor in possession is firstly defined by the EIR (2015): '… a debtor in respect of which insolvency proceedings have been opened which do not necessarily involve the appointment of an insolvency practitioner or the complete transfer of the rights and duties to administer the debtor's assets to an insolvency practitioner and where, therefore, the debtor remains totally or at least partially in control of its assets and affairs'.[444] The provision is based on the assumption that two or more EU Member States have included debtor in possession proceedings into their legislation.

177. In the Recommendation of the European Commission of March 2014 the concept of debtor in possession is referred to, especially in Recital 17: 'To promote efficiency and reduce delays and costs, national preventive restructuring frameworks should include flexible procedures limiting court formalities to where they are necessary and proportionate in order to safeguard the interests of creditors and other interested parties likely to be affected. For example, to avoid unnecessary costs and reflect the early nature of the procedure, debtors should in principle be left in control of their assets (… and the appointment of a mediator or a supervisor should not be compulsory, but made on a case-by-case basis)'. The role of the mediator would be one of assisting the debtor and creditors in negotiations on a restructuring plan while the role of the supervisor would be one of overseeing the activities of the debtor and taking the necessary measures in order to protect the interests of creditors and other interested parties. Reference is made to recommendation 6, specifically under (b): 'Debtors should have access to a framework which allows them to restructure their business with the objective of preventing insolvency. The framework should contain the following elements: … (b) the debtor should keep control over the day-to-day operation of its business;'. It rather seems that a debtor in possession during a restructuring never acts on its own. He is guided more specifically by a 'supervisor'.[445]

178. According to the UNCITRAL Legislative Guide 2004 the national insolvency law should clearly specify the balance of the rights and obligations between the debtor and any insolvency representative appointed as a provisional measure. Between the time an application for commencement of insolvency proceedings is made and commencement of those proceedings, the debtor is able to operate its business and to use and dispose of assets in the ordinary course of business, except to the extent restricted by the court.[446] Furthermore, the national insolvency law should specify the role of the debtor in the continuing operation of the business during insolvency proceedings. According to UNCITRAL, different approaches may be taken:

i. retention of full control of the business, with appropriate protections including varying levels of control of the debtor and provisions for displacement of the debtor in specified circumstances;
ii. limited displacement, where the debtor may continue to operate the business on a day-to-day basis, subject to the supervision of an insolvency representative, in which event the division of responsibilities between the debtor and the insolvency representative should be specified in the law; or

[444] The debtor in possession (DIP) is mentioned in Articles 6(2), 28, 29, 38(1) and (3), 55(5) and 79 EIR (2015).
[445] Reference is made to para. 1.1.2, regarding a mediator, and para. 1.1.3, concerning a supervisor.
[446] Recommendation 41.

iii. total displacement of the debtor from any role in the business and the appointment of an insolvency representative.

179. In the World Bank Principles (2016) a distinction is made between liquidation proceedings and reorganisation proceedings. Unlike the UNCITRAL, the World Bank states that in liquidation proceedings, the board of directors should be replaced by an insolvency representative with authority to administer the estate in the interest of creditors. The control of the estate should be surrendered immediately to the insolvency representative. In creditor-initiated filings - where circumstances warrant - an interim administrator with limited functions should be appointed to monitor the business in order to ensure that creditor interests are protected.[447] According to the World Bank, there are typically three preferred approaches in reorganisation proceedings:

i. exclusive control of the proceeding is entrusted to an independent insolvency representative;
ii. governance responsibilities remain invested in management; or
iii. supervision of management is undertaken by an impartial and independent insolvency representative or supervisor.

In case of the second and third approach, the complete administrative power should be shifted to the insolvency representative if the board of directors proves to be incompetent or negligent or has engaged in fraud or other misbehaviour.[448]

180. Also the Principles of European Insolvency Law 2003 provide for the possibility of a debtor in possession. According to paragraph 14.1, the debtor may, subject to supervision, be allowed to manage and dispose of the assets.[449]

181. The debtor in possession is a phenomenon well known in the USA. Characteristic for the USA's bankruptcy law system is the 'bankruptcy clause' in the US Constitution, i.e. the federal pre-emption (supremacy) of the Bankruptcy Code.[450] The states' entity governance law, however, continues to play an important role in the debtor's operations, both post-petition and post-confirmation. In the ABI Report (2014)[451] the Commission endeavoured to clarify the boundaries between the two systems and better articulate the debtor in possession's ability to transact business during the chapter 11 case. The Commission clarified the distinction between 'debtor' and 'debtor in possession'.

182. Under section 1121 of the Bankruptcy Code, the debtor may file a chapter 11 plan. When a company files a chapter 11 case, it assumes the role of debtor in possession, which has certain rights, powers, and duties different from the prepetition debtor. This distinction is important given the often competing and conflicting interests present in the bankruptcy estate and the challenges that a debtor would face if required to negotiate and draft a chapter 11 plan that satisfied some fiduciary duty to these competing stakeholders. Specifically, under section 1107 of the Bankruptcy Code, the DIP has the rights, powers, and

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447 Principle C6.1.

448 Principle C6.2.

449 In that case the proceeding follows the Principles mentioned in paragraph 1-13, except to the extent that they presuppose an administrator.

450 U.S. Constitution Article I, § 8, cl. 4.

451 American Bankruptcy Institute, '2012-2014 Final Report and Recommendations', (2014), available at https://abiworld.app.box.com/s/vvircv5xv83aavl4dp4h.

duties of a bankruptcy trustee. The DIP is also a fiduciary for the estate. Most provisions of the Bankruptcy Code relevant to a chapter 11 case authorize the trustee, and in turn the DIP, to take certain actions and exercise certain rights. Other provisions that require disclosures, impose obligations, or concern creditors' rights in the case tend to apply to, or reference, the debtor. One important exception to this general categorical divide is section 1121 of the Bankruptcy Code, which provides that '[t]he debtor may file a plan with a petition commencing a voluntary case, or at any time in a voluntary case or an involuntary case.' Moreover, '… only the debtor may file a plan until the 120 days after' the petition date.

183. On the matter of fiduciary duties, mentioned above, the Bankruptcy Code defers to state law governance principles regarding the fiduciary duties of a DIP's governing body, whether a board of directors, board of managers, or similar concentrated management structure, as well as its directors, officers, or similar managing persons. This deference generally means that those individuals or entities owe the estate duties of care and loyalty, and an obligation of good faith. These state law duties and obligations govern the conduct of those individuals or entities in operating the business and managing its affairs. In addition, state or other applicable non-bankruptcy law may require the DIP or its governing body to obtain approvals or satisfy specified conditions before taking certain actions for, or on behalf of, the debtor. Examples are state law or the debtor's articles of association requiring the debtor's board of directors to obtain the approval of shareholders before selling all or substantially all of the debtor's assets or state law requiring the board of directors to hold an annual shareholders meeting. Generally, the ABI Commission found that courts generally allow debtors in possession to proceed with section 363 sales of all or substantially all of its assets without any equity security holder approval under applicable state law or the debtor's organizational documents. The Commission agreed that the Bankruptcy Code should be amended to clarify the ability of the board of directors or similar governing body to pursue and consummate section 363 transactions without approvals required by state entity governance law, including an equity security holders' vote.

184. However, the ABI Report signals that US courts have taken a different approach to the shareholders meeting requirement.[452] Some courts review a demand on the DIP to hold the annual shareholders meeting under a norm which considers whether the shareholders' rights to vote for directors '… and thus to control corporate policy … will not be disturbed unless a clear case of abuse is made out', other courts have, however, enjoined the shareholders meeting or denied a shareholder's request to compel the meeting when the strategic objectives of the requesting shareholders are determined to be adverse to the interests of the estate.[453] In a case in which a debtor's chapter 11 plan will likely propose a new capital structure and new board members or managers, and it may propose a merger or other change in control transaction, as well as other various actions required or permitted by section 1123 of the Bankruptcy Code.[454] Although the ABI Commission

[452] Report, at 195.
[453] Report, at 195.
[454] Section 1123(a)(5) specifically provides:
'(a) Notwithstanding any otherwise applicable nonbankruptcy law, a plan shall – …
(5) provide adequate means for the plan's implementation, such as –
(A) retention by the debtor of all or any part of the property of the estate;

recognized that complying with an annual meeting requirement, or responding to a shareholder's request for a special meeting, many times will impose costs on the estate and will delay the case, it did not believe that a general prohibition on shareholders' meetings during chapter 11 cases was an appropriate response. When the debtor acting as such for the benefit of its shareholders (as opposed to the debtor in possession acting as representative of the estate) may propose a plan, it may be inappropriate to deny the shareholders the right to elect the directors who are representing the shareholders' interests. The Commission determined that this issue was best resolved by courts under the current law and the facts of the particular case.

185. In addition, the Commission discussed the interplay of bankruptcy law and applicable non-bankruptcy law in the context of transactions necessary to implement, or contemplated by, a chapter 11 plan. The Commission agreed with those courts interpreting section 1123(a) as an empowering statute and recommended that sections 1141 and 1142 be amended to clarify the pre-emptive effect of that section. Finally, it found that the pre-emptive effect of the chapter 11 plan, confirmation order, or section 363x sale order with respect to transactions included therein should not relieve the directors, officers, or similar managing persons of the debtor, debtor in possession, or reorganized debtor of their fiduciary duties under applicable state entity governance law in implementing or affecting any transactions under the plan or sale order.

186. The Commission considered the continued utility of the distinction between the debtor and the DIP in the plan process context. It observed that the debtor as a plan proponent must consider the interests of the company and the company's obligations to creditors and equity security holders in developing its chapter 11 plan. In this capacity, the debtor may be called upon to make difficult decisions concerning the business, its workforce, its assets, and its relationships with stakeholders. Although the debtor will negotiate with key stakeholders and attempt to achieve a consensus on its plan, it may not be able to start (or end) those negotiations with a plan structure that primarily benefits creditors alone. Moreover, what is in the best interests of creditors may not necessarily be in the best long-term interests of the company or its equity security holders in the plan context. The Commissioners analysed whether it would be feasible for a DIP to serve multiple masters by acting as a fiduciary for equity security holders and creditors in the plan process. The Commissioners discussed the potential conflicts of interests and competing objectives that could paralyze a debtor in possession acting in this dual role. A DIP should not be placed in the position of negotiating a plan for the company and its equity security holders with the

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(B) transfer of all or any part of the property of the estate to one or more entities, whether organized before or after the confirmation of such plan;
(C) merger or consolidation of the debtor with one or more persons;
(D) sale of all or any part of the property of the estate, either subject to or free of any lien, or the distribution of all or any part of the property of the estate among those having an interest in such property of the estate;
(E) satisfaction or modification of any lien;
(F) cancellation or modification of any indenture or similar instrument;
(G) curing or waiving of any default;
(H) extension of a maturity date or a change in an interest rate or other term of outstanding securities;
(I) amendment of the debtor's charter; or
(J) issuance of securities of the debtor, or of any entity referred to in subparagraph (B) or (C) of this paragraph, for cash, for property, for existing securities, or in exchange for claims or interests, or for any other appropriate purpose.'

creditors whose interests the debtor in possession represents as a fiduciary of the estate. A party negotiating on behalf of different parties in the same deal rarely produces the best or a fair result. Accordingly, the Commission agreed that the debtor should be separated from the debtor in possession in the plan context, and that the debtor acting as plan proponent should not be considered a fiduciary for the creditors.

187. The Commission then discussed what fiduciary duties, if any, the debtor's directors, officers, or similar managing persons should owe in the plan process. As such, the Commission found that the most efficient approach would be to impose whatever duties applicable state entity governance law would impose in these circumstances. This approach also would be consistent with other duty-related principles discussed by the Commission. In closing, the Commission proposes amendments in the Bankruptcy Code to clarify:

- that a debtor in its capacity as such and as a plan proponent, is required to comply only with its fiduciary duties under applicable state entity governance law in negotiating, drafting, and seeking confirmation of a chapter 11 plan.
- to clarify that a DIP's board of directors, officers, or similar managing persons act as fiduciaries for the debtor in connection with the plan process (including, but not limited to, formulation, confirmation, and consummation of the plan), and applicable state law fiduciary duties should continue to govern their conduct.
- to foster efficient and effective representation, in that professionals for the DIP should be able to represent the DIP in its capacity as an estate fiduciary and in its separate capacity as a debtor and plan proponent (without violating section 327 of the Code).

1.1.5.3 Debtor's/Director's duties when a business fails

188. The specific rights and duties of a DIP regime only apply once formal (judicial) proceedings have actually started. The debtor or the debtor's management in case of a company may, however, face specific insolvency-related or rescue-related legal obligation at an earlier stage.

189. For an individual entrepreneur, legal obligations with regard to their failing business commonly only stem from contract law. Covenants in financial or supply contracts may require reporting to key creditors about a deteriorating financial situation. The resulting creditor response (e.g. acceleration of payments, termination or of contracts, but also a formal motion to open insolvency proceedings) may then prompt a formal procedure by which a business rescue can be aspired. In addition, general contract and tort (or even criminal) law may require insolvent debtors to disclose their financial situation to unaware counterparties when still trading instead of filing.

190. For a company debtor, company and insolvency law commonly provides for additional legal obligations for those individuals who are in charge: the debtor's management and shadow managers.

Company Law

191. Based on the findings in relation to directors' duties in companies approaching insolvency, four main legal strategies used by Member States can be identified. As introduced earlier, these strategies are used to address the problem of inefficient risk-shifting in the vicinity of insolvency:

1. The duty to convene a meeting or the 're-capitalise or liquidate-rule'
2. The duty to file for insolvency
3. The duty to act with care (sanctioned by a wrongful trading provision)

192. According to Article 19 of the Second European Company Law Directive[455] a general meeting of shareholders must be called in case of a serious loss of the subscribed capital. It is up to the Member States to formulate the relevant conditions under which a general meeting must be called. During this meeting, the shareholders should consider whether the company should be wound up or that any other measures should be taken. According to subsection 2 of Article 19 the amount of loss deemed to be serious may not be set at a figure higher than half the subscribed capital. The majority of the Member States have implemented Article 19 of the Second European Company Law Directive as a mere duty.[456] For example in Germany the board of directors of a public company has to call a shareholders' meeting promptly if upon preparation of the annual balance sheet or an interim balance sheet it becomes apparent, or if in the exercise of proper judgment it must be assumed that a public company has incurred a loss equal to one half of the share capital.[457] Latvian law provides for a similar provision for private companies. The board of directors is obliged to convene a general meeting of shareholders in case the losses of the company exceed a half of the share capital.[458] However, it seems that the mere duty to convene a general meeting of shareholders produces costs without offering any significant benefits to companies or creditors. This is because in practice, shareholders do not take steps or resolve matters during these type of meetings.[459]

193. With regard to the public company, Latvian law applies the so-called 're-capitalise or liquidate-rule'. This rule goes beyond the mere duty to call a general meeting under Article 19 of the Second Company Law Directive. The Member States who adopted this rule,[460] require companies upon loss of half of their subscribed capital to make a choice between either re-capitalising the company or liquidating the company.[461] The Latvian public companies' legislation is a good example and provides that if the losses of the company exceed half of the share capital of the company, the board of directors shall notify the council regarding this fact and shall convene a meeting of shareholders, where it shall

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[455] Directive 2012/30/EU of the European parliament and of the council of 25 October 2012 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 54 of the Treaty on the Functioning of the European Union, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent.

[456] Austria, Belgium, Germany, Greece, Hungary, Latvia (for the private company only), The Netherlands, Poland, and The United Kingdom.

[457] Article 92 subsection 1 AG.

[458] Section 219 Commercial Law 2000.

[459] Study on Directors' Duties and Liability, prepared for the European Commission DG Markt by: C. Gerner-Beuerle, P. Paech and E.P. Schuster, 2013, p. 216.

[460] France, Italy, Latvia (for the public company only), Spain and Sweden.

[461] In Italy the choice between liquidation and recapitalization is due when the loss exceeds the subscribed capital (Article 2447 and Article 2482ter Italian civil code).

provide explanations. The meeting of shareholders subsequently shall decide regarding the covering of the losses, or shall take one of the following decisions: (i) to allocate appropriate security to creditors of the company; (ii) to reduce equity capital; (iii) to terminate the operations of and to liquidate or reorganise the company, or (iv) to submit a petition for insolvency.[462]

194. Another example can be found in the Swedish legislation. If the board has a reason to suspect that the company's assets do not cover more than half of the registered share capital the board of directors is obliged to immediately draw up a controlling balance sheet to be reviewed by the company's auditor. If the balance sheet shows that the company's net assets are indeed less than half of the registered share capital, the board of directors has to convene a shareholders' meeting. The shareholders' meeting has three options: (i) to augment the assets in the company to cover the share capital, (ii) to liquidate the company or (iii) to proceed the business for a maximum of eight months (if at the end of the period eight months the share capital is not entirely covered, the company has to be liquidated).[463]

195. The laws of most Member States provide a ground for liability in case the board of directors fails to convene a meeting of shareholders and/or other obligations connected with it are not met. In Sweden for example, the directors become personally and jointly liable for the company's obligations that incurred during the period in which the obligations of the directors are not met.[464]

196. In addition, directors are subject to general duties protecting the company, its shareholders and its stakeholders against mismanagement and misconduct. However, if the company approaches insolvency, the addressees of the main duties of directors may change. The change of directors' duties is caused by the change of the corporate objective of companies in financial distress, ie a shift from acting in the best interest of the company to acting in the best interest of the creditors. In general, directors have a duty to act in the best interest of the company. In most Member States, this is characterised by the stakeholder approach.[465] In these Member States the duties of the directors are aimed at benefitting all the stakeholders. Mostly, this duty is not specifically codified in the Member State's company law, but is developed in jurisprudence. Dutch law for example only states that in the performance of their task, the directors of a company conform to the interest of the company and the business connected with it.[466] In the minority of the Member States,[467] for example in the UK, there is an emphasis on acting merely for the benefit of the shareholders. If a company approaches insolvency, however, in all Member States the duties of the directors are more focussed on the interests of the creditors. This is also the case in the Member States who do not apply the stakeholder approach, such as the UK. According to Section 172 of the Companies Act, the director’s fiduciary duty to promote the success of the company is expressly subject to any enactment of rule of law requiring directors, in certain

[462] Section 271 Commercial Law 2000.
[463] Sections 13-16, Chapter 25 Companies Act.
[464] Section 18, Chapter 25 Companies Act.
[465] Austria, Belgium France, Germany, Greece, Hungary, Italy, The Netherlands, Poland, Spain and Sweden.
[466] Article 2:129/239 (4) DCC.
[467] Latvia and The United Kingdom.

circumstances, to consider or act in the interests of the creditors of the company when it is nearing insolvency, see Section 172(3) of the Companies Act 2006.

Duty to file

197. One main strategy used by the Member States to ensure creditors' interests are properly taken into account in the vicinity of insolvency is the duty for a director to timely file for insolvency. This duty on the part of the board of directors exists in the majority of the Member States.[468] However, the time in which the directors have to file for insolvency varies widely across the Member States. Furthermore, there is some uncertainty in some Member States as to when this time period actually begins. This might cause legal uncertainty because mostly, the duty to file is connected with a consequential liability for any depletion of the company's assets resulting from the delayed filing. Finally, there are some differences in the nature of liability.

198. The circumstances triggering the duty to file for insolvency proceeding vary across the Member States. Therefore, the specific reference time upon which the board of directors has to file for insolvency, is not always clear. In some Member States[469] the relevant triggering factors are illiquidity (when the company is unable to pay its debts as they fall due, or: cash-flow insolvency) and over-indebtedness (when the company's liabilities, including its contingent and prospective liabilities, exceed its assets, or: balance-sheet insolvency), while other Member States[470] only make use of the 'cessation of payments of debts-requirement'.

199. In addition, the time period in which directors have to file for insolvency varies across the Member States. In Germany, Greece and Austria, the directors have to file without undue delay and in any case within three weeks,[471] 30 days,[472] respectively 60 days[473] after 'insolvency' as defined above occurred. In Belgium the directors have to file within one month,[474] in Poland within 30 days, in France within 45 days[475] and in Spain within two months.[476] Latvian law does not provide for a specific time period in which the directors have to file for insolvency.
The duty to file for insolvency is buttressed by a consequential liability of directors for any depletion of the company's assets resulting from the delayed filing, commonly a civil liability.[477] In some Member States, however, late filing also amounts to a criminal offense.[478]

[468] Austria, Belgium, France, Germany, Greece, Italy, Latvia, Poland and Spain.
[469] See e.g. Austria, Germany, Poland.
[470] See e.g. Belgium and France, also Latvia.
[471] Section 17(2) InsO.
[472] Article 98 GBC.
[473] Section 69(2) Insolvency Code.
[474] Article 9 Belgian Bankruptcy Act.
[475] Article L 640-4 French Commercial Code.
[476] Article 5 Insolvency Act.
[477] See e.g. Austria, Belgium, France, Greece, Italy, Latvia, Poland and Spain.
[478] See Austria, Belgium Germany, Italy, Latvia and Poland.

200. Instead of adopting the duty to file for insolvency, some Member States[479] provide for a duty to cease trading when creditors' interests are at risk, the so-called 'wrongful trading-rule'. This alternative approach may be illustrated best by a quick reference to English law where the wrongful trading provision is laid down in Section 214 of the Insolvency Act 1986. A director who knew or ought to have known that a company had no reasonable prospect of not entering insolvency and did not take every step to minimise potential losses to creditors can be held personally liable. To assess whether a director is guilty of wrongful trading, a subjective test and an objective test are applied. The facts which a director of a company ought to know or ascertain, the conclusions which he ought to reach and the steps which he ought to take are those which would be known or ascertained, or reached or taken, by a reasonably diligent person having:

a. the general knowledge, skill and experience that may reasonably be expected of a person carrying out the same functions as are carried out by that director in relation to the company (the objective test) and;
b. the general knowledge, skill and experience that a specific director has (the subjective test).

201. In addition to this ‘knowledge condition’, a ‘minimising loss defence’ exists under Section 214(3), providing that the court shall not order compensation if it is satisfied that the director concerned took ‘every step’ with a view of minimising the potential loss to the company’s creditors.[480]

EU harmonisation efforts

202. In company law, Article 19 of the Second European Company Law Directive provides for the necessity of convening a general meeting of shareholders in case of a serious loss of the subscribed capital. According to the European Commission, this requirement could jeopardise the effectiveness of the restructuring plan's adoption and implementation.[481] Therefore, Article 32 of the Proposal requires Member States to derogate from this provision to the extent and for the period necessary for the establishment of the preventive restructuring framework.

203. Apart from company law directives, harmonisation on EU level in the field of director’s liabilities in the vicinity of insolvency is still lacking. These gaps and deficiencies with regard to the substantive rules on directors’ duties on a EU-level, create legal uncertainty and a cross-border investment barrier.[482] On 22 November 2016, the European Commission adopted its legislative proposal on preventive restructuring, insolvency and second chance that might lead to a harmonised set of director’s duties.[483]

1.1.5.4 Impetus for recommendations

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[479] See England & Wales, Hungary, The Netherlands, also Sweden (where it may also lead to criminal prosecution).
[480] Compare Jente Dengler, Wrongful Trading: Scaring off Reckless Directors, in 13 International Corporate Rescue 2016, p. 413 et seq.
[481] Explanatory Memorandum of the Proposal, p. 11-12.
[482] EcoDa & AIG, Guide to Directors' Duties and Liabilities, p. 8.
[483] See Article 18 of the Proposal Restructuring Directive (2016).

204. Any rules regarding the debtor from the perspective of a failing business should contain some very basic specifications. They should differentiate between individual and company debtors and address, in the latter case, management and shareholders specifically. In addition, they should provide for a consistent set of rules for all stages of a business crisis in company and insolvency law. Finally, rules for a debtor in possession in a (reorganisation or insolvency) procedure must reflect the specific purpose of leaving the debtor in control.

Companies and individuals

205. The position of a debtor can be very different. In case of an individual entrepreneur, the debtor itself is a human being with all the self-interest in maintaining reputation, income and self-respect from running a business. At the same time, becoming insolvent is an essential threat to the economic existence and future of the entrepreneur – often followed by a high post-procedure debt burden and no income. Here, social aspects are important and debt relief tools should be used to incentivise debtors to use procedural options actively and timely.

206. In contrast, where the debtor is a company or even a corporation, shareholders and managers are the individuals to focus on. These actors are often only involved with a limited risk exposure. Directors often only have an employment and bonus oriented incentive to act in times of crisis. Shareholder interests are more complex. While corporate shareholders may only seek a way to recover their equity investment, company shareholders would actually fear a personal liability for all company debt. Rules that aim at safeguarding a business rescue must recognise such differences.

Monitoring and externalising

207. Any legal restructuring and insolvency framework is only able to provide for the rescue of viable businesses and the efficient liquidation of non-viable businesses if the framework gets involved at a stage in the firm's crisis where a rescue is still feasible or, at least, funds still exist to cover an orderly liquidation. Early access to such a framework is essential. Any decision to access a restructuring and insolvency framework requires the insight that a problem exists and the will to make use of the tools of the framework.

208. The timely realization of a crisis can be safeguarded by monitoring or book-keeping obligations. Such obligations are to be addressed to the individual debtor or the director of a company in terms of statutory rules (e.g. under company law) or contracts (e.g. covenants).

209. Where signals of a crisis are detected, a duty to report is required to make sure that such signals are not ignored. Contract terms may require a report to the counterparty (e.g. a major lender or supplier). Company law rules should oblige directors to report to shareholders; capital market rules already include a duty to immediately report market-relevant information. Reporting duties may, however, also involve third parties. They could be extended to advisors and creditors with insider knowledge (e.g. tax advisor, tax or social security agencies, financial creditor who is informed under covenants). On the receiving end, reports could be sent to external players involved in an early warning framework, like e.g. business support institutions (see Chapter 2).

210. Faced with such a report, shareholders must decide whether to re-capitalise the company or liquidate it. If they consider a recapitalisation, they would have an option to do so under company law or can decide to use the tools of restructuring proceedings, e.g. where a unanimity requirement under company law hinders a decision. Informed creditors would have to decide whether they want to continue trading and, if so, under which conditions.

211. From the perspective of a monitoring and reporting framework, any debtor is obliged to inform contractual counterparties about a substantial risk of default when contracting after the detection of a crisis. The wrongful trading approach can, thus, be easily traced back to fundamental contract law principles that provide for a liability for any individual acting for the debtor (e.g. the individual debtor himself or the company's director).

212. Introducing extensive duties to monitor and report must, however, not raise the risks of involved and obeying parties to be liable based on the acquired knowledge. Legislators must provide for a safeguarding 'safe harbour' for informed stakeholders that respond to reports by continued trading or crediting against possible fraudulent transfer claims or civil liability based on that very fact.

212. In such a framework, filing a motion to commence formal restructuring or insolvency proceedings is nothing but a (late) way to report and externalise a detected existential business crisis. Such a filing can be done based on the decision to cease the business operation. It can also follow a decision to restructure under restructuring law conditions or to try and sell a business in a liquidation procedure as a going-concern. Still, a right to file is clearly distinct from a duty to file, in particular if such a duty is connected with a criminal charge. Such a duty would require clearly defined elements which is difficult to do when referring to an economic situation (illiquidity, over-indebtness). Experience in Member States with a duty to file (like e.g. Germany) shows that even a harsh duty to file has not actually solved the problem of late filing. Overall, it seems preferable to impose widespread rights to file for insolvency amongst informed stakeholders combined with an early duty of the debtor/director to report a failing business situation timely to shareholders and creditors (e.g. a significant loss of capital or negative business earnings for a subsequent number of years or the moment the director foresees illiquidity). Thus, stakeholder would gain time to respond to a deteriorating business situation which gives them more options to turn the business around. At the same time, the motion to initiate formal proceedings would not only be in the hand of the debtor/director, but also in those of other stakeholders. Still, if the director ignores the duty to give notice of crisis thresholds, he should be liable for any damage cause for the company. Any liability against creditors should follow only from contract law principles (e.g. a general duty to inform about a crisis when negotiating a contract).

Specific duties in procedures

213. In restructuring or insolvency proceedings, the debtor's business should be administered by the debtor (DIP) if such proceedings aim solely at a business rescue and interruptions to business operations should be minimal. Here, creditor interest can be

sufficiently safeguarded by a supervisor and an option to terminate such proceedings where restructuring efforts fail or stall (see Chapter 2).

214. In unified proceedings like the Croatian, German, or Spanish insolvency procedure where a restructuring is possible but not the sole possible outcome, the debtor should only remain in possession where proceedings are initiated with creditor support in order to achieve a restructuring (pre-packaged plan). We hold that the DIP option is a restructuring tool only.

215. Thus, in accordance with the World Bank Principles, the debtor/directors should be replaced by an administrator in liquidation-oriented proceedings. The goal of liquidating the company's assets and paying its creditors can be reached most efficiently by an insolvency practitioner acting as an administrator. It is conceivable that the debtor in possession has a conflict of interest during a liquidation proceeding, for example in case of directors' liability for wrongful trading.

1.1.5.5 Recommendations

Recommendation 1.14: Member States should provide for a monitoring and reporting framework that includes a 're-capitalise or liquidate-rule' for companies and a duty to convene a shareholders' meeting upon loss of half of the subscribed share capital of the company.

Recommendation 1.15: During this meeting, the board has to present and discuss any proposed preventive restructuring measures, while the shareholders have a duty to decide to: (i) initiate workout negotiations, (ii) file for a restructuring procedure, (iii) to voluntarily wind up and liquidate the company, (iv) to file for insolvency liquidation.

Recommendation 1.16: Member States should introduce a 'safe harbour' defence to allow directors of a solvent company in financial distress to explore, with certain guidelines to be set, restructuring options without the risk of liability for insolvent (wrongful) trading.

Recommendation 1.17: Member States should provide for a duty for directors to timely inform shareholders and, where appropriate, other stakeholders (like e.g. suppliers or financial creditors) as soon as a business misses specific thresholds (e.g. a significant loss of capital or negative business earnings for a subsequent number of years or the moment the director foresees illiquidity). Any breach of such a duty should make the director liable against the company for damages. Member States should allow creditors and shareholder to initiate restructuring and insolvency proceedings based on such notice instead of a duty for company directors to file immediately.

Recommendation 1.18: The European Commission or other European institutions should support a comparative and empirical study on the duties and liability of directors of a failing company in the stage of a workout as well as in the position of a debtor in possession in proceedings.

1.1.6. Turnaround management

216. In the land of businesses, a multiple number of advisors are available to assist any company in achieving its goals. For business that have troubles with operational of financial performance, foresee rapidly changing sales channels (like internet), changing markets (renewal of legislation), changing customers' taste or changing sources for primary funding (upcoming private investors) advisors can be called upon. A segment of this group of consultants use, as a professional name 'turnaround manager' or 'corporate restructuring specialist'. What are their jobs? Although turnaround and turnaround management have no unified definition, scientific and professional literature mention a number of features that recur, leading to the following general description: turnaround management is the dynamic process of restructuring of a company which is in a life-threatening crisis, or, if no decisive action is taken, will end at some time in such a situation. The most important characteristics for such a management process include (i) to prevent imminent discontinuity (i.e. insolvency liquidation) as a goal, (ii) to foster (sustainable) recovery of the company by taking thorough measures at strategic, operational and/or financial level, as well as (iii) to initiate changes with regard to the company, its legal and organisational structure and the internal processes (production; services) of the company.

217. Turn around managers, advising in these matters, understand to act 'in the shadow of the law'. Their advice will be considering elements of law which will be relevant when taking actions based on the turnaround managers advise (or when taken no action at all): applicable laws on dismissal of employees, contractual positions of suppliers, financial positions of lenders, rules on liability of directors. Turnaround managers may limit themselves to advice, but in practice they will be heavily involved in implementation of the board's decisions, including negotiations with all stakeholders involved.[484]

218. In the lifecycle of a business and its many stakeholders the role of a turnaround manager is of utmost importance. In markets with heavy price competition the business will be struggling for its survival and pleased when the next few months no losses will have to be born. In other markets, a short termed view will be: we're sure better times are looming, the economy restores, the market might pick up again and the customers return. Lenders and for instance suppliers of goods and services will have a longer term view: will the company have a future existence?; isn't not too far slipped behind compared to its competitors?, and, if so, what is the best strategy today for a lender, terminate the loan and then take possession of collateral? Or allow some time to find new money from a new or an additional lender?

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[484] See Pandit, Some Recommendations for Improved Research on Corporate Turnaround, in M@n@gement 3(2), p. 31: '… A [corporate] turnaround may be defined as the recovery of a firm's economic performance following an existence-threatening decline. The decline may occur over several years although there are situations when extraordinary events occurring over a shorter period of time can place a firm in peril (…) A successful recovery, in its most subdued form, may involve mere survival with economic performance only just acceptable to the firm's various stakeholders. On the other hand, in its most positive form, the recovery may lead to the firm achieving sustainable, superior competitive positions in its chosen areas of activity …' The process of turnaround management has been described in Jan Adriaanse, Dick van Offeren and Jean-Pierrre van der Rest, *Turnaound Management* (Serie Recht en Praktijk Insolventierecht 7, Deventer: Wolters Kluwer 2016). For an overview of historical, business and ethical issues, see Jan Adriaanse and Jean-Pierre van der Rest (eds.), *Turnaround Management and Bankruptcy* (New York: Routledge 2017).

And the company: should it inform suppliers? In this zenith of conflicting interests, the task of a turnaround manager is crucial in navigating the company to its future and many times to assist in creating confidence of all parties in an economic survival in the medium-term. Including parties in negotiations and buying into a turnaround plan and a restructuring plan will be a challenge and the plan itself an important tool.

1.1.6.1 Turnaround manager in the EU

219. Turnaround activities may be a part of the role of IOHs. In England for instance, during administration, that administrator has wide powers to manage the company, including to do anything necessary or expedient for the management of the affairs, business and property of the company. Although there may be no court involvement whatsoever (appointment of permission to take certain actions) an administrator is an officer of the court which imposes upon him or her a general duty to act in good faith, fairly and honourably while in office.[485]
Whereas in the zone close to insolvency consensual restructuring should preserves more value and would save more jobs the professional advising should have specialist skills, both commercial and legal. Using an advisor who is insufficiently trained and may have other interests in mind that the independent review of the interests of the company and its stakeholders should be prevented. It is necessary to sift the wheat from the chaff.

220. Mention is made of a recent initiative of Turnaround Wing INSOL Europe. In October 2014 this group commissioned a project to the Leiden Law School to design 'Guidelines for out-of-court turnaround professionals'. By setting professional and ethical standards for the profession in Europe, these guidelines aim (i) to offer leadership to turnaround practice in Europe, (ii) to promote out-of-court restructuring rather than liquidation, (iii) to provide the basis for a long-term sustainable future for the business by ascertaining the quality of turnaround professionals, and (iv) to enhance the trust in the profession on the market.
The guidelines explicitly target out-of-court turnaround professionals.

1.1.6.2. INSOL Europe Turnaround Wing Guidelines

221. The Leiden Law School team has, with the involvement a many, drafted so-called INSOL Europe Turnaround Wing Guidelines (TW Guidelines), which define what turnaround and restructuring mean. There are six guidelines. Guideline 1 describes when the TW Guidelines apply, i.e. only in out-of-court assignments. Guideline 2 is on Professional Attitude, Guideline 3 on the Ethical Attitude of the Restructuring and Turnaround Professional (RTP). The essentials on Communication with the Client, Communication with Stakeholders and on Governance are covered by Guidelines 4 – 6.[486]

[485] *Ex parte James* (1874) L.R. Ch. App. 609. An administrator may always apply to the court for directions in connection with his functions.

[486] In Summer 2015, out of 117 respondents, 75% agreed with the TW Guidelines of which 21% strongly. In a Report of September 2015 recommendations are included in order (1) to have the TW Guidelines accepted by INSOL Europe, (2) to encourage application by the INSOL Europe membership in practice, (3) to have this application monitored by a monitoring committee, and (4) to adapt and expand the TW Guidelines gradually according to the findings of the monitoring committee. It also lists a number of issues that may have to be dealt

1.1.6.3. Recommendation

Recommendation 1.19: Member States should ensure that the relevant professional bodies are involved in the creation of standards and guidelines that will apply to turnaround managers and that they take into account best practices for appropriately regulated professional parties as set out in principles and guidelines on regulation of the restructuring and insolvency profession developed or adopted by European and international non-governmental organisations active in the area of restructuring and insolvency, such as the INSOL Europe Turnaround Wing Guidelines (TW Guidelines).

1.1.7. Chief Restructuring Officer

222. In practice, in order to achieve the goal of having a distressed debtor perform successfully under a certain plan and within a certain time, a Chief Restructuring Officer (CRO) may be appointed.[487] Although in practice the term is used in different settings, we focus on a turnaround manager, specifically accepting an appointment as a statutory director under company law, with a specific task. Generally, a CRO will have the required skills and management experience to drive operational as well as financial restructuring. He can assist management in leading the restructuring or may have a more distinctive role in cases where management lacks the appropriate skills or time to implement the restructuring plan. A CRO will generally possess direct relevant skills and experience with all matters of restructuring, such as negotiating with the companies stakeholders, including lenders, dealing with portfolios holding distressed or illiquid assets, restoring trust between e.g. shareholders and company management, but also have the relevant psychology insights to deal with senior management, the capacity to create clarity of (and confidence in) its position (‘fly on the wall for financial creditors’ or true independent advisor) and to drive operational change against reluctant managers or employees.[488]

223. In literature (scanty, for that matter) it is submitted that a CRO should have three primary responsibilities throughout the whole process of the restructuring: (i) bringing credibility and objectivity to the restructuring process, (ii) driving and creating stability to the entire restructuring process, and (iii) building a consensus amongst stakeholders about the direction of the restructuring.[489] In its position as trusted advisor, taking in account all

with in the next phase of the project (‘TW Guidelines 2.0’). For all relevant documents, see http://www.tri-leiden.eu/project/categories/turnaround-wing-project/.

[487] CRO does not mean Cathode Ray Oscilloscope (which pops up when googling for ‘CRO’) or Chief Risk Officer. We use the abbreviation CRO but in practice one also come across terms as Chief Restructuring Advisor (CRA) or Chief Transformation Officer (CTO). See Samantha Wood, ‘Fund Crisis and Change Management: A Fresh Approach’, International Corporate Rescue 2015-4, p. 234 et seq.

[488] In practice it is debated whether a CRO needs to be an industry specialist and whether s/he should ‘put out fires in the early days of the appointment’, see report on a discussion in INSOL World Second Quarter 2014, p.24.

[489] See Bob Rajan, Jan Dettbarn & Steffen Kronier, ‘The ABCs of the CRO’, eurofenix Summer 2014, 24 et seq., also available at http://www.alvarezandmarsal.com/sites/default/files/sidebar-callouts/chief-restructuring-officer.pdf. Stakeholders include: statutory directors, equity holders, debt holders, employees, suppliers, customers, and communities (representatives of regions where the debtor has operations, representatives/defenders of e.g. environmental interests or human rights. See also Detlev Specovius &

interests of the debtor and its stakeholders it should be warranted that a CRO is truly independent. Generally, practice favours a CRO, not as an advisor, but with executory powers.[490] In favour of such powers are the fact that it will generally provide stature, trust in accountability and right governance. As a disadvantage counts the fact of a CRO's same position as other directors with regard to matters of third party liability and his appointment also can be seen as a vote of confidence to the existing team of director.

Considering the uncertainties, we would, therefore, suggest the following:

Recommendation 1.20: The European Commission or other European institutions should support a comparative and empirical study on the role of a Chief Restructuring Officer (CRO) with the aim to formulate its specific (autonomous) powers, the way these relate to the other directors of the company as well as the CRO's accountability to all stakeholders involved and its liability for damages to third parties.

Katharina Uffmann, 'Interim Management in der Unternehmenskrise', Zeitschrift für Wirtschaftrecht (ZIP) 2016, 295 et seq.; Ann-Marie Laing and Alastair Beveridge, 'Assessing the Effectiveness of and Challenges facing Chief Restructuring Officers', INSOL International, June 2016. In this report it is submitted that based on a rather limited set of interviews, the general view was that it was easier to deliver the role of CRO as a company executive than as an advisor.

[490] The USA's Chapter 11 proceeding is a foreign insolvency proceeding in the meaning of § 343 of the German Insolvency Act. A CRO can be regarded as a debtor in possession; he fulfils the function equivalent of the German insolvency practitioner (*Insolvenzverwalter* ex § 113 German Insolvenzy Act), and therefore has the power to terminate an employment contract of an employee working in Germany, see Bundes Arbeids Gerechtshof 24 September 2015, NZI 2015, 1041; EWiR 4/2016, p. 121-122, with commentary of Paulus.

1.2. Procedural design of a restructuring and insolvency framework

224. The questionnaire used a specific language that requires an explanation. Along with common taxonomy,[491] we basically distinguish three types of (possibly) rescue-oriented procedures that need to be defined:

- **Workout**: The debtor concludes a contract with all relevant creditors and other stakeholders that contains a solution to the debtor's financial problems. A workout is a purely contractual solution, no courts are involved. This is why we also refer to such contracts as informal, private or out-of-court workouts.
- **Pre-insolvency proceedings**: A jurisdiction offers a judicial procedure with the sole purpose of rescuing a business in difficulties independent of their (formal) insolvency proceedings. The degree of court involvement into such procedures can be either substantial (e.g. with a court supervising restructuring negotiations, disclosure and plan voting) or minimal (e.g. with a court only involved after a restructuring plan received support from a majority but not all creditors; such procedures mix out-of-court workouts with a court involvement which is why they are often called "hybrid procedures"[492]).
- **Formal (restructuring and insolvency) proceedings**: Every jurisdiction provides for court proceedings that are designated for insolvent debtors only. Such proceedings require an insolvency test and court involvement from day one. They may not be rescue-oriented per se but provide for legal instruments to conduct a business restructuring or a going concern sale of the viable business (parts). Where jurisdictions do not immediately open such proceedings upon a motion in order to enable an in-depth insolvency test, interim proceedings are common. In our ELI Business Rescue Report, such interim proceedings are seen as being the initial part of formal insolvency proceedings.

1.2.1. Workout

225. A workout is a contract between the debtor and those creditors (and additional stakeholders like, for instance, a car manufacturer in auto supplier cases) that need to contribute in some way to resolve difficulties in the debtor's business. Often these difficulties arise from financial obligations that need to be served, e.g. an expiring line of bank credit or a maturing bond). Whenever (re-)financing such obligations is uncertain, the debtor's insolvency is at least probable, if not imminent. An extension or a restructuring of these obligations, or a refinancing agreement are required.

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[491] See Mihaela Carpus Carcea, Daria Ciriaci, Dimitri Lorenzani, Peter Pontuch, Carlos Cuerpo, 'The Economic Impact of Rescue and Recovery Frameworks in the EU' European Commission's Discussion Paper, September 2015, p. 4.

492 *Ibid.* See also Jose M. Garrido, *Out-of-Court Debt Restructuring* (World Bank Study 2012), paras. 1, 93, or Burkhard Hess, 'Hybride Sanierungsinstrumente zwischen der Europäischen Insolvenzverordnung und der Verordnung', in Alexander Bruns et al., (eds.), *Internationales, europäisches und ausländisches Recht, Festschrift für Rolf Stürner zum 70. Geburtstag* (Tübingen: Mohr Siebeck 2013), 1253-1261, or Rodrigo Olivares-Caminal, 'Introduction', in Rodrigo Olivares-Caminal (ed), *Expedited Corporate Debt Restructuring in the EU* (OUP 2015), 1.08 and 1.43.

226. The fundamental challenge for the debtor, when renegotiating debt contracts, arises from the fact that any change of these debt contracts are contracts themselves. A workout solution requires the actual contractual consent of all parties. And while the principle of contractual freedom allows the debtor to try and renegotiate the debt contract with relevant creditors only as well as to propose any restructuring solution that they hold fit, the principle also allows each and every creditor to decide whether or not to accept that proposal. This leaves creditors with a strong position at the table in a negotiation that is being conducted in the shadow of the debtor's insolvency.[493]

227. In order to arrive at an agreement, the debtor must be able to convince the relevant creditors that a performance of the debt contract is not possible although the business is viable and profit-making, and that accepting the restructuring offer is the best possible deal in the given situation. The inability of the debtor to achieve a creditor's consent despite workout efforts may originate from two very different ways in which creditors confront the debtor: a rational and a strategic hold-out. Both types of hold-outs need to be addressed separately.

1.2.1.1. Rational hold-outs

228. Creditors act rationally if they do not consent to a workout solution that does not convince them. Maybe they do not trust the proposed solution because they do not see why their claims cannot be paid in full or why the haircut must be as extensive as proposed; or maybe they need the full fulfilment of the claim as they need the liquidity themselves to meet their debts; or maybe they do not trust the debtor('s management) with the task of restructuring the business. To address such trust issues, the distribution of information is key. Debtors must fully disclose their business and secure the early and complete disclosure of all relevant information. Here, a legal framework may provide assistance. Our inventory reports indicate several instruments that eventually aim at trust building.

- Many Inventory Reports[494] refer to codes of conduct, a soft law instrument that repeat players in workout negotiations with troubled businesses (usually banks) have established. These non-binding rules provide for measures necessary to create space for successful negotiations when they advocate standstill-agreements, a preference for fresh money and ways to communicate and to distribute information.[495] They can be considered as an international standard.[496]

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[493] See e.g. V. Finch, 'Doctoring in the Shadow of Insolvency', The Journal of Business Law, November 2005, p. 690.

[494] Most prominent example is the "London Approach", a best practice amongst London City banks initiated by the Bank of England's informal set of principles in the late 1970's. For an analysis, see J.H. Armour and S. Deakin, 'Norms in Private Insolvency: the "London Approach'' to the Resolution of Financial Distress', in 1 Journal of Corporate Law Studies 2001, 21. See also Chapter 1.1.2.2 on international developments in insolvency mediation. According to our Inventory Reports, similar guidelines exist in Italy, Latvia, and are a work in progress in Greece and Poland. A similar best practice was reported for Spain. For Austria, see the 2015 "Restructuring Guidelines" published by repeat players ("Grundsätze für Restrukturierungen in Österreich"; available at http://www.schoenherr.eu/uploads/tx_news/Restructuringguide.pdf).

[495] Ibid.

[496] See the eight principles of INSOL International Workout Principles II (2017); Core Principle 3 of the EBRD Core Principles for an Insolvency Law Regime (2004); the Asian Bankers Association's Asia-Pacific Informal

– A “stick” to incentivise creditors to participate in workouts could be statutory rules or case law requiring creditors to participate in workout negotiations, or even making creditors liable for their unreasonable hold-out to a useful debt restructuring. However, our Inventory Reports have not disclosed such case law in one of their 13 jurisdictions.[497] Whether cases will occur under the new provisions of the French Code Civil, introduced in 2016, which introduced a path to amend debt contracts under the new “unforeseeability doctrine”,[498] remains to be seen.

– A hold-out may also be rational where extending credit or provide new finance in a refinancing deal carries the risk of a civil liability and of fraudulent transfer claims or subordination if the restructuring fails and the debtor enters in insolvency proceedings. In this regard, a clearly defined safe harbour for credit agreement in a restructuring is useful.[499] In Belgium, a workout agreement can be filed with the court (“informal amicable settlement[500]) which protects a performance under the agreement from future avoidance actions. In Greece, tax incentives and public debt relief to qualifying debtors and financing institutions have been enacted to facilitate the restructuring of non-performing loans out of court.[501] In Spain, Article 71 (bis) of the Insolvency Code provides for a safe harbour for Refinancing Agreements after being approved by an independent expert from the Commercial Registry.

– The French Inventory Report[502] refers to a (statutory) right for the debtor to involve a third party to act as supervisor and/or mediator.[503] In addition, a court would be

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Workout Guidelines for Promoting Corporate Restructuring in the Region (2013); Principle B3 of the World Bank Principles for Effective Insolvency and Creditor/Debtor Regimes (2016).

[497] In Germany, the Supreme Civil Court (BGH) denied such duties for creditors in a workout in 1993; see BGHZ 116, p. 319. Minority shareholders of companies with a large number of shareholders (often investment companies) may, however, be required to either support a restructuring initiated by a majority of shareholders in good faith or run the risk of being excluded; see again BGHZ 129, 136; BGHZ 183, 1 – *Sanieren oder Ausscheiden*.

[498] See C Ottaway and G Harang, ‘Reform of the French “Civil Code”’, eurofenix summer 2016, 32. See also Chapter 7.

[499] See the French Conciliation where fresh money provided under an agreement approved by the court enjoys a privilege in subsequent insolvency proceedings. Under German case law, fresh money provided under a feasible restructuring plan in good faith is safe from any liability but not enjoying a preference (see e.g. Herwart Huber, *Die Bedeutung des Sanierungskonzepts für eine Kreditgewährung an den kriselnden Unternehmenskunden*, NZI 2015, 489; see also BGH ZIP 2016, 1235). The European Commission also favors such safe harbours, see Recommendatios 27-29 of the Commission’s Recommendation (2014), or Article 10(1)(b) Proposal Restructuring Directive (2016).

[500] Article 15 BCA.

[501] See Law 4307/2014 (Article. 61) which introduced an emergency out-of-court work-out for applications filed until 30.9.2016. In Italy, tax incentives exist as well.

[502] In France, any debtor may request the appointment of a “mandataire ad hoc” in charge of facilitating and supervising workout negotiations with main creditors (Mandat ad hoc Article L. 611-3 of the Commercial Code). In contrast, only a debtor facing ‘legal, economic or financial difficulties’ may request the appointment of a conciliator by the President of the Commercial Court to assist in reaching an agreement with its main creditors and contractual partners that can later even be approved by a court (Conciliation; Article L. 611-4 et seq. of the Commercial Code). For an analysis, see Axel Flessner, ‘Insolvenzverfahren ohne Insolvenz?, Vorteile und Nachteile eines vorinsolvenzlichen Reorganisationsverfahren nach französischem Vorbild’, KTS 2010, p. 127 et seq.

involved in this process, thus turning pure out-of-court negotiations into a type of (pre-insolvency) court proceedings. The Spanish "Out-of-court payment agreement"[504] provides for a mediator for SME, appointed by the Commercial Registry or a Notary Public, to facilitate workout negotiations.

- Workout negotiations benefit from being timely initiated. With less time pressure, an obviously prudent debtor and possibly more value and liquidity still with the debtor's business, the chances of meeting support in workout negotiations should be higher. The Belgian Report refers to an "Enquête commerciale - Handelsonderzoek" ("commercial investigation procedure" under Articles 8-12 BCA) that seeks to prevent undertakings from becoming insolvent by monitoring their financial position and encouraging business reform at early signs of trouble.[505] French law provides for a voluntary "prevention group" with similar tasks. Accounting duties for the debtor, which only just allow them to actually monitor the firm's finances, and early warning mechanism in debt contracts, auditor and accountant contracts[506] or company law[507] could be useful to support the debtor.

229. Another tool to support a workout is the availability of a creditor action stay or moratorium in case a voluntary standstill agreement is not concluded. Such a moratorium would impair the right of affected creditors to collect on their claims or to utilise a contractual termination right (ipso facto clause), and it would, therefore, require a court order under the fundamental rights protection of most jurisdictions.[508] Such a court involvement would prompt an out-of-court workout negotiation to become, at least, a hybrid procedure. The availability of a moratorium will, thus, be discussed at 1.2.2.

1.2.1.2. Strategic hold-outs

230. While rational hold-outs can be addressed with trust-building instruments, a strategic hold-out needs a very different approach. Here, creditors do not conclude the workout agreement because they aim at other creditors and the debtors to pay them in full or above

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503 The option to involve a mediator or supervisor is also recommended in Article 9 of the European Commission's Recommendation (2014).

504 Article 231-242 Insolvency Code.

505 For Belgium it was reported that: "The commercial court establishes a chamber of commercial investigation, composed of standing judges and lay judges (with an economic background: bankers, business men, company directors, etc.), to monitor the financial situation of troubled business entities and request them to appear in court if their difficulties appear to be heading toward corporate insolvency. The chamber of commercial investigation aims at making the management of the undertaking aware of its problems by warning against potential insolvency risks and encouraging to seek proper advice and apply remedial measures." See: Belgian Report in Bob Wessels & Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming).

506 See again the Belgian Report at referring to "a legal obligation for external accountants, auditors, tax advisors, etc. to warn the management for serious and corresponding facts which may affect the debtor's business continuity" under Article 10 BCA since August 2013. See also Jose M. Garrido, *Out-of-Court Debt Restructuring* (World Bank Study 2012), para. 52, on accounting and auditing rules for financial creditors.

507 Company Law governing publicly held companies or limited liability companies frequently provides for an obligation of management to respond to a significant decrease in equity value – see Chapter 25 of the Swedish Companies Act or Sec 92 of the German Aktiengesetz (Act on PLC) or Sec 49(3) German GmbHG (Act on LLC).

508 See the French Conciliation or the Spanish Notice under Article 5bis of their Insolvency Code. See also Article 6 of the Proposal Restructuring Directive (2016).

the workout payoff for the sake of the restructuring.[509] Such creditors, often distressed debt investors that bought into the group for little money, hold the debtor as well as all other creditors with an interest in the success of the restructuring ransom with their hold-out position until someone buys their claims for the nominal value or a substantial profit – a picture often seen in today's bigger restructuring cases.

231. A creditor pursuing such a strategic hold-out would not be convinced by any of the trust building and support measures mentioned above. It requires a different toolset to address this type.

- A first preventive measure would be a ban on debt trading which would deny strategic investors to acquire a claim against a debtor in difficulties for the sole purpose of participating and high jacking workout negotiations. No such ban has been reported in our Inventory Reports. It does not seem to be a preferable option as it would also affect creditors who may suffer regulatory constraints or may require liquidity by denying them to trade their claims.[510]

- A second preventive measure would be a collective action clause in syndicated loan agreements or bond terms which would allow a majority of creditors to bind a minority creditor to a workout solution.[511]

- In some jurisdictions a strategic hold-out creditor, if proven, may not veto a workout under civil law principles (equity; "Treu und Glauben").[512]

- The most common approach reported in our Inventory Reports is to provide for access to courts for the purpose of overcoming a (possible) strategic hold-out. Binding a dissenting creditor to a debt restructuring contract (plan) requires the involvement of a court due to fundamental rights guaranties. While some jurisdictions provide for access to regular (formal) insolvency proceedings (e.g. US; Germany – so called pre-packaged bankruptcy), most European jurisdictions have introduced particular types of court proceedings for the purpose of sanctioning a workout – pre-insolvency procedures (to be discussed under 1.2.2.).

1.2.1.3. Impetus for recommendations

232. To address a difficult economic situation early in a quick and confidential way – meaning out-of-court[513] – has always been seen as the best way to rescue a business.[514]

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509 See also Rodrigo Olivares-Caminal, 'Introduction', in Rodrigo Olivares-Caminal (ed), *Expedited Corporate Debt Restructuring in the EU* (OUP 2015), 1.28.
510 See Jose M. Garrido, *Out-of-Court Debt Restructuring*,(World Bank Study 2012), para. 72.
511 See the German Bond Act (§ 5 SchVG) that allows for bond restructurings supported by a 75% majority if the bond terms contain a collective action clause.
512 The Dutch Civil Code may work this way under very limited circumstances with high thresholds (e.g. abuse of power; section 3:13 of the Dutch Civil Code; DCC; or violation of the general principle of reasonableness and fairness (*redelijkheid en billijkheid*); section 6:2 and 6:248 DCC).
513 These are the advantages of an out-of-court debt restructuring; see Jose M. Garrido, *Out-of-Court Debt Restructuring* (World Bank Study 2012), para. 15.
514 Karsten Schmidt, *Möglichkeiten der Sanierung von Unternehmen durch Maßnahmen im Unternehmens-, Arbeits-, Sozial- und Insolvenzrecht* (Gutachten D zum 54. Deutschen Juristentag. Unternehmens- und

Such an early and confidential approach means that contract and company law tools are to be used to achieve a debt restructuring or a full restructuring of the debtor company's debt and capital structure. In respect to creditors, the renegotiation of the debt maturity or the debt level must aim at a contract that changes or replaces the old debt agreement or claim. In respect to shareholders, amendments to the articles of associations are negotiated under the respective company law regime that may require unanimous decisions or allow for a majority vote. All of such negotiations are "workout" negotiations as they need to achieve a contract with relevant stakeholders.

233. A legislative framework that wants to support workout negotiations must start from the fact that the main factor in such negotiations is to arrive at a point where relevant stakeholders agree to a proposed workout; they cooperate voluntarily. It is, at its core, a psychological matter that wants to be addressed.

Generally, people tend to cooperate if and when they trust in each other as well as in the fact that the agreement will best serve their individual interests. They need to trust in each other as well as in the proposed solution. As a result, successful negotiations depend on:

- trust established between all parties to the negotiations, and
- a period of time available to establish trust and to find a new debt structure that every party can trust in.

234. The generation of trust usually requires a personal relationship. With new players involved, trust needs to be established first – often in the course of negotiations. In addition to trusting each other, all parties also need to believe that the proposed new debt agreement is necessary but also feasible for the debtor's business. Key to this belief is the full disclosure of all relevant business related information and a timeframe to disclose and process these facts.[515] Creditors need to disclose their positions as well. In addition, parties need time to provide and understand new information, to evaluate and question new information, to think and talk about alternative options (exit options[516]), and to accept a solution.

235. The early initiation of a workout negotiations secures a timeframe that would allow the debtor to conduct trust building negotiations with relevant stakeholders without the stress of a quickly deteriorating business situation. Therefore, early warning mechanisms from contract or company law are useful, and, provided they do not cause an unbearable amount of paperwork, efficient. Warning mechanism like those mentioned in the Inventory Reports can be considered best practice.

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insolvenzrechtlicher Teil, München 1982), D 133. For a very recent Brazilian experience, see S Milanese and A. C. Mazzuco, 'Restructuring Solutions in a Scenario of Economic Depression and the Challenge for Everyone involved in These Processes in Brazil', INSOL World 2015, Fourth Quarter, p. 16.

[515] See also Jose M. Garrido, *Out-of-Court Debt Restructuring* (World Bank Study 2012), para. 62: "essential for reaching a consensual agreement".

[516] In this respect, any workout is negotiated 'in the shadow of insolvency law' (Jose M. Garrido, *Out-of-Court Debt Restructuring* (World Bank Study 2012), para. 23, also 67.

236. If a workout was initiated only at a later stage,[517] creditors might be incentivised to quickly act for their individual best interest as soon as they are contacted from a business in need of a debt rearrangement. Here, the collective value of workouts should be protected by (voluntary) standstill agreements that are concluded immediately at the outset of negotiations with all creditors involved, run for a very limited time, and depend on the debtor's progress in the negotiations.[518] A mediator or supervisor could be useful to assist the debtor but also to act as a neutral, trust inspiring figure provided that the extra costs of such an independent person are limited (possibly by a fee cap) and covered.[519] As creditors involved are often repeat players (e.g. banks, tax authorities, suppliers, insurers), soft law could provide a sufficient legal basis for ensuring the conclusion of such agreements ("enhanced workouts"[520]). Here, experience has shown that Codes of Conduct issued by a supervising body (e.g. the Bank of England) have more effect that those issued by self-regulatory bodies.

237. Rational risk aversion should also be addressed by a legal framework that provides a safe harbour for fresh money provided in a restructuring based on a plausible restructuring plan. Creditors or shareholder confronted with the request to invest new money with the debtor's business will only do so if the additional risk of financing a restructuring agreement is balanced by a legal guarantee that in case of a failing business turn-around repayments under the new agreements are safe from avoidance actions and that claims for repayment are secured in subsequent insolvency proceedings (either by enjoying a ranking privilege or a priority security[521]) if they were made in good faith. Such good faith should be presumed for financing agreements that were concluded based on an (ex-ante) feasible restructuring plan. Finally, a favourable tax treatment of losses from such investments that would occur despite of the protection in subsequent proceedings could facilitate the availability of fresh money in workout situations.[522]

238. Still, strategic hold-outs cannot be overcome with the so far mentioned soft – often soft law – instruments. Strategic creditors act in their rational self-interest by not participating in a standstill or later workout agreement. They do not need to establish trust. These types of hold-outs that have become notorious only recently, require an additional, coercive framework that allows for the protection of workout negotiations as well as for a binding workout solution irrespective of the hold-out creditor's position. Such a coercive framework

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[517] Jose M. Garrido, *Out-of-Court Debt Restructuring* (World Bank Study 2012), para. 12-13, suggests that this is always the case in a workout which might only be true for the pathological workouts that end up needing additional help.

[518] Standstill agreements usually provide for a short stay and for milestones that the debtor needs to achieve (e.g. hiring an advisor, providing specific information, proposing a restructuring plan, presenting an investor etc.). Missing a milestone may be considered as a covenant breach and allow creditors to lift the stay. See e.g. INSOL International Workout Principles II (2017); Austrian "Restructuring Guidelines" (2015) ("Grundsätze für Restrukturierungen in Österreich"), principle 1.

[519] See Bob Wessels, 'Mediation in Restructuring and Insolvency', eurofenix 2016, 24, and above at 1.1.2.3. See also the Commission's Report of 26.8.2016 on the application of Directive 2008/52/EC of the European Parliament and of the Council on certain aspects of mediation in civil and commercial matters, COM(2016) 542 final, 5 marking the use of mediation 'underdeveloped' in insolvency proceedings.

[520] See also Jose M. Garrido, *Out-of-Court Debt Restructuring* (World Bank Study 2012), para. 18, 78-92: "enhanced restructurings".

[521] See Jose M. Garrido, *Out-of-Court Debt Restructuring* (World Bank Study 2012), para. 26-29.

[522] See again Jose M. Garrido, *Out-of-Court Debt Restructuring* (World Bank Study 2012), para. 27, 32-39.

must meet constitutional demands and respect fundamental rights of creditors which usually leads to the creditor's right to turn to a court. The action of a court requires a statutory basis which prompted most jurisdictions to introduce a legal framework that is designed to provide the requested tools (for a detailed discussion see the discussion on pre-insolvency procedures below).

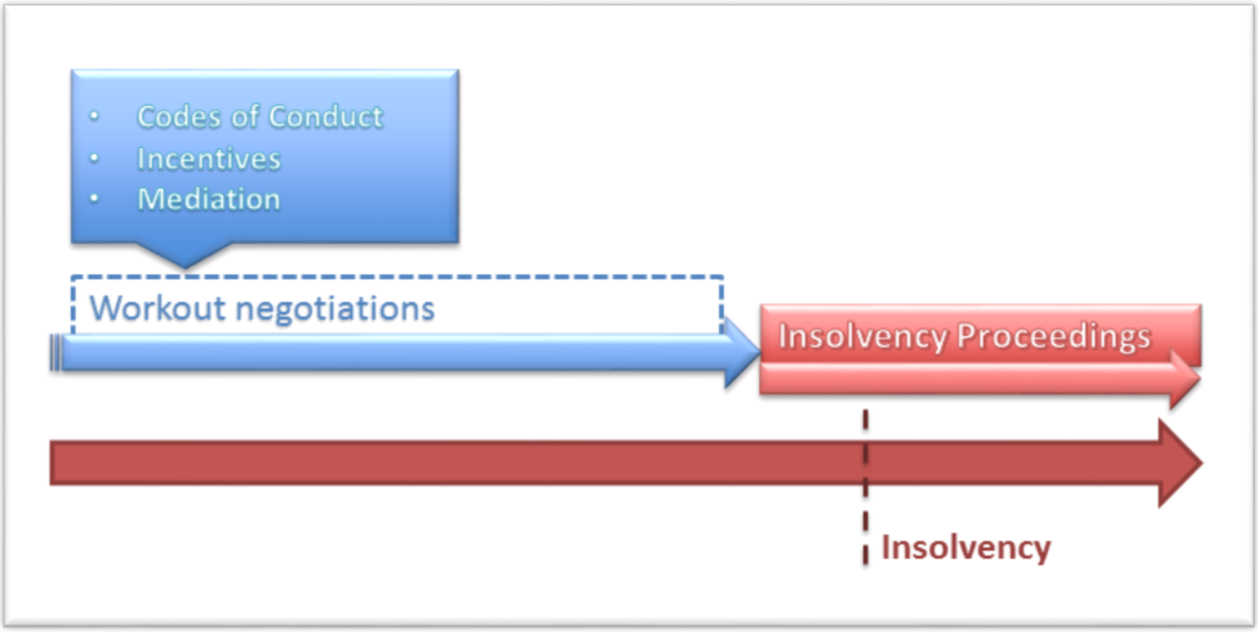

Table 1 – Workout support tools

1.2.1.4. Recommendations

Recommendation 1.21: Member States should provide for and support early warning mechanisms that detect a deteriorating business development and signal the respective urgency to act. Possible instruments are accounting and monitoring duties for the debtor or the debtor's management according to company or tax law as well as reporting duties under loan agreements (covenants). In addition, third parties with relevant information (accountants, tax advisors, possibly also local "prevention groups" of senior businessmen) should be incentivised or even obliged under the law governing their duties to flag any relevant negative development of a debtor's business.

Recommendation 1.22: Soft law instruments like codes of conduct should be used to establish a culture of trust building workout negotiations amongst repeat players (like banks, suppliers, union representatives, insurers etc.). Such codes should follow the example of existing codes and provide for standstill agreements, confidentiality agreements, the way to organise and control a full disclosure (including the flow of information), and for rules how to conduct negotiations (including an option to involve third parties to act as supervisors or mediators). Member States should ensure that the relevant professional bodies are consulted and involved in the creation of such soft law instruments and that they take into account best practices as set out in principles and guidelines developed or adopted by European and international non-governmental organisations active in the area of restructuring and insolvency.

1.2.2 Pre-insolvency procedures

239. Pre-insolvency procedures are judicial proceedings. Their only common features are that they (1) aim solely at rescuing the debtor's business (2) outside of traditional (formal) insolvency proceedings. As such a rescue is usually initiated before the debtors is subject to insolvency proceedings, the term "pre-insolvency" has become the standard attribute to describe such proceedings. It does not necessarily mean, however, that the debtor is not yet insolvent when initiating such proceedings.

240. Our Inventory Reports show a wide variety of such "pre-insolvency proceedings" across the EU, sometimes even in a single jurisdiction (e.g. in France). In general, two types of such proceedings can be distinguished: (1) procedures that facilitate workout negotiations by involving a court, and (2) procedures that allow for a restructuring of the debtor with tools similar to formal insolvency proceedings.

241. Type 1-procedures (workout-supporting proceedings)[523] typically

- do not provide for more tools than the availability of a moratorium and a judge sanctioning a workout agreement that met dissent;
- do not affect all creditors (and shareholders) under the plan but only involved those needed (usually financial creditors like banks and bondholders); and
- do not require a non-insolvency test or any kind of threshold for access.

They may also reduce the court involvement to a minimum (hybrid proceedings).

242. In contrast, type 2-procedures (restructuring proceedings) typically

- provide for a broader range of restructuring tools (e.g. restructuring plan; moratorium; sometimes also facilitated redundancies or rights on executory contracts);
- are collective proceedings as they affect all creditors (and shareholders); and
- require the debtor to show severe financial difficulties to justify access to facilitating restructuring tools.

243. As a result, such of these procedures may resemble restructuring proceedings known from formal insolvency proceedings, in particular, if formal restructuring proceedings also provide for a debtor in possession instead of an appointed insolvency practitioner to administer the estate.

[523] See also Jose M. Garrido, *Out-of-Court Debt Restructuring* (World Bank Study 2012), para. 1, 19: "hybrid proceedings".

244. In addition to these two types of pre-insolvency proceedings, a type 3-procedure is in use to address hold-out in workout negotiations. Here, formal insolvency proceedings are eligible to confirm a pre-packaged or even pre-voted[524] restructuring plan with the full protective force of insolvency proceedings (see the pre-voted bankruptcy option in US Bankruptcy Code s 1126(b)). While pre-packaged or pre-negotiated restructuring plans may become subject of formal insolvency proceedings in many jurisdictions, pre-voted plans are, if at all, (and should only be) confirmed in type 1-pre-insolvency (workout-supporting) procedures because they allow for a minimized court involvement.

Overview of pre-insolvency procedures in jurisdictions of our report

Member State	**Pre-insolvency proceedings**	**Type**	**Court involvement**	**Tools**
AT	URG Proceedings[525]	2	Yes	Plan sanctioning
BE	Formal Amicable Settlement[526]	1	Yes	Moratorium
DE	Bond Term Restructuring[527]	1	Optional[528]	Term sanctioning
EL	Recovery Procedure[529]	2	Yes	Plan sanctioning, moratorium
	Special Administration Procedure[530]	2	Yes	Auctioning off of the debtor’s business as a going concern
ES	Notice (“5bis Notice”)	1	Yes	Moratorium[531]
	Judicial Homolgation	1	Yes	Plan sanctioning
FR	Conciliation[532]	1	Optional[533]	Moratorium, Safe harbour
	Procédure de Sauvegarde[534]	2	Yes	Plan sanctioning; moratorium
	Procédure de Sauvegarde Accélérée[535]	2	Yes	Plan sanctioning; moratorium

[524] While a pre-voted plan has already been negotiated with the number of creditors (and stakeholders) required to meet statutory confirmation rules and received binding support (usually in terms of votes or agreements), a pre-packaged plan has not (yet) received such support or may not have even yet been solicited by debtor. Pre-voted plan are sometimes also referred to as pre-negotiated or pre-arranged plans (see Rodrigo Olivares-Caminal, ‘Introduction’, in Rodrigo Olivares-Caminal (ed), *Expedited Corporate Debt Restructuring in the EU* (OUP 2015) 1.68) which can be misleading because it’s not the negotiation, but the binding votes which makes such plans special.
[525] Reorganisation proceedings under the Business Reorganisation Act (Unternehmensreorganisationsgesetz).
[526] Article 43 BCA.
[527] § 5 SchVG (German Bond Act 2009).
[528] A court would only be involved if one of the affected bondholders files an objection.
[529] Article 99 et seq. Greek Bankruptcy Code (Law No. 3588/2007).
[530] Article 68 et seq. of L. 4307/2014.
[531] The notice opens a three-month period for negotiating either a refinancing agreement (Article 71 (bis) Insolvency Code) or a pre-pack voluntary arrangement proposal.
[532] Article L.611-4 et seq. Code de Commerce.
[533] Court involvement is only required in order to create a safe harbour.
[534] Article L.621-1 et seq. Code de Commerce.

	Procédure de Sauvegarde Financière Accélérée[536]	1	Yes	Plan sanctioning; limited stay
HU	-	--	--	--
IT	Accordi di ristrutturazione[537]	1	Yes	Plan sanctioning
	Concordato Preventivo[538]	2	Yes	Plan sanctioning, moratorium
LV	Out-of-court Legal Protection Proceedings	1	Yes	Plan sanctioning
NL	--	--	--	--
PL[539]	Arrangement Approval Proceedings	1	Yes	Plan sanctioning, restructuring advisor
	Accelerated Arrangement Proceedings	1/2	Yes	Moratorium, Supervisor or IP, plan voting and approval in court
	Arrangement Proceedings	2	Yes	Ibid
	Rehabilitation Proceedings	2	Yes	All tools of insolvency proceedings[540]
SE	--	--	--	--
UK	Scheme of Arrangement[541]	1	Yes	Plan sanctioning
	Company Voluntary Arrangement (CVA)[542]	1	Optional[543]	Plan sanctioning

Table 2 – Pre-insolvency proceedings (type, court involvement, available tools)

Stay (Moratorium)

245. The distinction between type 1- and type 2- pre-insolvency procedures based on their collective effects and tools available does not reflect the collective characteristics of a moratorium. In a “pure” type 1-procedure (workout-supporting proceedings), no collective effect would be present at all. A moratorium is, however, a stay of enforcement action and often also a stay of ipso-facto termination rights that affects all creditors collectively, not only those using those rights or those required for the workout. It would seem logical that type 1-proceedings that function as workout support and only bind those creditors to a plan that are required for a (financial) restructuring would not contain a moratorium or at least

[535] Article L.628-1 et seq. Code de Commerce. These proceedings follow after a failing conciliation attempt.
[536] Article L.628-9 Code de Commerce.
[537] Article 182 Italian Insolvency Code.
[538] Article 160 et seq. Italian Insolvency Code. Such proceedings may be initiated by a ‘concordato in bianco’.
[539] Proceedings under the new “Restructuring Law” that entered into force on Jan. 1, 2016. For a short introduction, see J. Brzeski and P. Wierzbicki, ‘Insolvency and restructuring: Reforms in Poland’, eurofenix Winter 2015/2016, p. 38.
[540] As Rehabilitation Proceedings are available only for insolvent debtors and provide for all tools of Polish insolvency proceedings (like IP appointment, moratorium, facilitated redundancies etc.), it might be better to consider them being a type of formal insolvency proceedings enacted in a pre-insolvency act.
[541] Part 26 of the Companies Act 2006.
[542] Sec. 1 of the Insolvency Act 1986.
[543] A court would only be involved if one of the affected creditors files an objection.

limit the effects of it to the few creditors involved. Most jurisdictions actually follow this line of thought (e.g. UK Scheme of Arrangements or CVA,[544] Polish Arrangement Approval Proceedings, Latvian Out-of-court Legal Protection Proceedings or the Italian accordi di ristrutturazione). Some, however, have provided for a moratorium for the time that the workout negotiations take place (e.g. Spanish 5b notice, the French Conciliation or Belgian Formal Amicable Settlement). Usually, such a moratorium is part or a type 2-procedure that would fully involve the court from the start of negotiations and whose plan often bind all creditors anyway (e.g. Italian concordato preventivo, the Polish Arrangement proceedings, all French sauvegarde procedures, or the Greek Recovery Procedure).

Binding creditors and shareholders

246. Pre-insolvency proceedings of both types usually only affect the claims of creditors. This reflects the fact that workout negotiations are usually initiated by the debtor and in the case of a company by the debtor's management. They do not involve shareholders at this point. Consequently, shareholder rights remain untouched and the do not need to be involved in any supporting procedure. With the development of modern multi-level debt instruments, the distinction of (junior or mezzanine) creditors and shareholders has become a little less clear in some cases which led to the idea of involving shareholder positions in a debt restructuring. Some jurisdictions have already reflected this rather recent trend by allowing the infringement of shareholders rights in type 1- and type 2- pre-insolvency proceedings. As a consequence, shareholders need to be involved in proceedings. The way to involve shareholder rights and the limits of infringements are discussed in Chapter 8.

Binding only some creditors

247. The new form of multi-source and multi-layer financing (through several bonds, syndicated and secured loans and mezzanine instruments) is also the reason for the demand for restructuring tools that only affect financial creditors. Some jurisdictions have made use of flexible procedures to cover the needs of a purely financial restructuring (e.g. the UK and the rediscovery of the Scheme of Arrangement). Others have introduced new procedures for this specific purpose (e.g. France and the Procédure de Sauvegarde Financière Accélérée; Germany updated their Bond Act). Many do not provide for proceedings limited to financial creditors (e.g. Spain or Poland). When considering a specific pre-insolvency procedure for financial creditors, a clear definition of this creditor class is required. Otherwise, one may find quite a diverse number of creditor groups on that side of a debtor's balance sheet. Trade creditors and lessors could also be seen as a "financial creditor" and their contracts could be restructured like loan or bonds terms under these proceedings.

[544] R3 has proposed the introduction of a stand-alone 21 days moratorium in 2016 – see R3, *A Moratorium for Businesses: Improving Business & Job Rescue in the UK* (2016), and on 25 May 2016, the Insolvency Service published a consultation paper which included a 3 month moratorium for all types of insolvency procedures including a CVA which has a collective effect anyway and has featured a moratorium in small business cases since 2000. For a positive response, see I. Fox, R. Anthony, N. Griffiths, W. Gunston and F. Yates, 'A Review of the Corporate Insolvency Framework: A Lawyers' Perspective', ICR 2016, at p. 300.

Supervision

248. Type 2-pre-insolvency procedures are court proceedings. There are initiated by a motion to a court, and the court supervises and safeguards the process of negotiations, organises the casting of votes and confirms an accepted plan. It is a fully supervised process that can be denied on day one if the legislator provides for a test to be passed what usually happens (see the next section.

249. Type 1-procedures, however, only involve a court on a later stage of the process. Such procedures usually leave the negotiating of a restructuring agreement and often also the casting of votes to the parties. Such minimised court involvement saves scarce judicial resources. Still, a one-stop court involvement at the end of the process can provide for a test of grounds to justify proceedings as well as a test of the fairness and legality of the agreement for a dissenting and objecting creditor.

General conditions for the opening of pre-insolvency proceedings

250. Pre-insolvency proceedings aim at supporting the restructuring of a debtor in financial difficulties by facilitating a composition agreement with relevant or all creditors. It is a tool to incentivise the debtor (or the debtor's management) to timely address a financial distress. Consequently, in all jurisdictions that we cover, the right to initiate such proceedings is given to the debtor. In most of them, the debtor owns this right exclusively.

251. As such procedures allow the debtor to infringe (some) creditor's rights, an agreement on the restructuring of debt would usually require a condition in which the debtor has or will soon become unable to pay all debt as they fall due. A test of such circumstances at the outset of pre-insolvency proceedings would therefore seem logical to prevent fraud. Still, only some jurisdictions actually require some sort of (imminent) insolvency test to initialise proceedings – often in order to justify a collective moratorium. Where the court is only asked to approve a workout agreement, such a test is usually not required or, at least, not practiced with respect to the majority of creditors that supported the agreement.

Member State	**Pre-insolvency proceedings**	**Type**	**Access test**	**Right to file**
AT	URG Proceedings[545]	2	"Need to reorganise"	Debtor
BE	Formal amicable settlement[546]	1	---	Debtor
DE	Bond term restructuring	1	---	Debtor
EL	Recovery Procedure	2	(Possible) insolvency	Debtor, creditor
	Special	2	Insolvency	Creditor

[545] Reorganisation proceedings under the Business Reorganisation Act (Unternehmensreorganisationsgesetz).
[546] Article 43 BCA.

	Administration Procedure			
ES	Notice ("5bis Notice")	1	Insolvency but not yet late filing	Debtor
	Judicial Homolgation	1	Sufficiently supported and certified[547] refinancing agreement	Debtor
FR	Conciliation	1	---	Debtor
	Procédure de Sauvegarde	2	"Difficulties", Not yet insolvent (no illiquidity)	Debtor
	Procédure de Sauvegarde accélérée	1 (2)	"Difficulties", Not insolvent for more than 45 days	Debtor
	Procédure de Sauvegarde Financière Accélérée	1	Ibid	Debtor
HU	--	--	--	--
IT	Accordi di ristrutturazione	1	--- (Abuse test)	Debtor
	Concordato preventivo	2	--- (Abuse test)	Debtor
LV	Out-of-court legal protection proceedings	1	Financial problems (not tested)	Debtor
NL	--	--	--	--
PL	Arrangement approval procedure	1	Financial difficulties, Not insolvent Less than 15% disputed claims	Debtor
	Accelerated Arrangement Proceedings	1/2	Ibid	Debtor
	Arrangement Proceedings	2	Ibid, but more than 15% disputed claims	Debtor

[547] Creditors holding at least 51% of the affected claims, and an auditor must testify sufficient creditor support. For more details, see e.g. J.M.M Molina and A.A. Marín, 'Court Approval of Refinancing Agreements in Spain', eurofenix Spring 2016, 35.

	Rehabilitation Proceedings[548]	2	Insolvency test	Debtor and creditor
SE				
UK	Scheme of Arrangement[549]	1	Not specified (court discretion)[550]	Debtor, creditors, administrator
	CVA	1		Debtor, administrator[551]

Table 3 – Pre-insolvency proceedings (type, access test, right to file)

Decision to make use of pre-insolvency proceedings in companies

252. All our Inventory Reports express the clear-cut basic rule that it is a matter of corporate governance to provide for specific approval requirements in the interest of shareholders. If there are no such provisions in the articles of association of the debtor, the directors are not obliged by company law to obtain approval before filing for pre-insolvency proceedings.[552]

253. In the same way, the prior involvement of works councils or employee representatives is not required by law in any of the covered Member States but may be required by the arrangement that the debtor has made with a workers' union.

Publicity rules

254. As a general rule, fair trial principles require the notification of all creditors and stakeholders whose rights are directly affected by the proceedings (e.g. by way of a moratorium) or a proposed restructuring plan.[553] Where pre-insolvency measures do not immediately impair any rights, like the sole act of filing or the appointment of a mediator or a conciliator, notice is usually not required.[554] In case of an impairment, known creditors are being informed by individual notice.[555] In addition, proceedings are usually published in court or insolvency registers,[556] sometimes already accessible via internet;[557] sometimes a special gazette is still being used.[558] Special rules for foreign creditors have not been reported. For publicly held companies, ad-hoc publicity under stock exchange publication

[548] As mentioned above, Rehabilitation Proceedings are available only for insolvent debtors and provide for all tools of Polish insolvency proceedings (like IP appointment, moratorium, facilitated redundancies etc.). They are to be considered as some type of formal insolvency proceedings enacted in a pre-insolvency act.

[549] Part 26 of the Companies Act 2006.

[550] If the scheme does not seem necessary the court may deny to convene meetings – see the England & Wales Inventory Report in Bob Wessels & Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming) .

[551] Only if the CVA is used in conjunction with an administration.

[552] Austrian company law on closely held corporations and partnerships may be the exception to this rule by requiring prior approval in order to safe directors from possible damages claims of shareholders.

[553] See also EBRD Core Principles for an Insolvency Law Regime (2004), Core Principle 2.

[554] See e.g. Belgium or France.

[555] Only a Spanish '5bis Notice' can be kept confidential if the debtor requests the court to maintain confidentiality.

[556] This was for instance reported by Greece, France, Latvia the UK, but not for Austria.EL, FR, LT, UK

[557] See Latvia or UK.

[558] Reported for Greece, Poland and Spain.

rules would usually require to publish relevant information on the firm's financial situation and restructuring measures.

1.2.2.1. Impetus for recommendations

255. If relevant creditors to a consensual debt adjustment reject a proposed workout solution, they might do so in good faith. Maybe they have private information or expert knowledge that indicates to them that the proposed solution will not work. Maybe they are legally obliged to demand payment in full (e.g. tax authorities in some jurisdictions[559]). Here, the contractual need for a consensual solution allows such creditors to veto a workout agreement and there is little doctrinal or economic justification to override their veto.

256. A creditor's veto may also be part of a hold-out strategy that has been adopted by a growing number of distressed debt investors in recent years. Here, the veto does not reflect a negative opinion about the feasibility of the proposed workout solution. The hold-out aims at forcing other creditors to pay or purchase the hold-out position for cash.[560] This strategy cannot be sufficiently addressed by mechanisms of trust building and of positive incentives that were described in Recommendations 1-3. Here, the legal framework must provide an institution that distinguishes a good faith veto from a strategic hold-out and applies coercive tools against the latter type of dissenting creditor. The application of such tools results in the infringement of rights of the dissenting creditors which again requires the involvement of a court to protect the fundamental rights of these creditors under all jurisdictions.

257. The key and robust tool to discipline a strategic hold-out creditor is the power to eliminate the hold-out position by denying their veto right. A legal framework could provide for a substantive contract law rule that invalidates a strategic veto (possibly based on an abuse of power doctrine or equity or 'Treu und Glauben' principles). The weak spot of such an approach would derive from the fact that such a rule would still allow any creditor to deny the applicability of said principle until being proven wrong in a respective law suit. Such a law suit takes time; and time is often exactly what is missing in a restructuring. And even if preliminary injunctions were available (which is not the case in all jurisdictions, e.g. the German[561]), such injunctions are preliminary by nature and uncertainty remains which is also bad for restructurings.

258. Restructurings require a quick and final decision about the validity of a workout agreement. It follows from fundamental rights (protection of property and due process) that a court needs to make that decision eventually. A legal framework should, therefore, provide for the competence of a court to sanction a workout agreement against the veto of a creditor who is not acting in good faith. In addition, hold-out strategies can be foiled from the start by allowing for an all-binding, qualified majority (75-80% of claims) decision about a proposed workout agreement. Where a high percentage of equally affected creditors accept

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[559] See Jose M. Garrido, *Out-of-Court Debt Restructuring*, World Bank Study (2012), para. 71 (footnote 43).

[560] Such strategic behaviour of creditors has also been described as the "anticommons problem" or the "game of chicken"; see Rolef de Weijs, *Too Big to Fail as a Game of Chicken with the State: What Insolvency Law Theory Has to Say About TBTF and Vice Versa*, EBOR 14 (2013), 201, 210/214.

[561] See Stephan Madaus, *Der Insolvenzplan* (Mohr Siebeck 2011), p. 544 et seq.

a workout solution, it can be assumed that a veto from a dissenting creditor is held in bad faith unless good faith is proven to the court.

259. The involvement of the court in supporting workout negotiations against strategic hold-outs can be reduced to a one-stop court involvement where the debtor presents the workout agreement including all supporting facts (disclosure, good faith negotiations, creditors voting to support the agreement with required majority) and the dissenting creditor may explain the objection in a hearing. Such “workout support proceedings” (or type 1-proceedings) are rather common according to our Inventory Reports.[562] As they are only initiated at the end of workout negotiations, it seems only logical to assume that they do not contain a collective stay (moratorium) to protect these negotiations. If, however, a relevant creditor endangers the negotiations by enforcement actions, an individual stay against this very creditor should be available (possibly under the excessive harm doctrine of local enforcement laws). A collective (necessarily public and doctrinal inconsistent) stay (moratorium)[563] would not be required.

260. While in a jurisdiction with a heavily burdened judicial system a one-stop court involvement seems preferable, jurisdictions with a strong tradition of in-court restructuring negotiations (e.g. France, Spain or the UK) may prefer to have a court involved from day one of the negotiations with dissenting creditors. Such type 2-pre-insolvency proceedings are more burdensome to the judicial system. But they allow for the protection of negotiations by an automatic and collective stay (moratorium). Being a collective measure, such a collective tool is only consistent with the scope of the proceedings if they affect all creditors collectively and publicly. Such procedures resemble insolvency proceedings rather than a workout support (see the French Sauvegarde proceedings).[564] In turn, such a (collective) moratorium should not be available if type 2 – proceedings do not affect all creditors but only a certain class or group of them (see e.g. a UK Scheme of Arrangements) because here the only collective affect would be the moratorium itself.[565]

261. Finally, the task of confirming a restructuring plan based on a stipulated majority of creditors and a good faith test could also be assigned to insolvency courts under insolvency proceedings (type 3-procedures).[566] Such an approach maintains a strict duality between out-of-court workouts and court-supported restructuring plans. The disadvantage of such a solution derives from the fact that any confirmation of a non-consensual plan would require the formal commencement of insolvency proceedings with all their negative effects in terms of costs, delays and negative publicity. The disintegrating effect of such proceedings for corporate groups, in particular, does effectively prevent them from considering such an option in a debt restructuring.

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[562] They are also recommended in Article 7 and 8 of the European Commission’s Recommendation (2014).

[563] See Recommendations 6(c), 10-14 Commission’s Recommendation (2014).

[564] Based on their collective effect, such procedures actually qualify to be listed in Annex A of the European Insolvency Regulation (2015) if they also infringe the right of the debtor in possession to administer the estate. A number of type 2 procedures have made that list already.

[565] The proposal of UK R3 reflects this tension by suggesting a standalone-moratorium that can be extended by a subsequent (collective) CVA but not by a (non-collective) Scheme of Arrangement; see R3, *A Moratorium for Businesses: Improving Business & Job Rescue in the UK* (2016), p. 2.

[566] See Chapter 11 “pre-voted bankruptcies” under 11 U.S.C. § 1126(b). German law also only allows for pre-packaged insolvency plans (German Insolvency Code, s 218(1)2).

262. The current debt restructuring market conditions seem to be addressed best by an efficient workout supporting regime outside of formal insolvency proceedings. Such proceedings should only affect the participants of a workout attempt by the debtor and allow the debtor to pursue a dual track strategy when negotiating a workout solution. The key to such a strategy is the argument that as soon as the required creditor majority supports the plan, the remaining creditors would act rational by surrendering because a quick and foreseeable court procedure would bind them anyway. As a result of court procedure being a credible exit option in workout negotiations, hold-out strategies would be abandoned without ever even actually going to court. The most effective procedure would, thus, be a procedure with very limited case numbers.

263. A full scale court procedure with collective effects (at least by way of a moratorium) would not allow for such a strategy as it would usually be more costly and less predictable for the debtor. In practice, such (type 2) proceedings are favoured by debtors that initiate a debt restructuring at a very late stage with their insolvency imminent or present. Such debtors often actually require an automatic stay against all creditors and a strong judicial support for staying alive. In our opinion, such debtors are best treated in efficient and rescue-friendly formal insolvency (reorganisation) proceedings, especially if such procedures also allow for a pre-packaged or even pre-voted plan.[567] The question whether to reorganise, sell or close the debtor's failing business is well addressed there. A framework that provides for both type 2 pre-insolvency and insolvency reorganisation proceedings appears to be excessive and redundant, because there are two procedures to cover the same type of troubled businesses with largely the same set of instruments. The only reason to have both is to avoid the negative publicity of formal insolvency proceedings at all costs. However, such effects may be covered by a well-drafted (and well-named) formal reorganisation procedure with guaranties for the debtor similar to pre-insolvency procedures (debtor in possession, right to file the initial plan etc.).

[567] For the symbiotic effects of such a combination see Jose M. Garrido, *Out-of-Court Debt Restructuring* (World Bank Study 2012), para. 100; see also Stephan Madaus, *Der Insolvenzplan* (Mohr Siebeck 2011), p. 563-564.

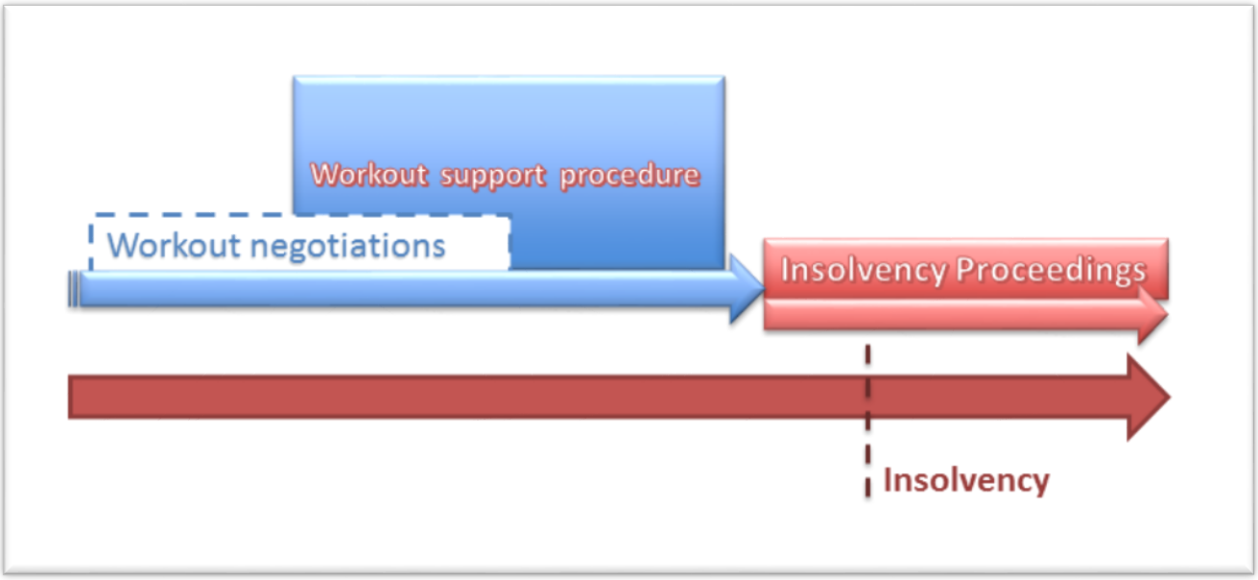

Table 4 - Workout Support Proceedings

1.2.2.2. Recommendations

Recommendation 1.23: Member States should provide for the competence of a court to sanction a workout agreement against the veto of one or more (secured or unsecured) creditors who are not acting in good faith. Where a high percentage (75-80%) of equally affected creditors accept a workout solution, it should be assumed that a veto from a minority of dissenting creditor is held in bad faith unless good faith is proven to the court.

Recommendation 1.24: Such workout support proceedings should not be complemented by an option to apply for a collective stay. Instead, workout negotiations should be safeguarded by an option to apply for an individual stay against the creditor acting detrimental to the workout efforts.

Recommendation 1.25: Such workout support proceedings should only be available for the debtor. They should not require a specific access test referring to the situation of the debtor's business. Instead, the court would only require the debtor to submit a workout agreement with sufficient creditor support according to the stipulated majority requirements.

1.2.3. Formal procedures

264. Formal restructuring and insolvency proceedings comprise all types of procedures that are designated for insolvent debtors. They do not aim at preventing insolvency but at managing the case of an insolvent debtor. Economic analysis would suggest that these procedures address a common pool problem by coordinating the access of all creditors to

the limited and insufficient amount of assets of the debtor for the benefit of all creditors.[568] Such proceedings are court proceedings from day one that affect all creditors collectively and usually require an insolvency test (common pool problem test) to be commenced. Whether such proceedings are bound to achieve the best outcome for creditors only or whether they should also include the interests of other stakeholders (employees, shareholders, local municipalities, macro-economic interests) is open for debate.[569] In principle, formal insolvency proceedings are characterised by their openness for any result, their inclusivity and their legal formality.[570]

265. Such proceedings usually offer rules on how to guarantee that all the debtor's assets are included (by extending to hidden assets abroad and by initiating avoidance actions), how to liquidate these assets, and on how to distribute the proceeds. In a piecemeal liquidation, the debtor's business may be wound up; a liquidation, however, also allows to sell the business as a going-concern and transfer the business to a new owner which effectively may save the business. This option is the main way of rescuing a business in many jurisdictions. Finally, formal insolvency proceedings have always contained a contractual way to overcome the insolvency of a debtor in form of a composition. Here, the debtor proposes a debt adjustment agreement to all creditors which requires the acceptance of a stipulated majority of creditors and a confirmation of the court to become effective. The traditional form of a composition allows the debtor to continue a business with a restructured debt level. It has developed in many jurisdictions into a tool that allows to address a restructuring of the debtor company's ownership, too (restructuring plan with debt-to-equity-swap option).

Overview of formal procedures in jurisdictions of our report

266. Our inventory reports indicate the following formal insolvency procedures with their purposes.

Member State	**Procedure**	**Purpose**	**Priority**
AT	Bankruptcy Proceedings	Liquidation	--
	Reorganisation Proceedings	Reorganisation	--

[568] See Thomas H. Jackson, 'Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain', 91 Yale L.J. 858 (1982); Thomas H. Jackson, *The Logic and Limits of Bankruptcy Law* (Harvard University Press 1986).

[569] The creditor-oriented economic theory of insolvency procedure probably still dominates academic discussions (see Sefa Franken, 'Creditor- and Debtor-Oriented Corporate Bankruptcy Regimes Revisited', EBOR 5 (2004), 645, 649; Federico M. Mucciarelli, 'Not Just Efficiency: Insolvency Law in the EU and Its Political Dimension', EBOR 14 (2013), p. 175, 179; or most recently Horst Eidenmüller, 'Was ist ein Insolvenzverfahren?' ZIP 2016, 145), or Jochem Hummelen, *Distress Dynamics. An Efficiency Assessment of Dutch Bankruptcy Law* (Eleven 2016). The theory also strongly influenced recent legislative acts in insolvency law, see Inventory Reports from Germany, Austria, Greece, the Netherlands, Poland or Sweden. Still, there has always been dissent – see France favouring safeguarding employment over creditor payoff in cases of a business rescue (French Inventory Report at para. 1.1.3.b in Bob Wessels & Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming); see also Roy Goode, *Principles of Corporate Insolvency Law* (4th edn, Sweet & Maxwell 2011), para. 2–16; Rizwaan J. Mokal, *Corporate Insolvency Law*, OUP 2005, 32-60; see also Karen Gross, '*Taking Community Interests Into Account in Bankruptcy: An Essay*', 72 Wash. U. L. Q. 1031 (1994).

[570] See Vanessa Finch, *Corporate Rescue: A Game of Three Halves*, Legal Studies 32 (2012), 302, 304 (for UK administrations).

	Reorganisation Proceedings with DIP	Reorganisation	--
BE	Judicial Reorganisation	Workout Reorganisation Business transfer	--
	Bankruptcy	Liquidation	--[571]
	Voluntary Winding up	Liquidation	--
DE	Insolvenzverfahren	Liquidation Reorganisation	--
EL	Bankruptcy Procedure	Liquidation Reorganisation	--
ES	Concurso	Reorganisation Liquidation	1 2
FR	Redressement Judiciaire	Reorganisation Business transfer	--
	Liquidation Judiciaire	Liquidation	--
HU	Reorganisation Procedure	Reorganisation	--
	Liquidation Procedure	Liquidation	--
IT	Fallimento	Liquidation Reorganisation (concordato)	-- --
LA	Ordinary Legal Protection Procedure	Reorganisation	--
	Insolvency Procedure	Liquidation	--
NE	Suspension of Payments	Reorganisation	--
	Debt Management	Reorganisation	--
	Bankruptcy Procedure	Liquidation	--
Pl	Arrangement Proceedings	Reorganisation	--
	Bankruptcy Proceedings	Liquidation	--
	Pre-pack Bankruptcy Proceedings	Business transfer	--
SE	Company Reorganisation	Reorganisation	--
	Bankruptcy	Liquidation	--
UK	Administration	Rescue	1
		Better distribution	2
		Distribution to a preferred or secured creditor	3
	Liquidation	Liquidation	--
	Administrative Receivership	Debt enforcement	--

Table 5 – Formal insolvency proceedings (purpose)

267. Overall, all jurisdictions that we covered provide for a default liquidation procedure that follows the traditional lines of a bankruptcy liquidation. In addition, all jurisdictions provide for ways to sell and transfer the business as a going-concern, and for a reorganisation option

[571] The bankruptcy court may suspend the decision to open Bankruptcy Proceedings for up to 15 days in order to allow the debtor to submit a request for Judicial Reorganisation Proceedings.

for the debtor based on the consent of a majority of creditors.[572] The latter reorganisation option can be an option in consolidated insolvency proceedings (e.g. Germany) or a separate type of collective procedure available for insolvent debtors (e.g. Hungary, Spain or Sweden). Where such separate (formal reorganisation) procedures are available for near insolvent debtors at their request (often under an imminent illiquidity test), they still differ from type 2 pre-insolvency proceedings insofar as formal reorganisation proceedings are only open, but not designed for not yet insolvent debtors. Indeed, some jurisdictions comprise both types of procedures.[573]

268. A hierarchy of procedural options (liquidation or reorganisation) was only reported for the Spanish Concurso and the UK Administration. Both procedures favour rescue attempts.[574] In addition, some jurisdictions favour a particular type of procedure by facilitating access to it (e.g. Belgium Reorganisation Proceedings, see also Hungary). While reorganisation proceedings are usually only available upon a motion by the debtor, the creditors' right to file for liquidation proceedings is commonly not restricted. Only after a reorganisation procedure has been initiated, it is usually protected against competing attempts to initiate a liquidation-oriented procedure (e.g. France, Greece). But it also works the other way around: e.g. in Belgium, Reorganisation Proceedings cannot be filed after Bankruptcy Proceedings have been opened. In consolidated systems, reorganisation or going-concern options are usually protected until a creditor decision is taken on the future of the business (e.g. Austria, Germany), meaning that the insolvency practitioner is basically obliged to continue a still running business up to that day.

1.2.4. Formal insolvency procedures available for a business rescue

269. It follows from our inventory reports that all procedures mentioned can be used to achieve a business rescue (except for UK Liquidation and Administrative Receivership, and Belgian Voluntary Winding up proceedings). While reorganisation-oriented proceedings will be initiated to restructure the debtor's debts or business, in liquidation-oriented proceedings a sale of the business as a going concern remains a viable option for the benefit of all stakeholders. The difference between both options comes from their specific purpose. In a reorganisation procedure, the rescue of the business is the sole purpose of proceedings while in a liquidation the transfer of the business is merely an option but not the sole purpose which lies in maximising creditors' payoff.

270. The sale of the business or its viable parts is the common way to rescue the business (rather than the legal entity) of the debtor. Some jurisdictions have facilitated such sales by allowing for pre-arranged or pre-packaged sales ("pre-packs"). Here, the formal commencement of insolvency proceedings (e.g. Administration in the UK or Pre-packaged Liquidation Proceedings in Poland) only provides the procedural basis for the transfer of the business free and clear from liabilities. For a detailed discussion see Chapter 7.

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[572] Such a menu of options reflects international standards; see World Bank Principles (2016), Principles B3.6, C1(iii) and (iv); UNCITRAL Legislative Guide (2004), Recommendation 2; EBRD Core Principles for an Insolvency Law Regime (2004), Core Principle 3; Principles of European Insolvency Law (2003), § 1.1.

[573] French law features a pre-insolvency type 2 procedure (Procédure de Sauvegarde) as well as a separate formal reorganisation procedure (Redressement Judiciaire).

[574] Principles of European Insolvency Law (2003), § 12.1 support such a legislation by only allowing for a liquidation if no reorganisation option is available.

General conditions to commence these proceedings

Member State	Procedure	Illiquidity	Over-indebtness	Imminent Illiquidity
AT	Bankruptcy Proceedings	Debtor Creditor	Debtor Creditor	--
	Reorganisation Proceedings	Debtor	Debtor	Debtor
	Reorganisation Proceedings with DIP	Debtor	Debtor	Debtor
BE	Judicial Reorganisation	Debtor (Creditor, Public Prosecutor, Investor)[575]	--	Debtor
	Bankruptcy	Debtor Creditor Public Prosecutor	--	--
DE	Insolvenzverfahren	Debtor Creditor	Debtor Creditor	Debtor
EL	Bankruptcy Procedure	Debtor Creditor Public Prosecutor		Debtor
ES	Concurso	Debtor Creditor	--	Debtor
FR	Redressement Judiciaire	Debtor Creditor State Prosecutor	--	--
	Liquidation Judiciaire	Debtor Creditor State Prosecutor	--	--
HU	Reorganisation Procedure	Debtor	--	Debtor
	Liquidation Procedure	Debtor Creditor	--	--
IT	Fallimento	Debtor Creditor Public Prosecutor	--	--
LA	Ordinary Legal Protection Procedure	Debtor	--	Debtor
	Insolvency Procedure	Debtor Creditor	Debtor Creditor	--

[575] If the debtor is bankrupt, the transfer of the business under Judicial Reorganisation Proceedings can be initiated by any creditor, the Public Prosecutor or a third party interested in bidding for the business.

NE	Suspension of Payments	--	--	Debtor
	Debt Management	--	--	Debtor
	Bankruptcy Procedure	Debtor Creditor Public Prosecutor	--	--
Pl	Arrangement Proceedings	Debtor	Debtor	Debtor
	Bankruptcy Proceedings	Debtor Personal Creditor	Debtor Personal Creditor	--
	Pre-pack Bankruptcy Proceedings	Debtor Personal Creditor	Debtor Personal Creditor	--
SE	Company Reorganisation	Debtor Creditor[576]	--	Debtor Creditor
	Bankruptcy	Debtor Creditor	--	--
UK	Administration	Debtor Creditor Public Authorities[577]	--	Debtor Creditor Public Authorities

Table 6 – Formal insolvency proceedings (insolvency test, right to file)

271. Formal insolvency proceedings are based on the fact that the debtor is insolvent. The definition of insolvency is, therefore, connected to the ground on which insolvency proceedings may be opened.

272. The traditional definition of insolvency is the inability of the debtor to pay liabilities as they fall due.[578] This definition is common to all jurisdictions covered. The inability to pay is proven by a cash flow test that is very similar across all jurisdictions and requires either the cessation of payments or the (not just temporary) inability of the debtor to pay all claims due today.

273. For corporate debtors, we find a second definition of insolvency in jurisdictions influenced by German law[579]: over-indebtedness. Where only a corporate entity is liable for

[576] However, the motion of a creditor is only successful if the debtor agrees to open Reorganisation Proceedings.
[577] The Financial Conduct Authority and the Prudential Regulation Authority are entitled to apply in relation to companies regulated by them according to the Financial Services and Markets Act 2000, s 359.
[578] See UNCITRAL Legislative Guide (2004), Recommendation 15(a); Principles of European Insolvency Law (2003), § 1.2.
[579] Peter Schlosser, 'Die Eröffnung des Insolvenzverfahrens', in Dieter Leipold (ed), *Insolvenzrecht im Umbruch* (1991) 9, 14, called it a 'German Alpine unicum'. The basic concept, however, is common to all insolvency regimes. Still, in many jurisdictions over-indebtness is a ground to prove an imminent inability to pay (see England & Wales or Italy). Only in few it provides a separate ground to commence proceedings (see Germany,

debt, insufficient assets are a legitimate ground to open insolvency proceedings.[580] A balance sheet test is applied to prove the fact of insufficient assets. Assets are usually valued according to their liquidation value. However, even if the valuation shows over-indebtedness, insolvency proceedings may only be opened if the forecast for the continuation of the business is negative (two-step approach).[581] Such an approach obviously contains a lot of room for imprecision as it comprises a valuation of the assets and a projection of the future business success of the company. This could be the reason why, in practice, this test does not seem to bear much relevance.[582]

274. While illiquidity and over-indebtedness justify a motion from individual creditors[583] as well as from the debtor,[584] reorganisation-oriented procedures restrict the right to file to the debtor. At the same time, the ground to open such proceedings is usually expanded by allowing a debtor to file at an earlier stage of the business crisis than the moment of insolvency. Usually, the future but imminent insolvency suffices for a voluntary motion of the debtor. In addition, some jurisdictions require the filing of a plan proposal when filing for reorganisation proceedings (e.g. Austria).

275. While a right to file is often restricted to debtors and their creditors, a number of jurisdictions entitle public authorities to initiate insolvency proceedings as well (e.g. Belgium, France, Greece, Italy, the Netherlands, also UK for regulated companies). This reflects the consideration of a public interest in a timely restructuring or an orderly liquidation.[585]

276. The right to initiate formal insolvency proceedings may also derive from the right to convert another type of (pre-insolvency or insolvency) procedure. These issues are discussed below (see Chapter 1.4.).

Decision to make use of formal proceedings in companies

277. The right to file on behalf of a company debtor is commonly assigned to their director. If there is more than one director, the board of directors decides in accordance with company law and the articles of association. In Spain, shareholders who are liable for the company's debt are also entitled to file.

Austria, Latvia, Poland, but also former Yugoslav countries, Czech Republic, Slovakia, Bulgaria, Estonia and Portugal).

[580] This idea is reflected when an economic analysis results in the statement that "insolvency proceedings should be initiated once whatever value is left in the firm is less than the firm's liabilities to its creditors" (Horst Eidenmüller, 'Comparative Corporate Insolvency Law', Working Paper, 2016, 12).

[581] See Austria and Germany. Under the new Polish Law, the state of over-indebtness must continue at least 24 months. For a comparison, see Felix Steffek, *Gláubigerschutz in der Kapitalgesellschaft, Krize und Insolvenz im englishen und deutschen Gesellschafts- und Insolvenzrecht*, (Mohr Siebeck 2011).

[582] This is especially true in Germany where in 2015 only 275 of 23.123 business insolvency proceedings were commenced based solely on the over-indebtness of the corporate debtor (1,19%); see Statistisches Bundesamt, *Fachserie 2, Reihe 4.1* (12/2015) 20.

[583] The creditor's right to file is often only limited by the abuse of right principle. Only few jurisdictions require additional tests that do not concern the existence of the claim (e.g. Spain).

[584] This reflects international standards – see World Bank Principles (2016), Principle C4.1; UNCITRAL Legislative Guide (2004), Recommendation 14.

[585] In some jurisdictions, public authorities are only allowed to file for liquidation proceedings, but not restructuring proceedings; see for instance Italy.

278. In jurisdictions with an obligation to file, each director is obliged individually and without the requirement of consulting other directors or shareholders (e.g. Austria, Germany, Poland). If no director is present anymore, the majority shareholder (see Austria) or any shareholder (Germany) is obliged to file.

279. In general (with the exception of the Netherlands[586]), a director's motion to file for liquidation proceedings does not require the prior approval of the supervisory board or the shareholder meeting, especially in case of an obligation to file. Shareholder approval is, however, quite common, yet usually not legally required, prior to a voluntary filing for reorganisation proceedings.[587] An unauthorised filing may, however, result in liability of the filing director for losses.

280. The prior approval of works councils is commonly not required under any labour or insolvency law. Still, directors are required to timely inform and consult employee representatives about the filing under European labour law standards[588] (see also Chapter 5.1.).

Protective interim measures

281. Liquidation proceedings and consolidated insolvency proceedings are not opened on the day of the motion.[589] Instead, interim proceedings are commenced that allow the court to investigate the facts described in the motion in order to decide about issues like a creditor's right to file, eligibility of the debtor or the required insolvency tests (see also below at 1.2.4. e). Under some jurisdictions, a motion can be denied if the assets of the debtor do not even cover the costs of the court and the insolvency practitioner (e.g. Germany) or if the case does not meet certain thresholds like a minimum amount of assets and debts (e.g. Italy). Interim proceedings allow for an investigation of such facts.

282. The delay resulting from such interim proceedings must not result in the depreciation of the estate, especially in terms of the termination of the debtor's business. The court is, therefore, entitled to safeguard the estate by ordering safeguarding measures like appointing an interim administrator or ordering a creditor action and/or debtor action moratorium, often combined with the duty of the debtor or administrator to continue the business.[590] The duration of interim proceedings and interim measures does not seem to be

[586] In the Netherlands, Articles 2:136/246 of the Dutch Civil Code provide that, unless otherwise provided in the bylaws, the board of the NV (company limited by shares) or BV (limited liability company) without instructions from the AGM are not entitled to file for opening of bankruptcy liquidation proceedings, see Bob Wessels '*Insolventierecht I* (Deventer: Kluwer 2016), para. 1216 et seq.
[587] Approval is legally required in UK in respect to administration.
[588] Directive 2002/14/EC of 11 March 2002 establishing a general framework for informing and consulting employees in the European Community.
[589] Only Spanish law contains an immediate commencement of insolvency proceedings upon the request of the debtor. A creditor's motion would cause interim proceedings and interim measures.
[590] This reflects international standards – see UNCITRAL Legislative Guide (2004), Recommendation 39, 46, 48; World Bank Principles (2016), Principle C5.1; EBRD Core Principles for an Insolvency Law Regime (2004), Core Principle 4; Principles of European Insolvency Law (2003), § 3.5.

limited by statute, thus giving the court discretion about the timing of a decision about the bankruptcy motion.

283. Restructuring proceedings are voluntary procedures in all jurisdictions and are usually commenced on the day of the debtor's motion (e.g. France, Hungary, Netherlands, Sweden, also UK administration). If not, interim measures are available (see Belgian Judicial Reorganisation or Polish Arrangement Proceedings) or the period is very short by statute (see France: 15 days).

General conditions for the opening formal proceedings

284. The grounds or triggers that allow for the commencement of the respective formal insolvency proceedings were already explained above (see 1.2.4.b). In addition, some jurisdictions require the debtor's assets to cover the costs of the court and the administrator (e.g. Austria, Germany). Some local insolvency laws provide for other thresholds like a minimum amount of assets and debts (e.g. Italy).

285. All jurisdictions require a motion to be supported be documents and information that address all preconditions of the respective proceedings. The court, an impartial state court in all jurisdictions, may convene a hearing to hear interested stakeholders under many insolvency laws (e.g. Belgium, Germany, Latvia, Netherlands, Poland); only few provide for a mandatory hearing (see France, Greece, Sweden for creditor motions, also UK). The court may further investigate ex officio in some jurisdictions (e.g. France, Germany, Greece) while the burden of proof lies with the applicant in others (e.g. Belgium, Hungary, Italy, Netherlands, Poland, Spain, Sweden, UK). If a competing petition for reorganisation proceedings is filed, the decision to open liquidation proceedings may be suspended (see Belgium, Italy).

286. The decision to open insolvency proceedings is subject to an appeal by the affected party[591] which is the debtor only (not their shareholders) in some Member States (e.g. Germany, Netherlands, Spain) while other include everyone affected by these proceedings (e.g. Austria,[592] Belgium; Greece;[593] Italy, Latvia). In contrast, the decision to deny relief may be appealed by the applicant only (being the filing debtor or creditor). On appeal, the decision may be fully reversed. A stay pending appeal is commonly not available;[594] only few jurisdictions provide for an optional stay of liquidation actions where an order to open proceedings is pending appeal (see Belgium, Italy, Sweden).

Exclusion of unviable businesses?

287. In pure liquidation proceedings as well as in consolidated proceedings that combined a default liquidation and an optional reorganisation, the question of the viability of the debtor's business is not a relevant issue at the outset of proceedings. The determination of a

[591] See World Bank Principles (2016), Principle C2.1; UNCITRAL Legislative Guide (2004), Recommendation 138.
[592] In Austria, this includes the Austrian privileged associations for the protection of creditor rights.
[593] In Greece, the decision declaring a debtor bankrupt can be challenged with judicial remedies of appeal and appeal in cassation by anyone who had participated in the proceedings.
[594] Following international standards – see World Bank Principles (2016), Principle C2.1.

going-concern value and the decision about how to realise such a value is assigned to the decision making system that is established in commenced proceedings.

288. As a consequence, an early viability test is only thinkable for procedures that solely aim at the reorganisation of the debtor's business. Still, no Inventory Report refers to a positive test of the business viability on the first day of such proceedings because it seems impossible for a judge to reasonably assess the viability of a business under a proposed plan (see the reported Belgian legislative discussion[595]). Instead, negative tests are reported: In Sweden and the UK, courts must come to the conclusion that the purpose of such proceedings can be achieved which allows to deny to open a reorganisation-oriented procedure if the court is certain that there is no chance for the business to continue. Belgium jurisprudences resort to the abuse of rights doctrine to deny Judicial Reorganisation Proceedings.

Publicity rules

289. The motion to file for insolvency proceedings is usually not published. Instead, notice is given to the debtor in case of a creditor's motion.[596] In case of a hearing, interested parties (debtor, filing creditor, major secured creditor, public prosecutor, workers' representative) may be invited; others are free to appear. In practice, a motion to file often does not remain confidential (especially due to the debtor's duties to inform under contract or capital markets law). If safeguarding interim measures like a stay or the appointment of an interim administrator are ordered, a publication is often mandatory (e.g. in Germany).[597]

300. The court order that opens insolvency proceedings is published in official gazettes as well as registers that are available online.[598] It is entered into the land and company registers. In addition, notice is served to the debtor, known creditors[599] and workers' representatives. Some jurisdictions also require the notification of other stakeholders (e.g. political representatives, the public prosecutor, regulatory authorities).

301. Specific provisions regarding the notification of foreign creditors have not been reported apart from the Swedish Act on Bankruptcies including Assets in another Nordic Country that requires a court to publish relevant bankruptcy decision from another Nordic state in its sec. 2.

595 See the Belgian Inventory Report at para. (1.1.4(f)) in Bob Wessels & Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming).

596 In accordance with World Bank Principles (2016), Principle C4.4; UNCITRAL Legislative Guide (2004), Recommendation 19(a).

597 In accordance with UNCITRAL Legislative Guide (2004), Recommendation 42(a).

598 This reflects international standards – see UNCITRAL Legislative Guide (2004), Recommendation 22-25; World Bank Principles (2016), Principle C2; Principles of European Insolvency Law (2003), § 1.4.

599 See Article 40 EIR and Article 54 EIR Recast providing that as soon as insolvency proceedings are opened in a Member State, the court of that State having jurisdiction or the insolvency practitioner appointed by that court '… shall immediately inform the known creditors'. In practice it will generally be the appointed office holder. The provision is in accordance with UNCITRAL Legislative Guide (2004), Recommendation 24; EBRD Core Principles for an Insolvency Law Regime (2004), Core Principle 2.

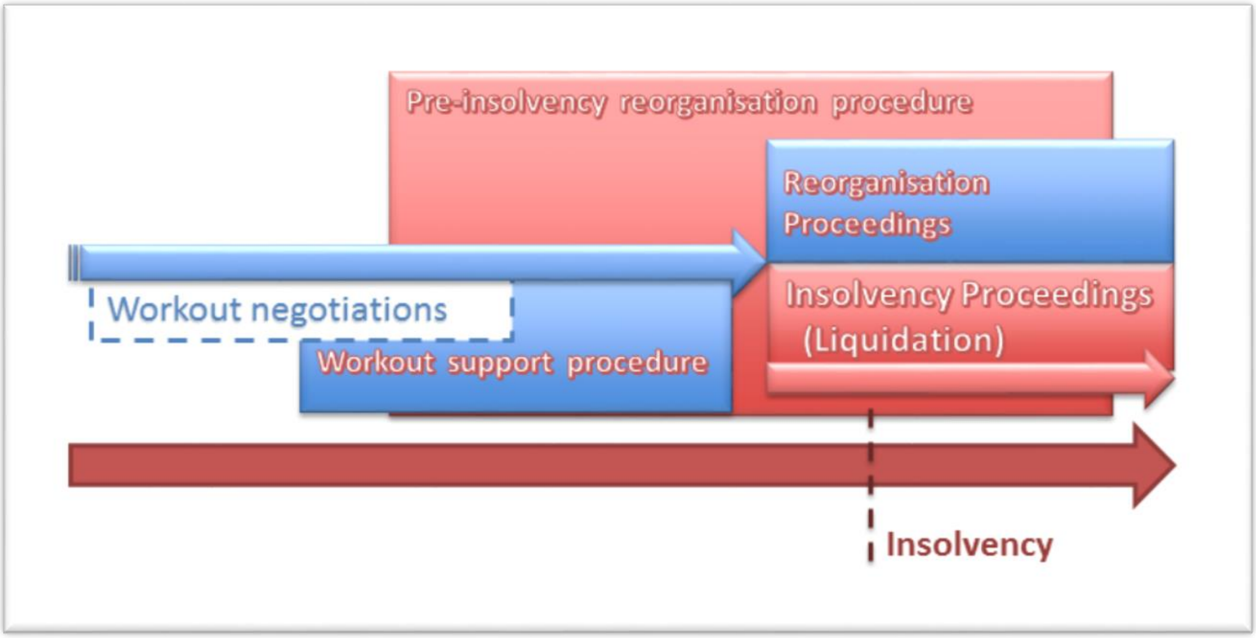

Table 7 – Combination of reported types of insolvency-related proceedings

1.2.4.1. Impetus for recommendations

302. The basis of every insolvency framework is an efficient liquidation regime that provides for a quick and cost efficient way to wind up a failed business and ensures a maximised return for creditors as well as a quick exit of a failed business from the market. Handled by strong and professional institutions (see 1.2. and 1.3.), an efficient insolvency framework is held to attract investments, improve access to credit and lower credit costs.[600]

A strong liquidation procedure, including a flexible transfer option

303. Where the debtors' business is viable, rescuing the business preserves valuable economic structures (including jobs). A business rescue in insolvency also usually increases the return to creditors and may leave value for shareholder investments. It is undisputed that an efficient insolvency framework must include a strong and predictable reorganisation option and countries around the world have introduced such options within the last decades.[601]

304. A business rescue in insolvency is often the result of liquidation proceedings. As such proceedings are conducted to sell all of the debtor's assets, they also allow for a sale of the assets required to continue the debtor's business as a whole (going concern sale). Where such an asset deal allows to purchase the business free and clear of old debt, the new owner may continue the business and, therefore, be willing to pay a good price. This way of rescuing a business has been further developed in some jurisdiction where "pre-pack sales"

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[600] See, for instance, Adalet McGowan, M. and D. Andrews, '*Insolvency Regimes And Productivity Growth: A Framework For Analysis* (OECD Economics Department Working Papers No. 1309, OECD Publishing, Paris 2016) available at http://dx.doi.org/10.1787/5jlv2jqhxgq6-en.
[601] The World Bank Doing Business Report 2016, p. 48.

are either done in practice or have found their way into expressive legislation (see Chapter 7).

305. In order to safeguard a going concern sale option, it is important to continue a debtor's business if it is still running on the filing day. This can be achieved by ensuring the timely filing of liquidation proceedings. As there is little to gain for the debtor (or the debtor's management) in such procedures, the right to file should also be granted to single creditors or relevant public authorities with sufficient knowledge about the financial situation of the debtor (e.g. tax authorities, social security agencies, registrars). Often, these agencies are also creditors and, therefore, allowed to file.

306. The very intrusive nature of liquidation proceedings demands for a close examination of the alleged grounds to open them. This is not only true for motions from creditors (involuntary filings), where the debtor is to be protected from unlawful creditor strategies, but also for motions from the debtor, where the debtor's management may attempt to infringe the position of shareholders or junior creditors.[602] The court should be allowed to hear affected stakeholders and to investigate relevant facts ex officio. As this take some time, interim measures to protect the estate from harmful acts of the debtor or creditors are required. These interim measures must not only comprise the right to appoint an interim administrator and to impose a creditor/debtor action moratorium. They must also ensure the continuation of the debtor's business (e.g. by safeguarding post-petition finance[603]) and, by doing so, the protection of a going concern sale option.

307. The size of the estate or its ability to probably cover the costs of the court and insolvency office holders should not necessarily be a factor in the decision to open judicial liquidation proceedings. Although public authorities should be able to cover their costs, insolvency proceedings have a significant macroeconomic importance in a market society. Practical experience from jurisdictions where proceedings are not opened due to insufficient assets (in particular Germany and the Netherlands) show that such regimes incentivise company directors who act in bad faith when a business fails to dispose of all assets prior a filing in order to escape the scrutiny of a court procedure. Even no asset cases should, therefore, be opened. The costs of such cases should not be borne by all participants but by a pubic fund or insurance scheme. Again, experience (e.g. in Russia) shows that insolvency practitioners who see no chance in earning their fees in a case, tend to spend little effort to their administration.

308. The decision whether (and for which price) to sell the debtor's business is immensely important for all stakeholders. It should, therefore, be assigned to those stakeholders that suffer from bad decision making in the first place – unsecured creditors. The decision directly affects the return that they can expect in a distribution. German insolvency law does reflect this approach by requiring the conclusion of a sale by the administrator to be approved in

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[602] For a discussion of a possible abuse of a voluntary motion in the German *Suhrkamp* case, see Moritz Brinkmann, 'Der strategische Eigenantrag - Missbrauch oder kunstgerechte Handhabung des Insolvenzverfahrens?', ZIP 2014, p. 197.

[603] The importance of post-commencement finance was stressed recently by The World Bank Doing Business Report 2016, p. 99 et seq. In the case of interim proceedings, these consideration also apply to post-petition finance.

advance by a creditor's decision (made by the creditors' committee or, especially in case of an insider deal, by the general creditors' meeting). Other jurisdictions require the approval of the court (see e.g. US, UK). For a detailed discussion of the issue see Chapter 7).

309. Liquidation proceedings see the debtors (as well as their shareholders and their management) side-lined by insolvency practitioners, creditor committees and courts. And still, recent practice has demonstrated that even in such cases a plan solution that binds all stakeholders may be useful. In the major bankruptcies of Lehman Brothers Holdings Inc., General Motors or Chrysler, the liquidation and distribution of (remaining) business parts was governed by a Chapter 11 plan.[604] In Germany, the insolvency plan governing the transfer of viable business parts and the liquidation of non-viable parts of PROKON Regenerative Energien GmbH has successfully provided for a basis to conduct an individual type of liquidation. Overall, business transfer and liquidation plans should both be available tools in liquidation proceedings as they are in reorganisation proceedings.

A restructuring procedure with predictable guarantees for the debtor

310. A liquidation holds nothing to gain for the debtor (except maybe for a later discharge). If the debtor intends to continue the business, the business needs to be saved by a reorganisation. The advantage of a reorganisation option in insolvency comes from the fact that it can be beneficial for all stakeholders. Creditors would have to accept a debt restructuring of some form but could expect to receive a higher payoff than in a liquidation. The debtor (or the debtor's management and shareholders) could retain the restructured business and jobs would be preserved in significant numbers. Overall, a reorganisation would limit the disruptions of an event that prompted the insolvency of the debtor and could, therefore, limit the costs of overcoming this event.

311. The reorganisation of an insolvent debtor's business is, against the background of an efficient going concern sale option in a liquidation, a tool in the primary interest of the debtor. The right to initiate such proceedings should, thus, only be granted to the debtor. Most jurisdictions that provide for separate reorganisation procedures in insolvency are reportedly follow this line of thought. As these proceedings are in the interest of the debtor, who would otherwise face a liquidation, there might be a case to immediately open such proceedings, especially if a reorganisation plan is presented with the motion. However, if such procedures allow for the infringement of shareholder rights (see Chapter 8), third party interest are involved in the opening decision to commence. Where shareholder rights are not sufficiently protected in the course of reorganisation proceedings (see e.g. Germany[605]), a close look at the grounds to open such proceedings might be required. Pre-packaged or even pre-voted[606]reorganisation plans may provide a reason to immediately open proceedings; they should, however, not be mandatory for entering such proceedings.

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[604] See for Chrysler and GM e.g. Barry E. Adler, 'A Reassessment of Bankruptcy Reorganisation After Chrysler and General Motors', 18 ABI L. Rev. 305 (2010).

[605] This issue has been discussed after the experience of the *Suhrkamp* case, see Stephan Madaus, 'Schutzschirme für streitende Gesellschafter? Die Lehren aus dem Suhrkamp-Verfahren für die Auslegung des neuen Insolvenzrechts', ZIP 2014, p. 500.

[606] A pre-voted restructuring plan would not be confirmed in formal restructuring proceedings under the procedural concept recommended here. Workout support proceedings would be available for that specific task.

312. The relationship between a liquidation and a reorganisation option for insolvent debtors should be characterised by the fact that a reorganisation allows for a consensual solution and that it should contain a better result for all stakeholders, including a dissenting one, than a liquidation. The initiation of reorganisation proceedings should, therefore, also be possible in the initial stage of liquidation proceedings and, if filed, precede a liquidation. And a conversion of a reorganisation to a liquidation should only be possible once the reorganisation option has vanished (for a further discussion on termination and conversion see Chapter 1.4).

313. Finally, a reorganisation procedure should cover every business that is (in danger of becoming) insolvent and does not possess the resources and time to pursue a workout strategy (see above under 1.2.2.). In order to incentivise early voluntary filings, such proceedings must offer a predictable and attractive debtor-oriented regime including, in particular, a strict debtor in possession rule (no disruptions of the debtor's ability to run the ordinary course of business), a protected right to file a plan, and an automatic and comprehensive moratorium. At the same time, the court and creditor representatives (committee or supervisor) should be allowed to examine the debtor's actions and initiate the conversion of reorganisation to liquidation proceedings as soon as the debtor's reorganisation strategy fails.[607]

314. A reorganisation procedure can only attract early voluntary filings if the initiation of such proceedings clearly signals to the public, especially to customers, business partners and shareholders, that the debtor is still in control of the situation. Reorganisation procedures should, therefore, be distinctly separated from common insolvency or liquidation proceedings that still carry a stigma in most jurisdictions. The negative experience in consolidated systems, which only offer a reorganisation option as part of commenced insolvency proceedings (e.g. Germany[608]), underline the importance of the publicity effects of not filing for insolvency in case of the initiation of reorganisation proceedings.

315. To be clear, having a separate reorganisation procedure for insolvent debtors with specific guaranties (DIP, plan solution etc.) does not mean that alternative liquidation proceedings cannot or even should not feature a plan (or composition) option if such option turns out to be the best way to handle the debtor's estate for the benefit of its creditors. Liquidation plans (which govern the way to sell the estate or to distribute the proceeds), but also compositions (which allow the debtor to buy the estate based on a payment plan) should be available options against the background of an efficient liquidation procedure.

316. Finally, any insolvency and restructuring framework that features support mechanisms aiming at a business rescue will keep troubled businesses alive which also means that competitors to other businesses remain in the market who would have exited without the frameworks support. Any rescue of a business results in a competitor not yet winning finally the competition for market shares. At a first glance, this effect may cause concerns whether

[607] For a detailed discussion of shortcomings of the reorganisation option under the current German Insolvency Code, see Stephan Madaus, 'Zustand und Perspektiven der Eigenverwaltung in Deutschland', KTS 2015, p. 115.
[608] See Christoph G. Paulus, 'Ein Kaleidoskop aus der Geschichte des Insolvenzrechts', JZ 2009, 148, 149; also Horst Eidenmüller, 'Comparative Corporate Insolvency Law', Working Paper (2016), p. 5.

a sophisticated rescue framework is compatible with competition law principles, in particular whether they constitute a harmful kind of state aid for failing businesses.[609] However, such concerns are not justified. First, setting a legal and procedural framework for business to handle an existential crisis is no state aid because the legislator is not supporting individual companies with direct support.[610] Instead, the legislator is shaping the market by regulations that define the rule and functioning of the market by defining the rights of and instruments available to all market participants. New regulation is no state aid because it simply marks the evolution of the market. Second, keeping viable competitors alive in a market maintains competition by ensuring a larger variety of market participants and, thus, promotes the very aim of competition law for the benefit of consumers in the market. Third, competition law remains highly relevant whenever the restructuring or insolvency framework is applied in a specific case. Here, the purchase of a failing business may be subject to EU or national antitrust laws or US merger guidelines.[611] Or an insolvency practitioner may act contrary to competition law by acquiring goods solely for the purpose of marketing them in a piecemeal liquidation sale.

1.2.4.2. Recommendations

Recommendation 1.26: Any rescue-friendly restructuring and insolvency framework grounds on an efficient liquidation procedure that allows for the sale of the debtor's business as a going-concern free and clear of old debt. The instrument of an insolvency plan should be available to allow for a more flexible liquidation of the estate (e.g. through a liquidation or transfer plan or a composition with the debtor).

Recommendation 1.27: Member States should safeguard the interim continuation of the debtor's business until a decision about whether to sell or to reorganise or to close down is made. It should also provide for interim financing protection.

Recommendation 1.28: An efficient liquidation procedure should be accompanied by a debtor-friendly and predictable reorganisation procedure that is clearly distinct in the public eye from conventional insolvency (liquidation) proceedings.

Recommendation 1.29: In case of a competition between a liquidation (sale) and a restructuring, a restructuring attempt should prevail.

Recommendation 1.30: The combination of a pre-insolvency workout support procedure with a strong restructuring procedure for a (near) insolvent debtor constitutes a sufficient procedural framework for a business rescue, especially when pre-packaged sales and insolvency plans are additional available options in formal insolvency proceedings.

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[609] See Christoph G. Paulus, 'Unternehmensrestrukturierung und Wettbewerb – Das Europäische Recht auf der Suche nach der richtigen Balance', WRP 2016, p. 1070, 1073.

[610] See TFEU Article 107 (1) for a definition of state aid: "any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods", also acknowledged by Christoph G. Paulus, *ibid*, p. 1074.

[611] See Ioannis Kokkoris, 'Competition Law Implications in the EU', in Rodrigo Olivares-Caminal (ed), *Expedited Corporate Debt Restructuring in the EU* (OUP 2015) p. 724-754.

Recommendation 1.31: The grounds to open formal proceedings should be harmonised reflecting the rather similar standard already existing across Member States. Liquidation proceedings should be opened where the debtor is not able to pay its dues as they fall due for a certain period of time (the cessation of payment being a clear indicator). The right to file should be assigned to the debtor and all creditors. Restructuring proceedings should be opened if the debtor files and proves that he is insolvent or insolvency is imminent.

1.2.4.3. Overview of the recommended procedural framework for business rescue

317. All recommendations combined establish a procedural benchmark that comprises a flexible workout support procedure with minimal court involvement and limited tools with a formal restructuring procedure with full court involvement and all tools next to a formal liquidation procedure with full court involvement and a liquidation focus.[612] It can be summarised like this:

Scenario 1 – Workout, and Workout Support Procedure:

- Situation: The debtor is not yet insolvent and responds early to a deteriorating business situation or difficulties in refinancing efforts
- Tools: Negotiations supported by Codes of Conduct, optionally a mediator and individual stay of harmful enforcement actions of individual creditors; dual track negotiations towards a consensual workout agreement with exit option "workout support procedure"
- Court involvement: Minimal, if at all
- Publicity: Minimal (due to transparency requirement in court proceedings), if at all

Scenario 2 – (Formal) Reorganisation Procedure:

- Situation: The debtor is not yet insolvent or already insolvent with a still running business, and responds late and with very limited funds to a deteriorating business situation or difficulties in refinancing efforts
- Tools: automatic stay; debtor in possession with (non-intrusive) supervisor; court proceedings aiming at a restructuring plan; financing support for post-petition- and post-commencement finance
- Court involvement: Full
- Publicity: Full

[612] Such kind of a framework is also recommended by the OECD, see Adalet McGowan, M. and D. Andrews, *Insolvency Regimes And Productivity Growth: A Framework For Analysis*, (OECD Economics Department Working Papers No. 1309, OECD Publishing, Paris 2016) p. 15-16. available at http://dx.doi.org/10.1787/5jlv2jqhxgq6-en.

Scenario 3 – (Formal) Liquidation Procedure:

- Situation: The debtor is insolvent with a still running business, and responds late and with very limited funds to a deteriorating business situation or difficulties in refinancing efforts
- Tools: automatic stay; administrator; court proceedings aiming at an efficient liquidation of the debtor's assets including a possible going-concern-sale; financing support for post-petition- and post-commencement finance; insolvency plan available for deviations from statutory liquidation rules in the common interest of creditors
- Court involvement: Full
- Publicity: Full

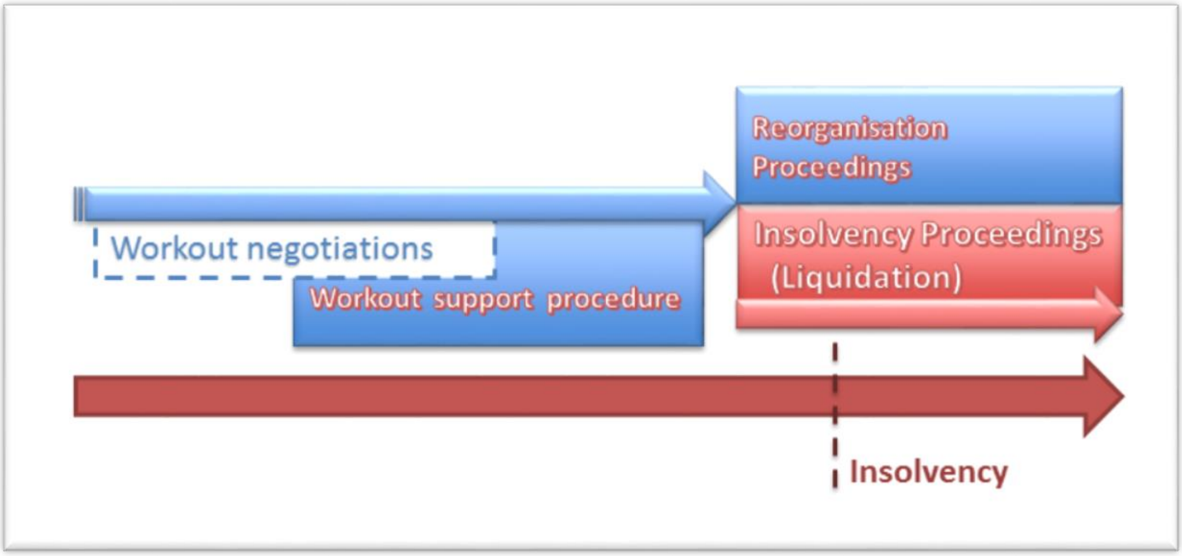

Table 8 – Recommended Combination of insolvency-related proceedings

1.3. Termination and conversion of proceedings

1.3.1. Termination of proceedings

318. All restructuring or insolvency proceedings end as soon as they are successfully completed. A final confirmation order on a restructuring plan ends restructuring or allows unified insolvency proceedings to come to a close.[613] Where, however, the debtor's business is sold as a going concern in the course of a liquidation, procedures may still take a while in order to distribute the sale proceeds and, possibly, to liquidate other assets or to pursue damages or fraudulent transfer claims.

319. Unsuccessful rescue attempts end procedures only if such procedures aim solely at a business rescue. Therefore, restructuring (only) proceedings are usually terminated as soon as the restructuring initiative is failing or abandoned. In jurisdictions with a unified insolvency procedure, which is a procedure that comprises a liquidation and a restructuring (plan) option (see e.g. Germany or Austria), a failing restructuring initiative of the debtor will not prompt the termination of proceedings, but instead initiate efforts to liquidate the debtor's assets (either as a going concern or in piece meal liquidation), often conditioned that there are sufficient assets left to cover the costs of liquidation proceedings (see the Netherlands, Germany, Greece or Austria).

320. A restructuring initiative may fail at different stages in the process, depending on the procedural requirements in each jurisdiction. In general, a proposed plan fails

- at any stage at the request of the debtor; some jurisdictions also allow for an official to request the termination;
- at the voting stage if there are not enough votes cast in favour of the plan;
- at the subsequent confirmation stage if the court finds a reason to deny confirmation; or
- at the appeal stage if a plan is successfully challenged on appeals.

321. In addition, restructuring proceedings may end on grounds of fraud and of inactivity. Here, the court who terminates (and sometimes converts) proceedings acts in order to prevent the abusive use of debtor-friendly restructuring proceedings.

322. Debtors who deal dishonestly with their creditors do not deserve the support of a restructuring procedure which is intended to assist debtors in solving financial problems with creditors. Such assistance is only justified if the result (a restructured debtor with a viable business) is in the common interest of all parties and the debtor is fully cooperating for the common aim. Debtors who acted fraudulently before commencing proceedings as well as debtors who – during proceedings – withhold information, agree on secret side deals, or give false accounts do not only lose the trust of their counterparty which is fundamental for a restructuring (see Chapter 1.1). They also destroy the very basis of any debtor-friendly restructuring procedure. As a consequence, such proceedings are usually terminated once

[613] See Germany in particular (Insolvency Code s 258).

that debtor's fraud has been established by the court, either ex officio or based on a motion of a creditor or another party (e.g. the public prosecutor in Belgium or the Netherlands).[614]

323. Another type of abusive use is defined by inactivity of the debtor after initiating restructuring proceedings. Here, the debtor seeks to enjoy the fruits of commenced proceedings, in particular a moratorium, without sufficiently working on a plan solution. Jurisdictions respond to this type of abuse by setting strict time limits. Our reports indicate deadlines for presenting a plan[615], casting votes[616], or even confirming a plan[617]. Expiring restructuring proceedings may end automatically (see e.g. Belgium) or, more commonly, are to be terminated or converted by the court (see e.g. Hungary, Latvia).

1.3.2. Conversion

324. In jurisdictions with separate restructuring and liquidation proceedings, the failure of a restructuring attempt in restructuring proceedings may not only result in the termination of such proceedings, but also in the automatic commencement of another type of court procedure which means that one procedure is converted to another – usually liquidation proceedings, sometimes, however, also restructuring proceedings if a jurisdiction provides for more than one type of restructuring proceedings (see e.g. Austria, Belgium or France).

325. While a quick conversion of failed restructuring proceedings to liquidation proceedings is recommended in international standards,[618] our reports show that there are only a few jurisdictions where the court supervising a restructuring procedure is actually allowed to not only terminate, but also convert failed restructuring proceedings ex officio into liquidation proceedings (see Latvia, also Austria for a restructuring in insolvency proceedings).[619] Usually, a conversion requires the request of a person eligible to file for the new type of procedure (the debtor, a creditor, or the public prosecutor, see e.g. France, Greece, Italy or Sweden). In addition, the court may be required to conduct an insolvency test before converting proceedings (see e.g. the conversion of Greek recovery proceedings); the simple fact of a failed restructuring does sufficiently justify the commencement of liquidation

[614] In Italy, the court may revoke any confirmed restructuring agreement if the commissario giudiziale (supervising the debtor) reports that the debtor possesses concealed or hidden assets, intentionally failed to report one or more claims, asserted the existence of non-existent assets or committed other acts of fraud, see Article 173 Insolvency Act.

[615] See the Austrian Restructuring Code (URG): 60 days, 30 days extension; French sauvegarde and restructuring proceedings: 6 month, 6 month extension (twice); French accelerated sauvegarde proceedings: 3 month, 1 month extension (twice); Greece restructuring procedure in bankruptcy proceedings: 3 month, 1 month extension; Hungarian proceedings: 120 days, 120 days extension (prolongable by creditor vote up to a year in total); Italian proceedings: 60 days, 120 days extension; Spanish 5bis notice: 3 month moratorium.

[616] See Austrian restructuring proceedings in insolvency: 60-90 days; Latvian restructuring proceedings: 2 months, 1 month' extension with creditor approval.

[617] See Belgian restructuring proceedings: 6 months, 6 months extension (twice); UK administration: 12 month (prolongable with court order or for 6 months with creditor approval); French conciliation: 5 months; Latvian restructuring proceedings: 2 years, 2 years extension with creditor approval; Swedish restructuring option: 3 months, 3 months extension.

[618] UNCITRAL Legislative Guide (2004), Recommendation 158; World Bank Principles (2016), Principle C1 (iv) and C14.3.

[619] Also in the Netherlands, Article 272(4) Netherlands Bankruptcy Act.

proceedings here. Some jurisdictions do not even provide for any kind of conversion (see Spain or Poland).

1.3.3. Reopening of proceedings

326. The matter of reopening proceedings is relevant in three very different scenarios.

327. First, once failed restructuring proceedings which were converted to insolvency proceedings could be reopened again if the debtor is allowed to request it in order to propose a new plan (see Austria, also Germany).

328. Second, restructuring proceedings which had ended successfully with the confirmation of a plan could be reopened if the provisions of the plan prove to be infeasible. Such failing plans cannot simply be modified in reopened proceedings in most jurisdictions (France seems to be the only exception). Hence, the only way to alter outdated plan provisions is to start from square one and file for another round of restructuring proceedings.[620] Such a request does prompt new procedures with (possibly) a new judge and a different insolvency practitioner.

329. Third and finally, liquidation proceedings may be reopened if new assets appear (often money from successful litigation) after the original liquidation proceedings had already ended. Here, only a few jurisdictions allow for liquidation proceedings to be fully reopened (e.g. France or Spain). More often, lawmakers have provided for a simplified distribution by the former insolvency practitioner under the supervision of the former court (see e.g. Austria, Hungary, Sweden or the Netherlands). Following an alternative approach, some jurisdictions have ordered a distribution out of court (Belgium and Poland) or simply to allocate such assets to the state (UK). If the liquidated debtor was a company that had already been deleted in the company register, the company would usually (except for England & Wales) not revive for the course of the additional distribution. Investments in liquidated and deleted companies are, therefore, commonly not a viable strategy to take over a corporate shell (e.g. for tax reasons).

1.3.4. Impetus for recommendations

330. Effective means to end a restructuring attempt as well as a liquidation are vital for any efficient framework. They prevent a delay of proceedings that would only produce costs, but no solution to the debtor's or creditors' problems. Termination and conversion tools, thus, prevent an abuse of proceedings by those stakeholders who take advantage of extended, but useless procedure (e.g. a non-viable debtor or professionals with a fee interest). They are more needed where the risk of abuse is either higher or where there is little protection by other means.

[620] In the US, such new rounds of plan proceedings are commonly called "chapter 22" or "chapter 33" proceedings; see e.g. Harvey R. Miller and Shai Y. Waisman, 'Is Chapter 11 Bankrupt?', 47 B.C.L. Rev. 129, 156-157 (2005).

Pre-insolvency proceedings

331. Looking at pre-insolvency proceedings, type 1-procedures (workout-supporting proceedings; see chapter 1.1.2) offer little room for abuse by stakeholders. They are based on a plan that was proposed by the debtor and accepted by a majority of the creditors which proves that the debtor does not use the procedure to escape creditors. A quick court involvement in the final stage of the workout does also give little room for a significant delay as long as an appeal does not automatically stay the implementation of a confirmed plan. A chance for delay and abuse would only be possible in such procedures if lawmakers were to allow for a stay or moratorium against some or even all creditors before a plan was accepted by a significant majority of creditors (which we do not recommend; see recommendation 2.06). Such a stay should only be available for the very short time that the debtors proves to be required to conclude already advanced restructuring negotiations.[621]

332. The chance of an abusive use by debtors is more relevant in type 2-procedures (pre-insolvency restructuring proceedings; see chapter 1.1.2). A debtor may enter such proceedings without a clear rescue strategy driven only by the urgent need for a moratorium. If lawmakers decide to introduce such a procedure (against our recommendation; see recommendation 1.30), they should define clear and short periods for the debtor to reach milestones, e.g. to present a plan, have a plan accepted in a creditors' meeting and have a plan confirmed by court. Our reports indicate that an initial period of three months, which can be extended by a court order if useful, is short, but adequate. Pre-insolvency proceedings must end when they expire. They should, however not be converted into liquidation procedures because it remains to be demonstrated that the debtor is actually insolvent after proceedings have failed.

Restructuring proceedings

333. The availability of a stay is also characteristic of reorganisation proceedings that we recommend for (near) insolvent debtors. The resulting incentive for abuse by debtors should also prompt lawmakers to define short and clear periods for procedural milestones (see above). Upon the expiration of such periods, court should be competent to not only terminate proceedings, but to automatically convert restructuring to insolvency proceedings. Here, the (imminent) insolvency of the debtor has already been established (or must be established ad hoc) and no further time should be wasted before an insolvency practitioner takes over the business, especially if this still leaves the option of a business rescue in terms of a going-concern sale or an insolvency plan restructuring.

Liquidation proceedings

334. Liquidation proceedings should allow the appointed insolvency practitioner to investigate the business and its rescue options. All options should still be on the table, including a going-concern sale and an insolvency plan solution designed by the insolvency practitioner or even the debtor. Even though, with a realistic view, most insolvencies will probably see a piecemeal liquidation, all stakeholder should still have the option to achieve a

[621] See e.g. the perquisites for a pre-insolvency stay in chapter XV of the Nordic-Baltic Recommendations on Insolvency Law.

different outcome by initiating a sale of the business or the development of a plan solution. At this point, creditors (or economically competent judges) should decide whether to postpose a quick piecemeal liquidation for the sake of auctioning the business as a going-concern or of a meeting to deliberate and vote on a plan. If the latter solutions fail, a piecemeal liquidation would quickly and automatically follow. Such an interchangeability of solutions controlled by the creditors before the background of a quick piecemeal liquidation has proven to be an efficient framework for insolvent companies of all sizes in Germany.

1.3.5. Recommendations

Recommendation 1.32: Member States should define clear and short periods for the debtor to reach milestones in procedures that make a stay or moratorium available for the debtor before creditors have voted to support the plan.

Recommendation 1.33: Member States should authorise courts to convert restructuring proceedings into insolvency proceedings (with a liquidation bias) only if the (imminent) insolvency of the debtor has already been established.

Recommendation 1.34: Member States should provide for common insolvency proceedings that allow for a quick and efficient piecemeal liquidation, but also a quick going-concern sale of the debtor’s business or a different type of solution, even a restructuring, based on an insolvency plan adopted by the creditors and confirmed by the court.

CHAPTER 2:
Financing a rescue

335. With the start of a workout, workout support proceedings or formal insolvency proceedings, a business enters a new phase in its business life cycle, resulting in a restructured business or, when restructuring fails, the liquidation of its assets. This phase will also give rise to new costs, including fees for the involvement of advisors (legal, financial, turnaround) and, perhaps, a court and an IP. Furthermore, cash restraints must be overcome in order to secure the continuation of the business for the duration of proceedings (interim finance), but also in order to implement succesful restructuring measures following the conclusion of proceedings (new finance or plan implementation finance). Considering the financial situation of a troubled business, financing needs will usually require lenders, instead of shareholders, to provide for cash to meet these costs. At the same time, a stay of enforcement actions and payment dues may serve as a valuable instrument for securing incoming cash flow as well as limited cash reserves for a rescue effort. In this chapter, we evaluate these cash related instruments.

2.1. New financing (fresh money)

2.1.1. Terminology

336. The terminology that is commonly applied to describe the finance obtained by distressed businesses in order to secure the continuation of a business as as well as restructuring measures is rather diverse. Drawing on international instruments, this includes a wide range of terms such as ‘new financing’, ‘post-commencement finance’, ‘post-insolvency financing’, ‘post-bankruptcy financing’, ‘new priority finance’, ‘new financing’, ‘additional funding’, ‘new money’, ‘fresh money’, and ‘interim finance’.[622] It seems approriate the principally distingish two types of finance.

Interim finance

337. Immediately after entering a restructuring process, in particular after the commencement of public formal proceedings, the company often needs additional funds to meet the cash needs of operating the business in its ordinary course. Supplies must be ordered and paid, salaries and other administrative expenses fall due. Financing agreement that the debtor enters into in the period between the (petition or) commencement of (formal) proceedings and their conclusion or termination are called “post-commencement

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[622] See e.g. American Law Institute, Transnational Insolvency: Cooperation among the NAFTA Countries: Principles of Cooperation among the NAFTA Countries (2000), Procedural Principle 19; INSOL International: Workout Principles II (2017), Commentary to Principle Eight; UNCITRAL Legislative Guide (2004), Part Two (II), Recommendations 63 and 64; EBRD Core Principles for an Insolvency Law Regime (2004), Principle 8; World Bank Principles (2016), Principle C16.2; American Law Institute and International Insolvency Institute, Global Principles for Cooperation in International Insolvency Cases (2012), Principle 31; European Communication and Cooperation Guidelines for Cross-Border Insolvency (2007), Guideline 14.2; Commission’s Recommendation (2014) 6 (e); EU Cross-Border Court-to-Court Cooperation Guidelines (2015), Principle 23; Proposal Restructuring Directive (2016), Articles 2(11) and 2(12), and Nordic-Baltic Insolvency Network, *Nordic-Baltic Recommendation on Insolvency Law*, (Stockholm: Wolters Kluwer 2016), p,.74 at 7.

finance" in US bankruptcy law and the UNCITRAL Legislative Guide.[623] Such funds are obtained in order to continue a business as usual and, by doing so, to preserve the going concern value of the debtor's estate. As these lending agreement are often due to be repaid upon the termination of proceedings, we prefer to refer to them as "interim finance".[624]

New finance

338. Clearly distinct from interim finance is another type of lending in the course of a restructuring that addresses the needs for additional cash in order to implement restructuring measures after a plan has been adopted in successful workouts or proceedings. Where a plan implementation is not financed by raising new equity, loan agreements are foreseen in the financial scheme of a plan which we refer to as "new finance", a term that fits well within both workout and formal frameworks as well the European insolvency and restructuring terminology.[625]

2.1.2. Significant elements from National Inventory Reports

2.1.2.1. New finance

339. The national Inventory Reports show that many jurisdictions recognise the importance of new financing in an attempt to rescue distressed businesses or to maximise the going-concern value by having specific provisions in their law.[626] Commonly, such arrangements are an integral part of the financial scheme of a restructuring plan and governed by respective legal regimes which means that courts approve the restructuring plan based on the acceptance of creditors.[627]

340. A common way to protect the interests of lenders of new finance is by granting them a priority in a possible subsequent insolvency. In many jurisdictions, such priority is available to claims arising from new finance agreements if such a privilege was either explicitely agreed to in the plan or subject to a separate court confirmation.[628] Only few jurisdictions have option to prioritise new finance.[629] If priority is granted, claims from new finance usually rank ahead of unsecured claims. In France, however, a super-priority is reported

[623] See UNCITRAL Legislative Guide (2004), para.94.

[624] Member States may have a specific termination as well; see e.g. Germany: "Massekredit".

[625] See Article 16 of the Proposal Restructuring Directive (2016), distinguishing interim and new finance. Using similar terminology: Jennifer Payne and Janis Sarra, Tripping the Light Fantastic: A comparative analysis of the European Commission's proposals for new and interim financing of insolvent businesses (forthcoming).

[626] Countries that have no specific legal provisions on new finance include England and Wales, Hungary, The Netherlands, and Poland. Other countries introduced specific legal provisions on new finance, including Belgium (Judicial Reorganisation, see e.g. Article 37 BCA), France (see e.g. Article L. 611-11), Greece (see e.g. Article 154 (a) GBC), Latvia (see e.g. Paragraph 40, section 5 of Latvian Insolvency law), Spain (see e.g. Article 84 (11) LC), and Sweden (see e.g. Section 10 of the Swedish Rights of Priority Act (1970:979) (*Sw*. Förmånsrättslag).

[627] This is the case, among others, in Austria, Belgium, Germany, Greece, Spain, France, Hungary, Italy, The Netherlands, Poland and Sweden. See paragraphs 8.5.1 and 8.5.2 for the process and criteria for reviewing and confirmation of new finance.

[628] See Austria, Belgium, Germany, Greece, France, Italy, Latvia, The Netherlands and Sweden.

[629] See for instance England & Wales for Out-of-Court-Workouts, Scheme of Arrangements, Company Voluntary Arrangements, but also Hungary and Poland.

meaning that claims deriving from confirmed new finance arrangements in a procédure de sauvegarde or a redressement judiciaire even rank above other secured and unsecured creditors.

Safe harbours for new finance from avoidance actions are available in several jurisdictions (Austria, Greece, France and Italy). Again, some jurisdictions do not provide for specific protection against claw back actions, as is the case in Poland and England & Wales.

2.1.2.2. Interim finance

341. Interim finance is only required to raise cash for the purpose of conducting a proceeding in which a best possible outcome must be secured. Financing a running business for a limited period of time in order to enable a decision about a rescue plan or a going concern sale is by its nature an educated guess on the feasability of such a solution. If such a solution later proves to be impossible, the business is shut down anyway, but the additional costs of interim finance are to be borne by all unsecured creditors as the interim lender gets paid first. Hence, any decision to accept interim finance is a decision about causing additional administrative expenses for the estate. As such it is relevant for the payoff to all unsecured creditors. Any legal regime must, therefore, safeguard their legitimate interests in influencing that borrowing decision. The involvement of an insolvency practitioner or/and the approval by a court are possible options to safeguard their interests.

342. In formal insolvency proceedings, the insolvency practitioner will usually conclude interim finance.[630] In case of debtor-in-possession proceedings, the approval of a supervising insolvency practitioner may be mandatory: For instance in Austrian Reorganisation Proceedings with Self-Administration, the debtor may negotiate interim finance, but will need approval from the supervisor. In other jurisidictions, the approval by an insolvency practitioner for entering into interim financing arrangements is not mandatory, but only such an approval would provide lenders with special protection or priority for the repayment claims. For instance in Sweden, claims arising from agreements concluded during the company reorganisation enjoy a general priority only where these agreements were approved by the insolvency practitioner.[631] In jurisdictions with no specific provisions on interim financing (e.g. Hungary or England & Wales), the role of the insolvency practitioner is not defined.

343. Other jurisdictions may require the approval of a court and not of an insolvency practitioner (see Italy[632]). In addition, some jurisdictions require the approval from the debtor himself or the creditor's committee. In Austria (URG Proceedings), for instance, the insolvency practitioner is required to obtain a statement from the creditors' committee on proposed interim finance.[633] In Germany, the creditors' committee is also required to approve relevant interim financing.[634]

[630] See, for instance, in Austria, Belgium, Germanu, The Netherlands.
[631] Section 10 of the Swedish Rights of Priority Act (1970:979) (*Sw*. Förmånsrättslag).
[632] Article 182quinquies Italian Insolvency Act.
[633] Austrian Insolvency Law, § 114.
[634] § 160 (2) Nr. 2 InsO.

344. Commonly, claims from interim finance enjoy the priority of administrative expenses, which means they usually rank ahead of pre-commencement creditors, but not affect the rights of secured creditors.[635] In Belgium, however, interim finance may rank ahead of secured creditors. While, in principle, interim finance is ranked as an administrative expense, interim finance extended in the Judicial Reorganisation Proceeding and confirmed by the Belgian court can have priority over secured creditors when and to the extent that secured creditors have benefited from such finance themselves.[636]

2.1.3. Significant international tendencies

Interim (post-commencement) finance

345. A leading instrument on extending interim finance is the UNCITRAL Legislative Guide on Insolvency Law, Part I and II (2004) (UNCITRAL Legislative Guide).[637] Such finance is promoted, in particular at an early stage, to facilitate the continuity of a business with respect to both reorganisation and liquidation proceedings.[638] Also, the UNCITRAL Legislative Guide recommends that any insolvency law considers to 'recognize the need for such post-commencement finance, provide authorization for it and create priority or security for repayment of the lender.'[639] The UNCITRAL Legislative Guide has formulated this more specifically in particular in the following recommendations:

> '63. The insolvency law should facilitate and provide incentives for post-commencement finance to be obtained by the insolvency representative where the insolvency representative determines it to be necessary for the continued operation or survival of the business of the debtor or the preservation or enhancement of the value of the estate. The insolvency law may require the court to authorize or creditors to consent to the provision of post-commencement finance.
> 64. The insolvency law should establish the priority that may be accorded to post-commencement finance, ensuring at least the payment of the post-commencement finance provider ahead of ordinary unsecured creditors, including those unsecured creditors with administrative priority.
> 65. The insolvency law should enable a security interest to be granted for repayment of post-commencement finance, including a security interest on an unencumbered asset, including an after-acquired asset, or a junior or lower priority security interest on an already encumbered asset of the estate.'[640]

346. To secure the lender of receiving repayment, priority should be provided for post-commencement finance or, how it is called here, interim finance, resulting (at least) in a priority ahead of unsecured creditors (which is often referred to as administrative priority) and, where preferred, also a security interest on unencumbered or on encumbered assets.[641] The extension of security over encumbered assets with a more senior ranking will

[635] See, for instance, in Austria, Belgium, Germany, Italy, Latvia, The Netherlands, Sweden, UK.
[636] Article 37 Belgian Business Continuation Act.
[637] UNCITRAL Legislative Guide (2004), Part Two (II), at 94-107
[638] Idem, at 95.
[639] Idem, at 97.
[640] Idem, Recommendations 63-65.
[641] Idem, Recommendations 64 and 65. The provision of priority for new finance is recommended by most international instruments, including EBRD, Core Principles for an Insolvency Law Regime (2004), Principle 8;

require mostly consent of the (current) security holders and/or court confirmation.[642] Where reorganization proceedings are converted to liquidation proceedings, the priority for post-commencement finance should be recognized.[643]

347. Several other international instruments also suggest that court confirmation is required in obtaining interim finance, at least where new financing is provided outside the ordinary course of business.[644] If court approval is not required, insolvency practioners may still be personally liable for the repayment of such loans.[645]

348. With regard to priority, the approach under the US Bankruptcy Code is comparable to the recommendations of the UNCITRAL Legislative Guide. From Section 364 of the US Bankruptcy Code it follows that post-commencement finance (extended in the ordinary course of business) will be granted automatic administrative priority, ranking ahead of pre-existing unsecured creditors. However, obtaining unsecured finance incured outside the ordinary course of business, will also be granted administrative priority after confirmation by court. Priority over existing secured creditors is possible under certain specific conditions, including: (i) court confirmation of (ii) credit that otherwise could not be obtained, and (iii) adequate protection being granted for pre-commencement secured creditors. The American Bankruptcy Institute Commission (ABI Commission)to study the reform of Chapter 11 US Bankruptcy Code (ABI Report) also recognised that these latter two restrictions have, in practice, proven a bottlekneck.[646] Still, the presence of post-commencement finance increases the chances of a distressed business to opt for reorganisation in stead of liquidation. The ABI Commission considered that any provisions on post-commencement finance should therefore be '… permitting parties to negotiate market agreements that do not overreach or negatively impact the rights of other stakeholders beyond the terms necessary to obtain postpetition credit in a particular case.'[647] In this regard the ABI Commission recognised, in particular, the risks of abusing such finance, especially with respect to roll-up provisions and cross-collateralization provisions. For example, where under such provisions finance is obtained from pre-commencement creditors which provides them with additional protection on their pre-commencement claims.[648]

349. For members of a (multinational) enterprise group, interim finance will be of equal importance as it is to any ordinary businesses in distress. In addition to the common sources available to obtain new finance for distressed businesses, in a group context, such finance may be obtained also from a group member. World Bank Principles hold that intra-group

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World Bank Principles (2016), Principle C9.2; UNCITRAL Legislative Guide (2010), Recommendation 215, and EU Cross-Border Court-to-Court Cooperation Guidelines (2015), Principle 23.

[642] Idem, Recommendations 66 and 67.

[643] Idem, Recommendation 68.

[644]Commission's Recommendation (2014) 6(e) and 28; ABI Report (2014), para. IV.B.2.

[645] See also UNCITRAL Legislative Guide (2004), para. 101, or the German insolvency law (Insolvency Code s. 61).

[646] ABI Report (2014), para. IV.B.2. See also Bob Wessels and Rolef J. de Weijs (eds.), *International Contributions to the Reform of Chapter 11 U.S. Bankruptcy Code* (European and International Insolvency Law Studies 2, Den Haag: Eleven International Publishing 2015).

[647] ABI Report (2014), para. IV.B.2.

[648] ABI Report (2014), para. IV.B.2. See also Bob Wessels and Rolef J. de Weijs (eds.), *International Contributions to the Reform of Chapter 11 U.S. Bankruptcy Code* (European and International Insolvency Law Studies 2, Den Haag: Eleven International Publishing 2015), Part A.

finance arrangements should be available, and should, where necessary, find support of both involved courts and insolvency practitioners.[649]

350. For Europe, the European Commission not only favours a safe harbour for new and interim finance supporting a restructuring from avoidance actions and liability, but also supports a priority for new finance in case of a subsequent insolvency.[650]

New (plan) finance

351. Specific recommendations with regard to financing arrangements for restructuring measures implemented after the conclusion of a plan have not yet been issued.

2.1.4. Impetus for recommendations on interim and new finance

352. From the national and international tendencies, it is obvious that providing fresh money plays an important role in any attempt to rescue a distressed business. In many cases a financially fatigue company is in high need of interim finance to provide the necessary working capital for short term continuation of the ordinary course of business, while a restructuring plan and new finance for implementing its measures is being negotiated and concluded. Most jurisdictions do not specifically distinguish these two forms of financing, though the legal framework for concluding interim and new finance does always differ signifcantly. While new finance and a possible protection of repayment claims (priority) is commonly approved within a restructuring plan and, thus, in most jurisdictions approved by creditors and confirmed by a court (see Chapter 8), interim finance is provided in anticipation of such a restructuring plan, often concluded by the administrator of the estate (insolvency practitioner or debtor in possession) – thus enjoying the privilege of an administrative expense – and sometimes subject to additional approval by the court, the creditors' committee or – in case of a DIP – the supervisor.

353. Since the background and aim of the two types of funding is different, such a separate regime is justified in order to promote a robust framework for providing new and interim finance. Interim finance is usually concluded on the outset of proceedings where time is of the essence and lending decision need to be made under significant time constaints. Therefore, any interim loan agreement should be concluded with as little formality as possile. Principally, the administrator of the estate (IP or DIP) should be competent to make th borrowing decision on his own, disciplined by a personal liablility in case of the later incapacity of the estate to repay. Only where such a borrowing decision would result in a significant administrative expense and, thus, may affect the pro-rata payoff of unsecured creditors, a court or, preferably, a creditors' committee approval should be mandatory.

354. In contrast, new finance allows for activities performed under a restructuring plan and, thus, is evidently subject to rules of restructuring plans which usually include creditors' approval and court confirmation. Any priority in a subsequent insolvency following a failing rescue attempt should, therefore, depend on a specific clause in the restructuring plan and

[649] The World Bank Principles (2016), Principle C16.2; UNCITRAL Legislative Guide (2010), Recommendations 211-216, and EU Cross-Border Court-to-Court Cooperation Guidelines (2015), Principle 23.
[650] See the Proposal Restructuring Directive (2016), Recital 31 and Articles 16(2) and 17(4).

consequently require creditor and court approval. Any additional (automatic) priority does neiher seem adequate nor required. Even in case of a workout, where affected creditors voluntarily agree to a restructuring arangement, priority for new finance should require a plan clause and additional court approval of the financial part of the arrangement. Only in this way, significant publicity is ensured in order to also make new creditors aware that they may face a significant preferential creditor if the debtor fails again.

355. In contrast to a priority, provisions for a safe harbour from lenders liability or claw back claims should have a statutory basis for interim and new finance alike. Here, certainty is required at the moment the lending decision is to be made. Such provisions should only allow for a liability or claw back if lenders acted in bad faith.

356. With regard to providing security for the lenders of interim or new financing, different options are available to secure their interests. First of all, security may be granted over unencumbered assets. As such may be lacking in many cases, secondly, involvement of pre-commencement secured creditors is required to grant new first-ranking security over existing assets. Up to these options, common civil law rules are applicable and sufficient. Thirdly, New first-ranking priority could be granted by court approval (super-priority) as it is possible under US Bankruptcy Code s. 364. Such an option, however, would significantly affect secured lending practices. Instead, additional personal security, especially in the form of a personal liability of the insolvency practitioner for repaying interim finance, seems a less intrusive while practical way, as common practice shows (e.g. in Germany).

2.1.6. Recommendations regarding new and interim finance

Recommendation 2.01: Member States should ensure that the administrator of the estate (insolvency practitioner or debtor in possession) has the right to take out interim finance based on its own discretion to the extend it is obtained in order to continue a business as usual and, by doing so, to preserve the going concern value of the debtor's estate. The performance of this right should be disciplined by a personal liability in case of the later incapacity of the estate to repay. Only where such a borrowing decision would result in a significant administrative expense, a court or, preferably, a creditors' committee approval should be mandatory.

Recommendation 2.02: Member States should provide that any priority for new (plan implementation) finance repayment claims in a subsequent insolvency requires a specific clause in the restructuring plan and consequently require the approval of creditors and the court. In case of a workout, priority for new finance should also require a clause in the agreement and additional court approval of the financial part of the arrangement.

Recommendation 2.03: Member States should provide for a statutory safe harbour for interim and new finance from lenders liability or claw back claims in case of a subsequent (formal) insolvency.

Recommendation 2.04: Providing security for the lenders of interim or new financing should follow the general rules of civil law rules.

2.2. Stay

2.2.1. Introduction

357. A stay (sometimes the term 'moratorium' is used) is an instrument by which the obligations of a debtor to pay one or more of its creditors for a certain period are set aside and the debtor's creditors are, for that same period, barred from enforcing their correspondent claims. In the context of insolvency, the UNCITRAL Legislative Guide formulates for 'stay of proceedings' the following: 'a measure that prevents the commencement, or suspends the continuation, of judicial, administrative or other individual actions concerning the debtor's assets, rights, obligations or liabilities, including actions to make security interests effective against third parties or to enforce a security interest; and prevents execution against the assets of the insolvency estate, the termination of a contract with the debtor, and the transfer, encumbrance or other disposition of any assets or rights of the insolvency estate.'[651] From this description flows that a 'stay' serves as a tool to balance, on the one hand, the interests involved with restructuring a viable business, and, on the other hand, the interest of certainty, predictability and stability of contractual positions.[652]

2.2.2. Significant elements from National Reports

2.2.2.1. Significant elements of a stay in formal proceedings from National Reports

358. From the National Reports it follows that several Member States have included the instrument of a 'stay' into their national insolvency systems, be it in nearly all shapes and forms.[653] These stays generally all have (elements of) the functions described above. These functions reflect the general rationale that a stay very often is of vital importance in the interest of ensuring the preservation of value and the prevention of fraud. A stay in many cases is essential to prevent seizure and other actions by individual creditors and the dissipation of assets by a debtor. Just as many times a stay does not primarily serve to guarantee equal treatment of creditors, but rather serves to protect the realisation of the intention of the debtor to restructure its business. The protection of the debtor from its creditors may also be in the enlightened and well-understood overall interest of the creditors who will accept the stay as a prerequisite for a successful restructuring if they want to stop the debtor 'bleeding' and prevent its imminent insolvency. The focus on self-interest of an individual creditor can, however, be quite counter-aligned, for example, if a secured creditor in general would not benefit from the continuation of the debtor's business. Again, other creditors are likely to react to a stay in a manner that could jeopardize a restructuring, such as terminating contracts required for the company's business continuation. Others

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[651] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions". Ditto: UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".

[652] See in general Reinhard Bork, 'Das Moratorium', in Stefan Grundmann et al (eds.), *Unternehmen, Markt und Verantwortung* (Festschrift für Klaus Hopt, Band 2, De Gruyter 2010), 1629-1646; Reinhard Bork, *Rescuing Companies in England and Germany* (Oxford University Press 2012), p. 129 et seq. In these publications the author also mentions 'constitutional issues', as a stay infriges creditors rights.

[653] See AFME study 'Potential economic gains from reforming insolvency law in Europe', February 2016, p. 18: 'Most EU Member States have introduced some form of stay as part of certain court-supervised insolvency and restructuring procedures. However, the design and quality of such stay provisions varies widely.'

would insist on delivery against pre-payment, which could result in additional liquidity problems and the success of the reorganization being possibly thwarted. The scope of a stay should be measured against such consequences if a national law orders a stay or at least would allow for it.

359. Below follows a short comparative view on some peculiarities of a stay in the Member States which were analysed by our National Correspondents. Where the purpose of this report is to specifically deal with the phenomenon of a stay to provide comfort for restructuring negotiations prior to the opening of a formal insolvency proceeding, our focus is on this type of a stay. In several reports, it is explained that the request for a stay may be included in an application for opening of formal insolvency proceedings. It could, however, also be a mandatory part of a formal restructuring process (see former Chapter 1.3). In workout support proceedings with limited court involvement, however, an optional stay with a limited scope might be adequate (see former Chapter 1.2).

360. Although the block-function of a stay is directed to all creditors, in certain laws the stay may have a more limited scope or Member States have included certain exceptions, e.g. for public claims (Spain, Hungary). A stay is generally targeted to unsecured and/or secured creditors and may, when it comes to formal proceedings, have the effect of making ineffective certain legal acts (e.g. in Italy judicial mortgage granted 90 days prior to filing). Our Inventory Reports demonstrate quite some variations on the length of a stay. To give a few examples: up to three months (CVA in England and Wales), two months plus a possible extension up to two months (the Dutch 'afkoelingsperiode'), up to 180 days (Debt restructuring agreement, following application for a 'Concordato preventivo in bianco' in Italy) or up to 270 days (Italy's 'Concordato', following application for a 'Concordato preventivo in bianco'), a two year grace period (in France for 'Mandat ad hoc' and 'Conciliation') or, after approval of a plan by the court, the initial stay may last two plus two years (Latvia).[654]

2.2.2.2. Significant elements of a stay in pre-insolvency proceedings from National Reports

361. To our National Correspondents, the question has been posed whether in EU Member States during negotiations an instrument is available that generally functions similar as a stay in formal proceedings, with some additional questions, such as how does such a stay arise (e.g. by court order) and subject to what conditions? Can the potential benefits of such an instrument be demonstrated and what is the maximum duration of such a stay?

362. We were not surprised that most of the Member States analysed responded negatively. The laws of Austria, Germany,[655] Greece, Hungary, Poland, the Netherlands and Sweden do not provide any form of stay protection for rescue plan negotiations that are conducted

[654] See Ignacio Buil Aldana (Consulting editor), *Investing in Distressed Debt in Europe: The TMA Handbook for Practitioners* (Woking: Globe Law Business Limited 2016), with short overviews of France, Germany, Italy and Spain.

[655] Once the insolvency application has been made, rescue negotiations are protected by interim measures, which is especially the case in a 'Protective Umbrella Procedure', see the chapter on Germany, in Bob Wessels & Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming).

outside formal procedures.[656] In England and Wales there is also no statutory moratorium in an out-of-court workout (see however for a company voluntary arrangement below). Also in a Scheme of arrangement there is no statutory moratorium, but the reporters add that in practice, parties will often agree to a contractual standstill in order to provide the necessary stable platform to effect a restructuring.[657] Payne[658] has explained that the possibility of such a standstill arrangement is facilitated by the fact that many schemes involve only the financial creditors, while trade creditors, being paid in full, do not participate in the scheme as their rights are not altered. The limited number of scheme creditors regarded by her as a sophisticated group that may be expected to appreciate that a rescue via a scheme is likely to be better for everyone than liquidation should the scheme fail, alternatively she explains that the development of the distressed debt market in the UK in the last decade may have led to these financial creditors selling their investment in a company to a third party rather than go through the process of enforcement of their claim against the debtor.

363. Evidently, in all these systems the freedom to negotiate (or the principle of 'freedom of contract') prevails. It is certainly possible for the parties to agree a contractual standstill in order to provide a stable platform to implement a negotiated restructuring plan (sometimes: an out-of-court workout). As the first principle of the INSOL International Workout Principles II (2017), states: 'Where a debtor is found to be in financial difficulties, all relevant creditors should be prepared to co-operate with each other to give sufficient (though limited) time (a "Standstill Period") to the debtor for information about the debtor to be obtained and evaluated and for proposals for resolving the debtor's financial difficulties to be formulated and assessed, unless such a course is inappropriate in a particular case.'[659]

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[656] In Latvia the stay is available only if a debtor drafts and negotiates the reorganization plan after the petition on legal protection procedure is submitted to the court and the court has set initiated the case. Such a stay can last two months with one month extension.

[657] In 2013 the court has granted a stay of proceedings for summary judgment so as to allow time for a scheme of arrangement to be put into place. The court has exercised its discretion to grant a stay of applications for summary judgment (to which there was no defence) in circumstances where steps to implement a scheme were well advanced and the scheme of arrangement had a reasonable prospect of success, see *FMS Wertmanagement AÖR v Vietnam Shipbuilding Industry Group & Ors* [2013] EWHC 1146.

[658] Jennifer Payne, 'The Future of Debt Restructuring', 2016, available at https://ssrn.com/abstract=2848160, at 12.

[659] These Pinciples were first published in 2000. More recently the Asian Bankers Association's Workout Guidelines (2013) have been published. They state the following with regard to a standstill in informal workouts:

'Breathing Space for Debtor Required

Financial Creditors should not withdraw facilities or be hasty to put the debtor in a formal insolvency administration or issue Court proceeding.

Standstill Prior to Meeting

Prior to the meeting of creditors, the status quo in relation to the debtor should be maintained. Financial Creditors should not take any enforcement action, other action, or reduce their exposure to the debtor until a meeting is held'.

Furthermore it is stated: 'Standstill Period

If Financial Creditors consider, at the meeting of such creditors, that it appears possible to resolve the financial difficulties of the debtor and to achieve long term viability of its business, all relevant creditors should be prepared to cooperate with each other to provide sufficient time (a 'Standstill Period') to enable information about the debtor to be obtained and evaluated and for proposals for resolving the debtor's financial difficulties to be formulated and assessed, unless such a course of action is inappropriate.

During the Standstill Period, all relevant Financial Creditors should agree to refrain from taking any steps to enforce their claims (other than disposal of their debt to a third party) or to reduce their exposure to the

364. The national legal systems of Belgium, France and Spain, however, contain certain rules with the function of a stay to protect rescue plan negotiations that are conducted outside formal procedures.

365. In Belgium, only during formal proceedings (judicial reorganisation), the stay applies to reorganisation plans or amicable agreements negotiated within this formal procedure. For amicable agreements entered into outside judicial reorganisation proceedings, the law provides for (limited) safe harbour provisions[660] for payments or performances under such an agreement in the event of a subsequent bankruptcy. The formal condition is that the amicable agreement has been submitted to the clerk's office and it should stipulate that it has been entered into for the purpose of the turnaround or reorganisation of the enterprise.

366. In England Schedule A1 to the Insolvency Act 1986 contains provisions for a moratorium for a company implementing a CVA. Such a company must be a 'small' company[661] and is not excluded from eligibility for a moratorium.[662] A moratorium can only be obtained by request of the directors. The reporters describe the procedure as follows (footnotes omitted): 'Once the nominee has issued a statement whether in his opinion the proposal is viable and whether meetings of creditors and shareholders should be convened, the directors will file certain documents with the court. The moratorium comes into effect as soon as certain documents are filed with the court. The moratorium generally lasts for 28 days. The moratorium ordinarily ends when creditors approve the proposal unless it is specifically extended. The duration can be extended for a period not beyond 2 months after the date on which notices of the meetings were sent out. The moratorium is in effect very similar to the moratorium available in administration.'

367. However, change has announced itself. In May 2016 the UK Government published a consultation seeking views on measures to update the UK's corporate insolvency regime. The proposed changes should facilitate the rescue of a greater number of viable, financially distressed companies.[663] The UK Government's goal is to enable more corporate rescues of

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debtor, but are entitled to expect that during the Standstill Period their position relative to other creditors and each other will not be prejudiced.
The length of such a Standstill Period should be limited to the time that is reasonably required to fulfill the objective of restructuring the debtor's business if that is possible. The length of a Standstill may be difficult to estimate and in some circumstances may need to be extended.
During the Standstill Period, the debtor should not take any action which might adversely affect the prospective return to relevant creditors (either collective or individually) as compared with the position of those creditors at the commencement of the Standstill Period.'

[660] Article 17, 2° and 18 Bankruptcy Act. There is no protection for (i) gratuitous or undervalue transactions, (ii) new security rights granted for existing debts, and (iii) transactions entered into with the intention to defraud creditors.

[661] A 'small' company satisfies two or more of the following requirements: (i) turnover of not more than £6.5 million; (ii) balance sheet total of not more than £3.26 million; and (iii) having not more than 50 employees.

[662] A company will not be eligible for a moratorium if it is in administration, is being wound up or where an administrative receiver has been appointed.

[663] See The Insolvency Service, 'A Review of the Corporate Insolvency Framework, A Consultation on Options for Reform', May 2016, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/525523/A_Review_of_the_Corporate_Insolvency_Framework.pdf. See also Reinhard Bork, *Rescuing Companies in England and Germany* (Oxford University Press, Oxford 2012), at para. 10.43 et seq.

viable businesses and to ensure that the insolvency regime delivers the best outcomes. Where businesses cannot be rescued, the insolvency regime should provide a low cost procedure for liquidating businesses and returning funds to creditors quickly. Although the consultation says that the UK regime delivers these objectives through a range of formal insolvency options (administration, CVA and liquidation) and pre-insolvency rescue options such as schemes of arrangement or informal creditor workouts, changes in the corporate debt market and the ambition of the UK Government to be in the top five in the world, and number one in Europe, in the World Bank's annual Doing Business Report, are the main drivers behind the proposals. The consultation relates to four proposals, one of which involves a moratorium which will provide companies with an opportunity to consider the best approach for rescuing the business whilst free from enforcement and legal action by creditors. In the consultation it is suggested that it would last for three months, with the possibility of an extension if needed. During the moratorium creditors would have a general 'right' to request information from the Insolvency Practitioner. The Government is considering extending this provision to all insolvency procedures to improve transparency and provide an additional safeguard for creditors. In September 2016, it was published that the moratorium proposal has been supported by 67% of the respondents to the consultation,[664] 37% of which agreed with the proposal as outlined in the consultation document, although it was generally felt that the safeguards for creditors should be strengthened.[665]

368. The laws of France include a system that judicial proceedings may be preceded by preventive procedures, namely the *mandat ad hoc* or the *conciliation*. Their basis is the principle of freedom of contract. Neither the debtor nor an assisting person (the *conciliateur*) has the power to force the creditors to the negotiations to grant any standstills or moratoriums. However, general French civil law allows any distressed debtor to request a court for the postponement or rescheduling of payments due to an individual creditor within the limit of two years, apart from any pre-/insolvency proceedings[666]. The resulting judgment will enable a stay of any prosecution actions initiated by the creditor, and of any enforcement proceedings that may have been initiated by the creditor, as well as a standstill on any increased interests or penalties incurred due to late payments. The stay is specifically

[664] In April 2016 R3, an insolvency trade body, presented a proposal 'A moratorium for Businesses: Improving Business and Job Rescue in the UK'. It made a call for a 'business rescue moratorium'. Such a moratorium would help save more companies under severe financial strain, saving more jobs and improving returns to creditors. During the moratorium (or: stay) period the debtor would have time to negotiate a rescue plan, sometimes mediated by a neutral third party, without the pressure of satisfying at once his creditors or having affected his assets by secured creditors. The proposal is available at https://www.r3.org.uk/index.cfm?page=1114&element=26794. Under the R3 proposal creditors would not be able to pursue debts owed by companies in a moratorium for just 21 days. This period could be extended for a further 21 days with court approval. During the moratorium, companies would be overseen by a 'Moratorium Supervisor' who would ensure the directors are using the moratorium as intended. Where the directors will remain in control of the company during the proposed moratorium, the proposal suggests that a licensed insolvency practitioner must be named in the filing who will act as a Moratorium Supervisor over the length of the moratorium. Directors must make a weekly report to the Moratorium Supervisor on progress made in the moratorium and he will act as a 'mediator' between the company and its creditors.

[665] The Insolvency Service, A Review of the Corporate Insolvency Framework, 2016, see https://www.gov.uk/government/consultations/a-review-of-the-corporate-insolvency-framework. Analysing these proposals: Jennifer Payne, 'The Future of Debt Restructuring', 2016, available at https://ssrn.com/abstract=2848160, at p. 15 et seq.

[666] Article 1244-1 of the Civil Code.

targetted to and restricted to the debt owed to the creditor against which the petition has been filed. It therefore has no collective effect.

369. In Spain, since 2014, the law[667] provides that no single judicial enforcement procedure commenced by creditors may be initiated (and those initiated will be suspended) when a percentage of creditors representing no less than 51% of the debtor's financial liabilities have approved the initiation of negotiations to conclude a Refinancing Agreement and where that creditor group has also committed itself not to pursue individual enforcement actions within the negotiation period.

2.2.3. Significant international tendencies

370. Several international soft law instruments recommend a stay to be available in an insolvency context, notably in formal insolvency proceedings.[668] On a country level no specific rules or practices have been reported. On the EU level, the Recommendation of March 2014 introduces a mechanism, which was suggested on the basis of Recital 18: 'A debtor should be able to request the court for a stay of individual enforcement actions and suspension of insolvency proceedings whose opening has been requested by creditors where such actions may adversely affect negotiations and hamper the prospects of a restructuring of the debtor's business. However, in order to provide for a fair balance between the rights of the debtor and of creditors, and taking into account the experience of recent reforms in the Member States, the stay should be initially granted for a period of no more than four months.[669]

2.2.4. Impetus for recommendations

371. We recall the general considerations that form the context of a stay: the inherent conflict between the general rule that a debtor should pay its debts when these are due and the (during recent years growing) importance given to the interest of viable companies to be able to restructure with an aim to create a larger value add for all stakeholders, including employees, the economy as a whole as well – on the longer term – the creditors. A stay acts as an instrument to bridge this conflict.

372. Such a bridge functions only in relation to the specific circumstances of the case at hand. We also submit that the more flexible the procedure to obtain a stay is, the earlier a debtor would consider to request a stay and, therefore the earlier he achieves the protection he wishes. In bridging the inherent conflict (creditors' rights as opposed to the interests of continuation of a debtor's viable business). Generally, in practice, one would see that in a pre-insolvency period a debtor would need time to form its opinion as to which

[667] The Royal Decree-Law 4/2014 and the Law 17/2014.

[668] Examples being the Principles of European Insolvency Law (2003) § 3.5; UNCITRAL Legislative Guide (2004), Recommendations 39, 46 and 48, Principle C5.2 of the World Bank Principles (2016), and EU JudgeCo Principles (2015), Principles 8 and 9.

[669] The recital resulted in Recommendations 10 – 14 in the Recommendation of March 2014. In the Proposal Restructuring Directive (2016) considerations regarding such a stay has led to (i) a stay of individual enforcement actions of up to four months (Article 6(4)), under certain prerequisites, up to twelve months (Article 6(7)), with suspension of the obligation to file for insolvency (Article 7(1)), except where the debtor becomes illiquid during the stay period (Article 7(3)).

goods are in inventory and/or which goods which he wants to keep in any case for the estate, for example in connection with a possible continuation or sale of (part of) the business. A debtor's building up to a plan can be undermined seriously, when placed by the third party creating a fait accompli in this period. There is, therefore, a need for the ability to impose a stay to such parties individually or collectively, during which third parties cannot exercise their rights or only with the authorization of the court. A stay should also prevent that all kinds of assets will be taken away out of fear that otherwise still others – especially the tax authorities – might then exercise their rights.

373. A first conclusion therefore is that overall there is a common interest in preserving the going-concern value for debtor and creditors as a group, which the logical result that it is for the common interest for the debtor and the creditors as well that essential assets and contracts are kept together. Moreover, it is in the common interest to check the estate for assets and contracts which are actually essential for the future (restructured) business.

374. These common interests must have their limitations. As a minimum requirement, the balance between the interests of the debtor and the creditors as a group should respond to the principal of proportionality, as well as be aligned with the specific context in which it will function. The principle of proportionality means that an infringement of creditors' rights should be kept to the minimum required. The functional limitation flows from its context: outside of formal proceedings, a stay is an instrument that should not have the purpose of supporting loss-making businesses, but rather facilitate the restructuring of the financial debt of viable, but over-indebted debtors (financial distress). Such debtors should have a positive operational cash flow which means that they are able to attract the interests of third parties (lenders) to fund its future working capital needs during the workout process. For such workouts, it should be hardly necessary to stay all creditors to protect negotiations and a confirmation process. It should suffice to limit an available stay to situations in which a single creditor is damaging the process by enforcing his rights to the disadvantage of all creditors and the debtor, e.g. by disrupting the business through enforcement actions.[670]

In formal (restructuring and insolvency) proceedings, however, a stay should be available automatically or by request and have a collective effect. The flat-rate statutory arrangement of an automatic stay connected to (an application for) the initiation of a formal procedure, evidently results in legal certainty and warrants against a possible loss of time. This form, however, demands a public notice and is not geared to the specific circumstances of the case. Such a form also may trigger strategic behaviour from a non-scrupulous debtor as a surprise attack for those creditors that are affected by the stay. Therefore, such a standardised immediate effect requires the supervision of a formal procedural setting and does not go well with the individual approach of a workout.

[670] An additional barrier for a creditor to enforce rights against a troubled debtor may come from a jurisdiction's civil law system. When a company is in financial trouble, most creditors will be aware of it as some (partial) payments were received late, rumors in the market occur or they are being informed by another creditor or informed by the debtor itself. Asking for full and timely payment in such a situation or – even only – accepting payment may be contractually legitimate, but also an act contrary to good faith to be observed by the receiving creditor even against his co-creditors. It may also be regarded that such a creditor withdraws from the concursus principle, which allows for the application of claw back rules.

Effects of a stay

375. In a workout setting, it follows from the nature of the optional right to apply an individual stay that the resulting 'freeze' has a relative effect. A stay's scope (affected creditors) and effect (on legal positions) is limited according to its function in a workout. If a debtor faces a situation in a workout negotiation where a full stay is deemed required, formal proceedings are available to provide such protection.

376. In formal (restructuring and insolvency) proceedings, a stay must to the full extend also allow for organising negotiations and deciding on rescue options (plan or going concern sale). Here a stay should: completely stop enforcement actions of creditors (including the tax authority); ban the realisation of assets by secured creditors, block applications for opening insolvency proceedings during restructuring proceedings; prevent the debtor to dispose or pay creditors out of the ordinary course of business; block the effects of contract termination or acceleration rights; suspend any pending proceedings and ban a set-off of a claim (as a successful set-off deprives the debtor of liquidity that may be necessary for funding its ongoing business activities).[671]

377. Still, also in formal proceedings, the court should be allowed to cut to size the effects of a stay by setting conditions. In case of a request by the debtor (outside of formal proceedings) and or if requested by a creditor, the court should order certain conditions or requirements for a stay which may involve an act (for example, for the debtor the provision of security), a payment (for example, reimbursing a real interest rate or pay a usage fee) or an obligation to abstain (prohibition of use, consumption or disposal). Conditions may also focus towards any third party, for example to permit the debtor to continue using its property or continued use of certain public licenses.

Duration

378. Duration involves a starting point, the determination of any length of the stay and its termination.

379. The length of a stay bears the stamp of the 'functional' considerations above. A serious and truthful plan-offer to restructure from the debtor in relation to a viable business in troubles should, in principle, make the use of a 'long' stay unnecessary. Thus, in a workout scenario, a stay should only last as long as it is reasonable to finalise already initiated negotiations. As such a process may have a different length in each case (e.g. 2 to 4 weeks), the duration of a stay should be ordered by a court, but not be set in a statute in the form of a minimum duration.

In case of a stay in formal proceedings, such a stay is only a first step. The stay period should be long enough to enable a sound assessment and decision on a rescue option. At the same time, it must also be ensured that a decision is reached within a reasonable timeframe. The stay should therefore be guaranteed, but limited in time. Bork assumes that '[I]n normal cases, a three-month limit should be sufficient to arrive at a restructuring decision, and the

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[671] Reinhard Bork, *Rescuing Companies in England and Germany* (Oxford University Press, Oxford 2012), para. 10.10

law should permit the court to grant extensions in exceptional situations'.[672] This assessment seems reasonable.

380. A stay ends when proceedings end, in particular when the restructuring plan starts getting implemented. From that moment on parties operate under normal (agreed) circumstances. The following occasions should also result in lifting a stay during restructuring proceedings: (i) the debtor discontinues its business, (ii) the court rejects the application for an extension of a stay, (iii) the debtor withdraws its restructuring plan without issuing a modified one, (iv) the plan is not approved in a voting, (v) the court does not confirm, or (vi) during all these steps the debtor acts against the provisions set in the staying order or otherwise acts in bad faith.

2.2.5. Recommendations regarding a stay

Recommendation 2.05: In a workout, all relevant creditors should be prepared to co-operate with each other to give sufficient (though limited) time (a "Standstill Period") to the debtor for information about the debtor to be obtained and evaluated and for proposals for resolving the debtor's financial difficulties to be formulated and assessed, unless such a course is inappropriate in a particular case. Member States should adopt or endorse principles and guidelines developed by international or European non-governmental organisations active in the area of restructuring and insolvency such as the INSOL International Workout Principles II.

Recommendation 2.06: In a workout support procedure, a stay should neither be automatic nor collective. Instead, a standstill agreement should protect the interest of all relevant stakeholders.

Recommendation 2.07: For safeguarding a workout, the debtor should be able to request a stay against a specific creditor whose actions have the capacity of frustrating all restructuring efforts. The duration and content of such an individual stay should be set by the court after hearing both sides. Any such stay is the result of a court's assessment of the application, laid down in a judicial order which is made to measure towards the individual circumstances as presented to the court and geared to the interests of all parties involved.

Recommendation 2.08: In formal restructuring or insolvency proceedings, a collective stay should be an automatic effect of the commencement of proceedings or available on request. Member States should provide for a stay to last as long as proceedings last, but should limit the duration of restructuring proceedings to avoid costly delay. A first, but extendable period of three months seems reasonable.

Recommendation 2.09: Any affected creditor may request to have the stay lifted with respect to its claims or interest and the court must decide, taking into account the interests of all parties involved.

[672] Reinhard Bork, *Rescuing Companies in England and Germany* (Oxford University Press, Oxford 2012), para. 10.08.

Recommendation 2.10: Any judicial order regarding a stay may contain requirements or other conditions which support a speedy, inexpensive, negotiated adjustment of a debtor's debts, including conditions that affected creditors will be adequately protected during the period of the stay, such as a compensation for use of assets.

CHAPTER 3:
Executory contracts

381. The viability of a business depends on the continuation of its essential contracts at least as much as on a successful business idea. Without an essential license, without energy and goods supply, without a work force or a lease, the debtors' business simply cannot continue. Without the prospect of contract continuation (in whatever form), any option to restructure, but also any value maximizing going concern sale in a liquidation, is off the table. The termination of contracts – by force of law or based on a contractual clause – due to the commencement of restructuring or insolvency proceedings must, therefore, be carefully considered.

382. In contrast, no special treatment is required for contracts under which at least one party had fully performed prior to the commencement of proceedings. If the debtor is yet due to perform, the counterparty may take a legal position which is laid down in national law, many times being that he is allowed only to file a claim for performance or damages and assume the ranks of an unsecured creditor. If on the other hand the counterparty has not yet performed, the respective claim is an asset of the estate and the administrator may demand performance. If both parties had fully performed their duties under a contract before the commencement of proceedings, the transactions under the contract may only be reconsidered under the rules for fraudulent transfers (see Chapter 6). Thus, a special legal framework taking care of contract continuation is only required if both contractual parties have not yet fully performed their obligations when proceedings are commenced. These contracts generally are called executory contracts, meaning contracts between the debtor and one or more creditors under which both sides still have obligations to perform at the moment insolvency proceedings commences (or, alternatively, at the moment a stay of individual enforcement actions is ordered or established by way of law).[673] Still, the general principle found is that the commencement of pre-insolvency or formal insolvency proceedings does per se terminate a contract to which the debtor is a party.[674]

3.1 Executory contracts

383. For executory contracts, any legal framework must balance the competing interests of the debtor's estate (and its creditors) with the interests of the counterparty in the light of the general goals of the laws in which such a framework functions. For an insolvent debtor, maximising the value of the debtor's estate is the main focus of any administration and insolvency policy for the benefit of all creditors. From this perspective, it is crucial to be able to perform every profitable executory contract while being allowed to reject any burdensome, loss-bearing contract that would only add to the debt pile. In case of a debtor with an on-going business, the interest in keeping the business alive requires the

[673] See David Hahn, 'The Internal Logic of Assumption of Executory Contracts', 13 U. Pa. J. Bus. L. 2011, 723. The term has a much narrower definition in US law after the definition proposed by Vern Countryman, 'Executory Contracts in Bankruptcy, Part I', 57 Minn. L. Rev., 1973, 439, 460, became section 365 in the US Bankruptcy Code; see also Jay L. Westbrook, 'A Functional Analysis of Executory Contracts', 74 Minn. L. Rev., 1089, 227 for a critical analysis. The underlying concept comprises all uncompleted contracts older and is known to all jurisdictions.
[674] This reflects an international standard; see Principles of European Insolvency Law (2003), § 6.1.

continuation of all contracts that allow that business to operate. However, the interest of the counterparties would usually call for respecting their pre-insolvency contractual rights including termination rights. Contract law usually reflects the risk of a party to a contract becoming insolvent either by a right to terminate the contract or, at least, a right to withhold performances until the insolvent party is ready to fulfil their obligations. Based on the policy principle of respecting pre-insolvency entitlements, any insolvency or restructuring framework is asked to limit any infringement of such contract law entitlements when protecting special restructuring and insolvency policy in general interest of all creditors and other stakeholders (like e.g. employees) including the debtor.

3.1.1 Treatment in formal insolvency proceedings

384. The common legal approach in formal insolvency proceedings, we found, is following the principle that the commencement of proceedings does not affect the contracts of the debtor. At the same time, in laws providing so, any contractual claim for a performance by the debtor is subject to an automatic or requested stay which prevents the counterparty from enforcing contractual rights (for termination rights; see 3.1.2.). This could also be the result of a provision in law determining that executory contracts will not continue unless the insolvency practitioner within a certain period of time states that he wishes to continue the contract. Also a stay shall commonly allow the administrator of the debtor's estate (usually an insolvency practitioner) to evaluate every executory contract before deciding whether to continue or to reject it. Thus, it is for him or her to decide about the continuation, assignment or termination of executory contracts within a specified timeframe.[675]

385. Rejected contracts are cleared and the counterparty may file an (unsecured) claim for damages if there are any.[676] Assumed contracts are to be performed by both parties in accordance with all provisions in the contract and other contract law requirements. The legitimate interest of the counterparty in receiving full performance from the debtor is commonly reflected in insolvency law provisions which rank the respective claims (including damages claims in case of a later default) as administrative expenses which are not affected by the stay anymore. Some jurisdictions offer additional safeguards in the form of guarantees[677] or the requirement of a court approval.[678] As a result, the interest of both contractual parties and insolvency stakeholders are balanced.

386. While the administrator's right to decide about the continuation or rejection of executory contracts works satisfactory for most types of contracts, some may require a special regime. First, the administrator's option is not consistent with "speculative" transactions (e.g. certain financial contracts) because it would allow the estate to only assume contracts that turned out to be profitable while rejecting all others. Here, insolvency would create a windfall profit. Second, the right to choose is also not well compatible with contracts that are based on a personal relationship with the debtor, if an insolvency

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675 This default rule on executory contracts was reported in all Inventory Reports. It is also recommended in international standards; see e.g. UNCITRAL Legislative Guide (2004), Recommendation 72.
676 This is obviously also the common approach; see our Inventory Reports on 3.1.1., or UNCITRAL Legislative Guide (2004), Recommendation 82.
677 See e.g. the Netherlands, Germany (Insolvency Code s. 61), Poland, also Sweden.
678 See US Bankruptcy Code s 365(a)

practitioner takes over. For both types of contracts, some jurisdictions provide for an ipso facto termination upon the commencement of proceedings.[679]

387. On the other hand, there are types of contract that may require to remain unaffected by the commencement of proceedings as well as by an option to reject because they are held to be essential for both the debtor and the counterparty (e.g. real estate lease,[680] employment,[681] utility[682] contracts). However, our reports do not indicate a common approach here. If contracts are continued, they cannot be terminated by the counterparty under contract law based on the financial status of the debtor, while the administrator may be allowed to terminate the contract observing a (shorter) statutory period.[683] Post-commencement claims of the counterparty are being protected as if the contract were elected for continuation.

388. Overall, a default rule on executory contracts in formal insolvency proceedings that contains the administrator's right to reject or continue a contract and the counterparty's right to be protected in case of being forced to perform under the continued contract seems well-balanced and commonly accepted.[684] Exemptions from the rule for specific types of contracts must be well considered and clearly defined.

3.1.2 Treatment in restructuring and pre-insolvency proceedings

389. Restructuring and pre-insolvency proceedings differ from formal insolvency proceedings by aiming solely at the survival of the (legal entity of the) debtor. The success of such procedures will often depend on limiting their effects to the extent necessary while not interfering with the debtor's daily business activities if possible. It would not seem helpful here to stay all executory contracts of the debtor pending the decision of the debtor whether to reject it or not. Instead, the basic principle of leaving contracts unaffected would prevail. The continuation principle would also include contracts which are essential for keeping the business afloat (license[685], lease, energy and goods supply, service, or employment contracts) and, thus, secure the basis of every restructuring effort.

390. On the other hand, the ability to terminate burdensome contracts without non-insolvency law restrictions (e.g. from labour law), has the potential of being a major restructuring instrument. They enable the debtor to, for instance, reduce redundant workforce or exit overly expensive or redundant long-term lease or license contracts for less or even no costs.

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679 See e.g. Austria, Belgium, Germany or Greece.

680 See, e.g., Germany or with some exceptions, Italy.

681 See Chapter 5.1.1.1.

682 According to our Inventory Reports, licensing, domain name, IP, or utility contracts do not yet enjoy any special treatment with regard to the right of the administrator to continue or reject them.

683 See, e.g., Austria, Germany, or France.

684 See David Hahn, 'The Internal Logic of Assumption of Executory Contracts', 13 U. Pa. J. Bus. L. 2011, 723, 731-735.

685 Reference is made to the soft law rules drafted by the *Association Internationale pour la Protection de la Propriété Intellectuelle* (International Association for the Protection of Intellectual Property) ('AIPPI') which aim at stimulating the international harmonization of rights and duties under insolvency regimes for licensing agreements, laid down in 2014 in a Resolution.

391. When balancing these competing interests, there is a clear distinction to be made for a restructuring in a pre-insolvency workout support procedure[686] and one pursued in a formal restructuring procedure. Presently, jurisdictions with a workout support procedure do not provide for any option to reject executory contracts. The paramount policy here is to only affect the rights of those creditors that are involved in the restructuring effort while leaving all others unimpaired.[687] The picture is different for jurisdictions featuring restructuring proceedings.[688] Such proceedings are available for insolvent as well as not (yet) insolvent[689] debtors and feature a number of tools and characteristics of formal insolvency (liquidation) proceedings (court involvement, collective effect of a stay etc.). Such proceedings usually also impact executory contracts by subjecting claims from such contracts to a stay and allowing the debtor to reject burdensome contracts.[690] At the same time, some types of contracts may enjoy a special protection (e.g. employment contracts; see Chapter 5.1.1.1.).

392. The specific design that we recommend for a restructuring framework (see Chapter 1.1.) allows for a clear allocation of the right to reject executory contracts because it provides for a clear distinction between workout support procedures and formal restructuring as well as insolvency proceedings. This distinction being that workout support procedures would not comprise such features, and formal restructuring as well as insolvency proceedings, would provide a wide number of restructuring tools including a stay and a rejection right. Here, regulation should include provisions securing services which are essential for continuing the business of the debtor[691] (or the counterparty in case of an insolvent licensor[692]), like real estate or purchase leases, energy supply, IP and domain services, or licenses.[693] Regulation could follow the example of regulation of employment contracts which are to be continued in principle, but can be terminated in short term if necessary for the restructuring (see Chapter 5.1.1.1.). In practice, a renegotiation of such contracts could be supported if the debtor were to terminate it more easily (yet not automatically) than under contract law.[694]

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686 We also refer to such procedures as type 1-procedures; see Chapter 1.1.2.

687 See, e.g., French Conciliation, the Belgian Amicable Settlement, the Spanish Judicial Homolgation, the German bond restructuring or English Schemes of Arrangement.

688 See also Fabrice Robert-Tissot, 'The Effects of a Reorganization on (Executory) Contracts: A Comparative Law and Policy Study [United States, France, Germany, Switzerland], 3 International Insolvency Law Review 2/2012, 234 et seq.

689 We also refer to such pre-insolvency procedures as type 2-procedures; see Chapter 1.1.2.

690 See, e.g., the French Procédure de Sauvegarde, the Italian Concordato Preventivo or the Polish Arrangement Proceedings.

691 See David Hahn, 'The Internal Logic of Assumption of Executory Contracts', 13 U. Pa. J. Bus. L. 2011, 723, 731. Such provisions for "essential supply contracts" were part of a consultation paper published by the UK Insolvency Service on 25 May 2016 aimed at reforming the UK's corporate insolvency regime. For a rather sceptical response, see Ian Fox, Rachel Anthony, Neil Griffiths, Will Gunston & Farrington Yates, 'A Review of the Corporate Insolvency Framework: A Lawyers' Perspective', 13 ICR 2016, p. 300, 302.

692 See US Bankruptcy Code s 365(n) as an example.

693 For German views regarding the validity of ipso facto clauses in energy contracts, see Florian Jacoby, *Lösungsklauseln in der Insolvenz*, in 35 ZIP 2014, 649 et seq; Klaus Wimmer, *Eine Lösung für die Lösungsklauseln* (Festschrift für Heinz Vallender zum 65. Geburtstag, Köln: RWS Verlag Kommunicationsforum GmbH 2015), p. 793-825.

694 In France, since 1 October 2016, a renewed Article 1195 Code Civil, introduces – inspired by soft law instruments – the rule that the court can change (or terminate) a contract in case of '… *un changement de circonstances imprévisible lors de de la conclusion du contrat rend l'exécution excessivement onéreuse pour une partie qui n'avait pas accepté d'en assumer le risque*' (a change of circumstances that was unforseeable at the

3.2 Termination and modification of contractual rights

393. Rules on executory contracts are incomplete if they only define a right to reject or assume such contracts for the administrator of the estate after the commencement of proceedings left such contracts unaltered. Many contracts or even statutory rules in respective contract law contain clauses that give the counterparty the unconditional right to terminate or accelerate the contract in the event of a default which commonly includes the petition for commencement, or the commencement of insolvency proceedings, but also the appointment of an insolvency practitioner (so called ipso facto clauses). If such contractual rights were to remain intact, the preliminary continuation of a contract and the right of the administrator to decide would become irrelevant in most cases.[695]

394. Following this line of thought, most jurisdictions in our study allow insolvency rules to override ipso facto clauses. In many jurisdictions, such clauses are null and void in case of any kind of insolvency proceedings[696], while in others such clauses are only invalid in case of restructuring[697] or bankruptcy[698] proceedings. English law,[699] however, follows a different approach and respects all contractual terms including ipso facto clauses, in particular in the context of complex financial agreements, within the broad limits of the pari passu principle and the anti-deprivation rule.

395. This analysis shows that no common or approximated standard has yet been developed with regards to ipso facto clauses in executory contracts. Allowing insolvency and restructuring law to override such contractual rights is an infringement of pre-insolvency entitlements that requires meaningful justification and appropriate safeguards. Considering that any restructuring is doomed if the commencement of proceedings may prompt financial creditors to accelerate the repayment of credit or licensors and lessors to terminate contracts, there is good reason to justify overriding insolvency rules for the sake of keeping a business alive, with a view of continuing such business. In return, insolvency law must also provide for safeguards for the counterparty, which is now bound to work with a debtor in restructuring or even insolvency, by securing the timely performance of the debtor under the contract. Only if contractual rights of termination are essential beyond the scope of the contractual relationship, which may be the case for certain (not all) financial contracts (e.g. derivatives), they are to be respected.

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time of the conclusion of the contract renders performance excessively onerous for a party who had not accepted the risk of such a change), including a duty to renegotiate before seising the court. Change of circumstances as a contractual dogma has not been subject of this report. See for an overview: B. Başoğlu (ed.), The Effects of Financial Crisis on the Binding Force of Contracts – Renegotition, Rescission or Revision, Springer 2016.

[695] It is possible that creditors between themselves (in inter-creditor agreements) restrict themselves to instigate any form of insolvency proceeding. On the use of these clause so-called 'non-petition' clauses, Hamisch Anderson, 'Non-Petition Clauses', Nottingham Insolvency and Business Law e-Journal 2013, 3, 15 et seq.

[696] See Austria, Germany, Italy or Spain. This reflects international standards, see UNCITRAL Legislative Guide (2004), Recommendation 70.

[697] See Belgium, France

[698] See Poland.

[699] See also Greek law.

396. For these reasons, a differentiated approach seems best fitted to handle ipso facto clauses. To ensure that contractual acceleration or termination clauses are only overridden where it is necessary to keep the debtors business alive in order to support restructuring efforts or a going concern sale in a liquidation, such clauses should remain valid, but their enforcement should be affected by any (collective or individual) stay of enforcement actions under respective restructuring or insolvency law.[700] Following this approach, lawmakers should provide for (1) safe harbours for clearly and narrowly defined types of (executory) contracts that would neither be affected by such a stay nor fall under the administrator's right to decide. They should also provide for (2) a way to lift the stay as soon as efforts to continue the business fail and a piecemeal liquidation is inevitable.

3.3 Transfer of contracts in a going-concern asset deal of the debtor's business

397. The continuation of a profitable executory contract, e.g. a long term real estate lease with a rent below market value, is certainly essential in a restructuring. If, however, the only viable option is the sale of the debtor's business (asset deal)[701], potential bidders would only be willing to pay more if they are able to assume such profitable contracts. Under contract law, the required assignment of contracts usually requires the consent of the counterparty[702] and such consent may not be available for contracts that are not favourable to the counterparty anymore. Here, insolvency law could provide for an assignment of contracts regardless of the counterparties consent[703], or could authorise the insolvency courts to approve an assignment if the counterparty is not substantially disadvantaged by the assignment.[704] While a number of Member States have introduced such rules, most jurisdictions do not allow for any assignment of a contract (not just a claim) against the explicit consent of the counterparty.[705]

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[700] Such a broad scope of a stay would not only include ipso facto clauses, but also all other contractual clauses that allow a counterparty to terminate or accelerate a contract, e.g. based on a default.

[701] If the purchase is done by a share deal, the purchase acquires the corporate entity of the debtor including all contractual right which means that there is no need for any assignment. Often, however, a share deal is not an option, either because the debtor is not a company or because the purchaser is not interested in acquiring all debt connected to the entity. An asset deal is the only option then. See Chapter 7.

[702] An exception is the Italian Civil Code (Article 2558). Here, unless prohibited by the specific nature of the relevant agreement (for example: contracts with professional services providers), any transfer of the going concern of the debtor automatically comprises the transfer of all contracts of the debtor to the purchaser. The counterparty may not object, but has the right to terminate the contract within three months for just cause if a pre-existing ground for termination subsists. Exceptions also exist in Swedish civil law for lease and IP contracts, and – indirect – in the Netherlands, see the final part of Article 6:236(e) Civil Code which provides that in contracts with a consumer (a party natural person, not acting in the exercise of a profession or business) the following clause, included in general contract conditions, is presumed to be unreasonably onerous, namely a clause under which the consumer is to grant advance permission to pass the agreement obligations to a third party, unless the consumer at any time has the power to terminate the contract, or the counterparty is liable for the fulfillment of the obligations of the third party *or the transition takes place in connection with the transfer of an undertaking to which both the obligations and the opposite stipulated rights belong* (italics by the reporters).

[703] See the Spanish Insolvency Code Article 146 (bis). Similar rules seem to exist in Latvian and Polish insolvency law.

[704] See UNCITRAL Legislative Guide (2004), Recommendation 83. Such a court order is available under the French Commercial Code Article L.642-7.

[705] See Austria, Belgium, England & Wales, Germany, Hungary, the Netherlands and Sweden.

398. As there is no common or approximated standard for the assignment of contracts against the objection of the counterparty in national insolvency *and* civil law, applying the principle of respecting pre-insolvency entitlements will not result in a common solution. At the same time, insolvency and restructuring law offers ways to make use of profitable contracts by maintaining the entity of the debtor by way of a restructuring or a share deal. If these options are not available due to the circumstances of a specific case, civil law would usually call for a consensual agreement with the counterparty to assign the contract to a purchase of the debtor's business (assets). Overall, such a regime seems to balance the interests of the debtor's creditors and the counterparty quite well at first sight. It would, however, delay the transfer of profitable contractual provisions if such provision would survive the negotiations about the counterparty's consent at all. Additional intervention by insolvency law tools could, therefore, be useful. To this end we would recommend a rule under which all executory contracts that are still valid[706] are assigned to the purchaser of the debtor's business in a going-concern asset deal[707] while only allowing the counterparty to file an objection to the supervising (or sale confirming)[708] insolvency court claiming to be worse off with the new contract party in comparison to the debtor.

3.4 Recommendations

Recommendation 3.01: Member States should follow the principle that the commencement of proceedings does not affect executory contracts of the debtor. Rights from such contracts should be subject to a stay and the administrator of the debtor's estate (insolvency practitioner or debtor in possession) should be allowed to decide on the continuation or rejection of any executory contract provided that the legitimate interests of the counterparty are respected. Exemptions for specific types of executory contracts should be limited, well considered and clearly defined.

Recommendation 3.02: Member States should limit the right to decide about the continuation or rejection of any executory contract to formal restructuring or insolvency proceedings. The tool should not be available in a workout or a workout support procedure.

Recommendation 3.03: Member States should consider specific legislation for executory contracts that are essential for continuing the business of the debtor like, for instance, real estate lease, energy supply, intellectual property and domain services, or license agreements. When doing so, Member States should take into account internationally accepted soft law rules.

Recommendation 3.04: Member States should provide that contractual acceleration or termination clauses in executory contracts themselves remain unimpaired and valid.

[706] The rules governing the rejection or continuation of executory contracts would allow for the prior selection of transferred contracts by the administrator of the debtor's estate (which is the insolvency practitioner in liquidation proceedings).
[707] The assignment would not include liabilities of the debtor under the contract incurred before the clearing date.
[708] See Chapter 7 for the role of courts in such sales.

However, acts of enforcement or execution of such clauses should have a no effect in case of a stay of enforcement actions under respective restructuring and insolvency law.

Recommendation 3.05: Member States should ensure the right to lift the stay as soon as efforts to continue the business fail and a (piecemeal) liquidation is inevitable.

Recommendation 3.06: Member States should introduce rules that allow for assigning all executory contracts that are still valid to the purchaser of the debtor's business in a going-concern asset deal. Such rules should include the right of the counterparty of the assigned contracts to file an objection to the court claiming to be worse off with the new contract party in comparison to the debtor.

CHAPTER 4:
Ranking of creditor claims; governance role of creditors

399. This chapter covers the creditors' role in insolvency proceedings. First, we look at the creditors' right to receive payments on their claims. In the second part, we look at the right of creditors to make procedural decisions in insolvency or restructuring proceedings.

4.1 Introduction

400. Insolvency proceedings in their classical sense are, at their core, liquidation proceedings. The efficient liquidation of the estate and the distribution of receivables amongst creditors are the core function of such a procedure. As by definition of an insolvent debtor, the proceeds from selling the estate will not suffice to pay all creditors the full amount of their claims, insolvency law may only choose between three options: (1) all creditors are paid equally pro rata, or (2) some creditors are paid first before others, or (3) a mixture of both options. All jurisdictions in our survey have taken the third path. And while our Inventory Reports show significant divergences among Member States as to ranking of creditors in detail, most national laws provide for a list of ranking of claims, which presents basic similarities.

401. As a general rule, all unpaid creditors are affected by the insolvency of their common debtor in the very same way.[709] They cannot expect to be paid in full. Here, the only equitable and fair solution would be a pari passu treatment of creditors meaning that all creditors are treated equally on the basis of and in proportion to their pre-insolvency entitlement and no creditor (or class of creditors) may obtain preferential treatment. We submit that this is the real cornerstone of insolvency proceedings.

402. However, some creditors may present good reasons to be paid more than this 'equal' part up to be paid in full. These payments may be essential to even conduct orderly proceedings (courts, insolvency office holders) or to keep the debtor's business alive (interim financers). Some creditors may have particular social needs (e.g. employees) while others may perform specific public functions (e.g. tax authorities, social security agencies). Some may have simply bargained for a preference (secured creditors). All national legislators have responded to such needs and guaranteed full payment to specific classes of creditors. Considering the limited capacity of an insolvent estate, such a full payment for some creditors results in less or even pro rata payment for the remaining creditors. Preferences in distributions lead to a ranking of creditors.

403. In general civil law preferences, without exception, fully apply in insolvency proceedings. Legislators may grant preferences in various ways.[710] Most efficiently, a creditor may be authorised to detract a specific asset (movable, immovable or right) from

[709] In case of contractual creditors, from all existing mutual obligations stemming from a contract, we limit ourselves in this chapter to the payment obligation from the debtor to the creditor.
[710] For a detailed report (apart from our Inventory Reports), see e.g. Dennis Faber, Niels Vermunt, Jason Kilborn, Tomáŝ Richter, Ignacio Tirado (eds), *Ranking and Priority of Creditors* (OUP 2016) collecting (but not analysing or comparing) reports from Australia, Austria, Belgium, Canada, Czech Republic, England, France, Germany, Ireland, Netherlands, Poland, Scotland, Spain, Sweden and the US.

the estate in order to liquidate or otherwise realise the asset autonomously and independently from the conduct of the insolvency proceedings. Such an authorisation to detract could be based on a retention of title (property) or a security right (lien) which may again derive from contractual agreements or statutory provisions. Often, such rights only refer to specific assets. They may, however, also encumber a wide range of assets (e.g. a floating charge). All these forms of preferences flow from the Member States' general civil law systems.

404. Another legislative way to grant preferences – often laid down in laws relating to insolvency – is to stipulate a preferential payment from the proceeds resulting from the liquidation of the estate in the course of proceedings. Here, no assets are extracted from the estate which may allow for the continuation of the debtor's business and its going concern sale. Preferential distribution may again be based on a security right (which extends to receivables), but also on a simple statutory provision.

4.2 Ranking of creditors

405. Our Inventory Reports indicate that national legislators have made use of all available techniques to create preferences, both in general civil laws as well as in insolvency laws, for a variety of policy reasons. In order to allow *ex ante* evaluations of insolvency risks and preserve the expectations of all the parties involved, it is important that classes of creditors are specified in clear terms, in particular individuating those creditors enjoying the right to be satisfied in priority[711].

406. For the priority of claims, national insolvency laws employ a wide variety of different approaches, both with respect to priorities between different ranks and the treatment of creditors within a particular rank, for example different sub-ranks may be created among unsecured creditors.[712] The UNCITRAL Legislative Guide on Insolvency Law provides an overview. To begin with priorities between different ranks, most national insolvency laws recognise the rights of secured creditors to have a first priority to satisfy their claims, either from general funds or the proceeds of sale of the specific encumbered assets.[713] The administrative expenses of the insolvency proceeding often rank below secured claims but above unsecured claims.[714] However, there are also insolvency laws that rank secured claims below the costs of administration and other claims, such as unpaid wage claims, tax claims, environmental claims and personal injury claims.[715] Once the claims of all secured and priority creditors have been satisfied, the balance of the insolvency estate would generally be distributed to ordinary unsecured creditors on a pro rata basis before being distributed to any equity holders.[716] The UNCITRAL Legislative Guide on Insolvency Law then recommends the following priority order for claims other than secured debt:

1. administrative costs and expenses;

[711] World Bank Principles (2016), Principle C12.1; UNCITRAL Legislative Guide (2004), Recommendation 186.
[712] UNCITRAL Legislative Guide (2004), Recommendation 267.
[713] UNCITRAL Legislative Guide (2004), Recommendation 269.
[714] UNCITRAL Legislative Guide (2004), Recommendation 270.
[715] UNCITRAL Legislative Guide (2004), Recommendation 269.
[716] UNCITRAL Legislative Guide (2004), Recommendation 273.

2. claims with priority;
3. ordinary unsecured claims; and
4. deferred claims or claims subordinated under the law.[717]

Recently Wood has submitted that usually, the 'corporate ladder' comprises of at least six main ranks or rungs, in the following way:

1. super-priority creditors (with some super-super priority creditors);
2. priority creditors;
3. pari passu creditors;
4. subordinated creditors;
5. equity shareholders; and
6. expropriated creditors.

Wood has observed that sometimes there are some 60 or 70 rungs on the ladder.[718]
In principle, jurisdictions differentiate in the classes mentioned in the UNCITRAL Legislative Guide on Insolvency Law.[719] With only a few limited exceptions (see below), ranking results in absolute priority meaning that lower ranking creditors only receive value after all superior claims are paid.[720]

4.2.1 Creditors owning assets in the estate

407. Creditors who may legally claim that specific assets do not belong to the debtor's estate are entitled to detract these assets from the administration because their assets do not form a part of the estate. Thus, these assets cannot be liquidated in the course of insolvency proceedings. Such a creditor, usually the proprietor of an asset, is not formally a ranked creditor as such a creditor has no right or interest in the debtor's estate. However, the right to claim an asset may harm proceedings nevertheless if that very asset turns out to be essential for the continuation and possible restructuring (or sale) of the debtor's business. If a legal framework allows for retention of title clauses, proprietary rights indeed show all characteristics of a security right. Overall, it is the insolvency and restructuring regime governing the underlying (lease or purchase) agreements that commonly determines whether the proprietor may actually withdraw assets from the business (see Chapter 3).

408. A peculiar way to extract assets from the debtor's estate comes in the form of set-off rights or netting arrangements. Here, any creditor (secured or unsecured) may detract the

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[717] UNCITRAL Legislative Guide (2004), Recommendations 275-276.
[718] P.R. Wood, 'The Bankruptcy Ladder of Priorities', Business Law International, 209 et seq. For an extensive overview of some 20 countries all over the world, see D. Faber, N. Vermunt, J. Kilborn, T. Richter and I. Tirado, *Ranking and Priority of Creditors* (Oxford: Oxford University Press 2016). It is evident that for England this list is obvious incomplete as no place ir reserved for the prescribed part payable to unsecured creditors pursuant s.176A of the Insolvency Act 1986.
[719] Some countries provide a distinction between reorganisation and liquidation proceedings. For instance, in BE judicial reorganisation proceedings are not considered as a situation of *concursus creditorum*. They are subject to bankruptcy rules only in case of transfer of the enterprise under the supervision of a court. Reorganisation does not involve a ranking of creditors: n between creditors subject to a moratorium (pre-commencement claims) and not (into existence after the commencement). In France, ranking applicable to reorganisation resemble closely that valid for liquidation and is rarely applied in the practice, only when a particular asset is sold by competent trustee or where the business is sold as a going concern.
[720] Principles of European Insolvency Law (2003), § 12.2.

counterclaim of the debtor's estate (which is fully valuable) by netting it with their claims against an insolvent debtor. Jurisdictions commonly respect pre-commencement setoff rights. They also observe netting arrangements in financial contracts.

4.2.2 Creditors privileged by secured claims (pre-commencement privilege)

409. A preferential treatment of secured credit is common to all jurisdictions surveyed. All insolvency regimes in Europe respect security rights arrangements of the debtor as long as they are permitted under local civil (contract) law and do not constitute a fraudulent transfer of assets under respective insolvency law provisions. Overall, creditors may decide to *ex ante* mitigate the insolvency risks in their business relationship with the debtor by requiring the debtor to grant them a security right in the debtor's assets. Such a right in rem is generally able to fulfil its purpose as the creditor actually enjoys a preferential treatment based on and to the extent guaranteed by such a right in the case of an insolvency.

410. Security rights can be vested both on movables and immovable individually – by perfecting mortgages and pledges,[721] property liens,[722] other consensual securities[723] like the transfer of property and the assignment of rights for security purposes[724] – or collectively by way of floating charges[725] or collective transfers for security purposes.

411. Such security rights often rest upon a contractual agreement, but they may also have a statutory basis. The latter (non-consensual security rights) allow for the same preferential treatment as the former. Statutory liens are often granted to secure specific creditors whose power to negotiate security rights is limited, but who are held to be in need of protection (e.g. artisans or sailors). Instead of granting such creditors are general preference in the distribution of receivables, lawmakers secure sufficient protection in insolvency by perfecting a security interest on a specific set of assets.

412. Security rights protect the interest of the secured creditor in a cash payment from the debtor, often based on a credit or loan agreement. Thus, it is the value of the encumbered asset that is protected by security rights. Under insolvency (liquidation) rules, secured creditors may, therefore, not always request the transfer of encumbered assets, but only claim the receivables after all assets were sold in the course of liquidation proceedings.[726] In most jurisdictions, however, secured creditors are entitled to request the administrator to yield the relevant assets to them. By taking over the encumbered asset, the secured claim can be deemed fully satisfied. Some jurisdictions allow the secured creditor to file a deficiency claim if the proceeds of a sale do not fully cover the secured claim.[727]

413. The right which a security right provides in insolvency can be described for many jurisdictions by a ranking which sees secured claims ranked first.[728] In these jurisdictions,

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[721] These types of liens are common to all the jurisdictions in our project.
[722] See France, Italy, Poland or Sweden.
[723] See France and Italy.
[724] See Austria, Germany or Italy.
[725] See Belgium, Hungary, Sweden or England & Wales.
[726] See e.g. German Insolvency Code, s. 166 (for encumbered movables and assigned rights).
[727] See e.g. Belgium or Germany. See also UNCITRAL Legislative Guide (2004), Recommendation 188.
[728] See Austria, Germany, England & Wales, the Netherlands, Spain, or Sweden.

secured creditors can either detract encumbered assets or claim first ranking distribution of proceeds of a sale of these assets. Such a priority for secured credit results a problem for all other creditors, however. In an economy where all available assets are made available for secured credit, little to no unencumbered assets are left in the estate of the debtor when an insolvency proceeding commences. The lack of unencumbered assets is difficult for all those jurisdictions in particular that require sufficient assets to cover the costs of proceedings to even commence insolvency proceedings in the first place. In response to this effect, some jurisdictions deduct up to 10 percent from the proceeds of a sale of encumbered assets to cover the costs of proceedings.[729] If the deduction exceeds the costs, any surplus may be distributed to other (unsecured) creditors.

414. The widespread use of security rights does, however, not only jeopardize the commencement of insolvency proceedings by causing the insufficiency of the estate to cover their costs. It also endangers the success of commenced insolvency or restructuring proceedings as such procedures require additional interim finance if a business is still running and to be rescued. And last, but not least, new finance is also essential to implement restructuring means after a successful conclusion of restructuring proceedings. For all these types of finance, credit is required and may only be available if the debtor (or administrator) is able to grant security rights, which again is difficult if the debtor has no unencumbered assets left. By now, only very few jurisdictions have specifically addressed the issue of supporting interim (or DIP) and rescue financing (see Chapter 2). If so, a well-known solution is to allow a court to authorise new first ranking security rights on already encumbered assets ("super-priority") if the debtor is unable to obtain credit otherwise and the interest of the impaired secured creditor is adequately protected.[730] In France, financial agreements in a ratified conciliation agreement enjoy a conciliation privilege in a subsequent insolvency by being paid ahead of secured creditors from the proceeds of asset sales.

4.2.3 Creditors privileged by insolvency rules on distribution (post-commencement privilege)

415. Legislators may not only grant the privilege of being paid before the general class of creditors by accepting pre-commencement agreements or statutory provisions securing such a legal position (security rights). Alternatively, lawmakers may include such a privilege directly in the rules on the distribution of proceeds of an insolvency liquidation (post-commencement privilege).[731] Our reports show that all jurisdictions have provided for both types of privileges.

416. Commonly, such a privilege is attributed to claims resulting from the administration of the insolvency proceedings (costs of proceedings) and the debtor's estate (administrative

[729] See Belgium, Germany, Hungary or Poland. Under English law, a floating charge may cover all assets, but in cases with an insufficient estate to cover costs and preferential claims, these claims take priority. In addition, a "prescribed part" of encumbered net value up to £600,000 overall must be made available for the satisfaction of unsecured debts.

[730] See the original provision in the US Bankruptcy Code s 364 (d).

[731] See also the definition of Vanessa Finch, *Corporate Insolvency Law Perspectives and Principles* (Cambridge University Press 2002), p. 425: "Preferential debts are unsecured debts which, by force of statute, fall to be paid in a winding up in priority to all other unsecured debts but which abate rateably as among themselves."

expenses[732]), in particular in cases with an ongoing concern of the business.[733] While claims for procedural costs (fees for the court and the insolvency office holder) may even interfere with secured claims (see above), post-commencement claims resulting from the administration of the estate are commonly to be paid first[734] from liquidation proceeds of the unencumbered estate. In addition, such claims are not affected by a moratorium or stay. Such a full payment guarantee is particularly important in restructuring and insolvency cases involving an ongoing business because suppliers, employees and other key business partners would only continue their cooperation with the debtor's business if they can trust in continued payments despite the commencement of proceedings. The only limit to this guarantee is the possible insufficiency of the estate to even cover such preferred claims. In that case, an order of priority for different classes of expenses may give further reassurance to important creditors.[735]

417. Principle C 16.2 of the 2016 World Bank Principles for Effective Creditor/Debtor Regimes suggests an insolvency law system should permit an enterprise group member subject to insolvency proceedings to provide or facilitate post-commencement finance or other kind of financial assistance to other enterprises in the group which are also subject to insolvency proceedings.[736] This Principle further provides that the insolvency law system should specify the priority accorded to such post-commencement finance.[737] Similarly, the UNCITRAL Legislative Guide on Insolvency Law also recommends that the insolvency law should establish the priority that may be accorded to post-commencement finance, ensuring at least the payment of the post-commencement finance provider ahead of ordinary unsecured creditors, including those unsecured creditors with administrative priority.[738]

418. In addition to *post*-commencement claims (administrative expenses), there is a common practice of providing for the preferential treatment of specific classes of *pre*-commencement creditors. With the sole exception of Germany, all national correspondents to our project report that their laws contain such kind of a privilege in order to protect various policy interests (mostly social and fiscal). Most common is a preferential treatment of claims for unpaid taxes[739] and employee salaries[740]. Some jurisdictions (like for instance Belgium or Sweden) have developed a very detailed system of preferences while other have substantially reduced the number of preferential classes of creditors (see e.g. England &

[732] They may comprise management and liquidation costs, post-commencement creditor claims from new contracts entered into by insolvency office holder (or debtor in possession) or assigned executory contracts (like e.g. employees' salaries).

[733] The only exception is Hungary where post-commencement claims are treated as pre-commencement ones including a duty to file the claim within a strict deadline.

[734] After all procedural costs are deducted. In France, they are paid only after super-preferential 60-day wage claims.

[735] See e.g. Austria, England & Wales, Germany or Spain. See also the Principles of European Insolvency Law § 6.3.

[736] World Bank Principles (2016), Principle C 16.2.

[737] World Bank Principles (2016), Principle C 16.2.

[738] UNCITRAL Legislative Guide (2004), Recommendation 119.

[739] See e.g. Belgium, Greece, Hungary, Latvia, the Netherlands or Poland.

[740] See all jurisdictions covered in our report except for Austria and Germany. Such a preference for employee claims is also recommended in the Principles of European Insolvency Law (2003), § 7.2. In the World Bank Principles (2016), Principle C12.4 recommends "balancing the rights of employees with those of other creditors."

Wales). Often, the preference gives the right to be paid ahead of other unsecured creditors out of the liquidation proceeds from all unencumbered assets of the estate. Sometimes, preferred creditors may only claim proceeds from a certain set of assets of the estate.[741]

4.2.4 Ordinary creditors

419. Pre-commencement creditors without a pre- or post-commencement privilege (security right or insolvency law privilege) are ordinary creditors and awarded a *pari passu* ranking among each other, so that they are satisfied equally pro rata from the remaining receivables of the estate.

4.2.5 Subordinated creditors

420. All jurisdictions (except for France) rank some classes of claims to be paid from the proceeds of the proceedings only after all ordinary claims have been paid in full. Such subordinated or deferred creditors can usually not expect to receive anything on behalf of their claims in insolvency proceedings where, by definition, the estate does not suffice to cover all ordinary claims. They may, however, expect a payment in a restructuring if such proceedings are to commence in timely manner.

421. Claims may be subordinated by virtue of law, court decision or contract. The policy underlying a statutory subordination may vary. Often, post-commencement interest and contractual late payment fines on ordinary claims are first ranking subordinated claims.[742] In several jurisdictions, shareholders are paid last in insolvency liquidation just as they would in company law liquidation. The subordination of shareholders often not only includes claims arising from membership, but also from other independent contracts (so-called: shareholder loans).[743] It may also extend to claims of company insiders like directors or relatives of the debtor, of company directors and shareholders.[744]

422. Our Inventory Reports indicate that there is no common treatment of subordination agreements. While such agreements are the only ground for subordination in some jurisdictions (like the Netherlands), they are held contrary to public policy and therefore ineffective in others (like England & Wales). In a number of jurisdictions, subordination agreements between unsecured creditors are valid and effective.[745]

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[741] See, for instance, Belgium where privileged tax authorities, employees and social security agencies may only claim proceeds from the totality of movable assets.

[742] See England & Wales, Germany, the Netherlands or Latvia.

[743] See Hungary. See also Germany or Poland where shareholder loans with limited liability companies are subordinated. In Italy shareholder loans with limited liability companies and with joint-stock companies are also subordinated, provided that, for instance, they were made in a company situation which should have required an equity injection instead). Also see England & Wales where only claims arising from membership are deferred.

[744] See Hungary, also Spain.

[745] See e.g. Austria, Belgium, Germany, the Netherlands or Poland. In Austria and the Netherlands, subordination may also result from a unilateral declaration of the creditor. In Belgium, a ranking agreement may also be stipulated between secured creditors.

4.3 Impetus for recommendations on ranking

423. It is a fundamental principle of insolvency law that pre-insolvency entitlements of creditors should be respected by insolvency and restructuring rules on distribution unless there are legitimate grounds to a post-commencement redistribution of value.[746] Thus, secured transactions should be upheld and honoured in the course of insolvency and restructuring proceedings on principle.[747] Secured creditors should be able to rely on the value of their collateral.[748] Any deviation under insolvency law must be justified on the basis of a specific legitimate interest, clearly defined and allow each creditor to predict and calculate ex ante their legal position in a possible future insolvency of their debtor. For the same reason, the pari passu principle does not comprise a proportional distribution amongst all creditors, but only amongst those alike (in the same distributional rank).[749]

424. A first legitimate interest of insolvency and restructuring law is to guarantee orderly procedures by securing the payment of costs to all actors, that contribute to a restructuring or an insolvency proceeding, in particular courts and insolvency office holders involved.[750] Their high quality professional work safeguards the rights of all stakeholders in the debtor's (near) insolvency and it is not available pro bono (see above Chapter 1.3.) which is why their fees should not be paid from taxpayer money as long as there are (encumbered) assets available in the estate. Lawmakers could grant a general super-priority for fees[751], but such a general rule would leave some level of ambiguity about the involvement of secured credit. Instead, a clear and predictable deduction from the proceeds of the sale of encumbered assets would secure a pool of cash in each procedure to pay fees and, if sufficiently large, to cover other administrative expenses or even a minimal distribution to ordinary creditors. In a world of ever present secured transactions and debtor estates with few to none unencumbered assets, a general deduction of up to 10 per cent of the receivables from the sale of all or at least some (e.g. movable) collateral should be considered a fair price for

[746] Overall, this principle should be commonly accepted. There is, of course, a much debated dispute amongst scholars about the legitimacy of redistribution effects – with the creditor's bargain theory arguing that there is no good reason for redistribution but the hypothetical creditors' decision to do so (see Thomas H. Jackson, 'Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain', 91 Yale L.J. 1982, p. 858; Thomas H. Jackson, *The Logic and Limits of Bankruptcy Law* (Harvard University Press 1986), and many traditionalists arguing that insolvency law has always played and should always play a redistribution role because the insolvency of a (company) debtor affects more stakeholders than only common pool creditors and that such insolvency related conflicts must be addressed by insolvency law as well; see e.g. Roy Goode, *Principles of Corporate Insolvency Law* (4th edn, Sweet & Maxwell 2011) p. 2-17.

[747] World Bank Principles (2016), Principle C12.2; UNCITRAL Legislative Guide (2004), Recommendation 188.

[748] It has also been argued that bank debt should always be senior debt to reduce ex post expenses for the (re)assessment of priorities; see Ivo Welch, 'Why Is Bank Debt Senior? A Theory of Asymmetry and Claim Priority Based on Influence Costs', 4 Review of Financial Studies 1203 (1997). In practice, however, the general power of banks to negotiate secured loans should sufficiently secure all advantages shown in the model.

[749] See Rizwaan Jameel Mokal, 'At the Intersection of Property and Insolvency: The Insolvent Company's Encumbered Assets', University College London Law Legal Studies Research Paper No. 09-01, 2008, p. 25-27, available at https://ssrn.com/abstract=1112309.

[750] In jurisdictions that allow a creditor to act in the common interest like an officer to the court, the reimbursement of costs of such acts may also deserve protection; see Steven Haag, 'Creditor-led Schemes of Arrangement: The Creditor as Claimant', International Corporate Rescue 2014/3.

[751] Such a privilege may also include the fees of the members of a creditor's committee if the respective legal regime gives them a central role in protecting the rights of all creditors instead of only their own interests; see e.g. Germany where such a committee supervises the insolvency practitioner and confirms the sale of assets.

secured creditors to pay in exchange for an orderly procedure that respects their rights and secures their enforcement.[752]

425. A second legitimate ground for limited inference with secured credit under insolvency and restructuring law is built on the fact that in cases with an ongoing business of the debtor a restructuring or even a sale of the business as a unit is able to generate the going concern value of that business which usually means a higher return for creditors than the receivables from a piecemeal liquidation. A restructuring as well as a going concern sale are only achievable, however, if the assets forming the business are not torn apart at the outset of proceedings by secured creditors who are enforcing their pre-commencement legal rights with regard to these assets.[753] In order to preserve a going concern value, the enforcement of secured claims should be deferred until the value is either generated (in a sale or restructuring plan) or gets out of reach. This does not mean that there always needs to be an automatic stay following the commencement of proceedings (which is commonly the case in formal insolvency and restructuring proceedings, at least against unsecured creditors; see above Chapter 2). The availability of an individual stay of the enforcement actions of relevant creditors would suffice (in particular in pre-insolvency proceedings; see above Chapter 1.2).

426. The common interest in securing the going concern value of the debtor's business would also justify a third type of deviation from pre-insolvency entitlements: the common legislation that gives administrative expenses a priority over ordinary claims. Costs that result from efforts to organise and orderly liquidate all assets in the estate (in a going concern sale as well as in a piecemeal auction process) or even reorganise the debtor's business are usually meant to maximise the realized value and would, therefore, be in the interest of all creditors. As a consequence, they should be paid ahead of them. The risk of such a privilege – an insolvency practitioner or debtor in possession carelessly producing expenses – should be addressed by a personal liability of the acting individual.

427. The widespread use of general preferences for specific classes of claims for social or fiscal policy reasons does not seem justified. While there may be a good policy reason to protect these types of ordinary creditors in insolvency, such preferences provide little actual relief in a world of insolvency cases with no or very few unencumbered assets and, therefore, very little to no money to actually distribute to preferred creditors. If lawmakers respond to this situation by ranking such creditors higher than secured creditors (see e.g. the French super-priority for unpaid employee salary), they badly impair the market for secured credit because it is difficult to ex ante predict the extent of super-preferred claims in a future insolvency and, thus, almost impossible to precisely calculate credit risks which usually makes credit more expensive. Instead, lawmakers should refrain from granting additional general preferences[754] and turn to other means of protection.[755] Employee's rights to be

[752] See also Rizwaan Jameel Mokal, *What Liquidation Does For Secured Creditors, And What It Does For You*, 71 Mod. L. Rev. 2008, 699, p. 711-712.

[753] This argument also applies to parties with similar rights such as counterparties to the debtor enforcing a retention of title.

[754] Such restraint is also recommended in international standards, see UNCITRAL Legislative Guide (2004), Recommendation 187, or World Bank Principles (2016), Principle 12.3.

[755] With Mucciarelli (Federico M. Mucciarelli, 'Not Just Effficiency: Insolvency Law in the EU and Its Political Dimension', 14 EBOR 2013, 175), we note that creditors' priorities have a distributive impact on creditors. As

paid can be sufficiently protected by insurance-type guarantee schemes safeguarding the payment of outstanding salary claims (see below in Chapter 5). The interests of specific social groups (like artisans, farmers, fishermen, dock workers, individuals injured by the debtor, etc.) could also be protected outside of insolvency proceedings. If they were to enjoy a privilege in insolvency, lawmakers should choose to grant them a statutory pre-insolvency security right in specific assets[756] instead of a general preference in a distribution.[757] Such a privilege is not only more efficient, it is also more consistent with the general principles of insolvency law (respecting pre-commencement entitlements) and with the functioning of the credit market (publicity, priority). Whether it should be extended to protect fiscal interests of the state (unpaid tax claims) is debatable. Generally, the state enjoys sufficient non-insolvency preference given the ability to quickly enforce tax claims without the need of obtaining a judgement. Additional protection seems hard to justify with respect to other creditors.[758] In practice, recovering the full amount (sometimes including fines) of social of fiscal claims is fully at odds with a sturdy support of a business rescue policy. Continuation of viable businesses and – thereby also – continuation of employment requires more flexible social and fiscal policies.[759]

428. In general, any more widespread use of security agreements and statutory liens must be considered carefully with its effect on business rescue options. Preferences must not hinder the restructuring of the debtor's business if that allows all stakeholders to do better collectively than they would do in an immediate liquidation. If the credit today is often

we have indicated, distributional rules many times reflect the hierarchies of values and interests in each jurisdiction. For this reason priorities certainly have a high political relevance. Mucciarelli – in an EU cross-border context – submits that they pose an obstacle to reforming the European Insolvency Regulation (2000) as changes will indirectly modify national social security strategies and equilibria: '… the choice regarding power allocation over bankruptcies in the EU depends on the progress of European integration and is mainly a matter of political legitimacy, not only of efficiency.' We submit that the same is true in efforts to approximate matters of national restructuring and insolvency laws.

[756] Such statutory pledges would preferable be placed on unencumbered assets close to such groups like, for instance, products they produce. They could also encumber specific future assets of the debtor, if necessary, ranking ahead of future security right for a contract creditor.

[757] There are numerous examples for this way of constructing a protection, see e.g. pledges for haulers or shippers, stock keepers under German commercial law; see Jan Felix Hoffmann, *Prioritätsgrundsatz und Gläubigergleichbehandlung* (Mohr Siebeck 2016) p. 304.

[758] Anto Kasak, 'Which types of claims should be preferred in insolvency proceedings', Corporate Rescue and Insolvency 2012, p. 178, 179.

[759] This view finds support in case law of the Court of Justice of the EU. In a VAT matter (to which the VAT Directive 2006/112/EC is applicable) in the context of an arrangement presented to creditors by the insolvent debtor, the CJEU responded on 7 April 2016, Case C 546/14 (C 546/14 *Degano Trasporti Sas di Ferruccio Degano & C., in liquidation, v Pubblico Ministero presso il Tribunale di Udine* EU:C:2016:206) to the question of the District Court of Udine asking whether the obligation on Member States to take all legislative and administrative measures appropriate for the full recovery of VAT, laid down by EU law, in fact prevents the use of collective proceedings other than insolvency liquidation, under which the insolvent trader liquidates all of its assets to satisfy its creditors and envisages settling its VAT debt in an amount which is no less than what that trader would pay in the event of bankruptcy. The CJEU ruled that Article 4(3) TEU (sincere cooperation between Member States) and certain specified articles of Directive 2006/112/EC on the common system of value added tax do not preclude that national legislation, such as that at issue in the main proceedings, must be interpreted as meaning that an insolvent trader may apply to a court to open a procedure for an arrangement with creditors for the purpose of settling its debts by liquidating its assets, in which that trader offers only partial payment of a VAT debt and establishes by an independent expert's report that that debt would not be repaid more fully in the event of that trader's bankruptcy. We submit that in general tax rules should not be applied rigidly.

secured credit, restructuring law must provide for means to restructuring secured credit as efficient as unsecured credit. If jurisdictions provide for a range of preferred pre-commencement claims, such claims should be available for a restructuring as well. Thus, restructuring plans should be able to include and to modify the entitlements of secured and preferred pre-commencement creditors (for more details see below Chapter 8).

4.4 Governance by creditors

429. Each and every type of a restructuring or insolvency procedure involves the legal rights of all or at least some creditors. It is the very meaning of the term *concursus* that creditors come together. As a consequence, it seems obvious to give the body of creditors a voice in such proceedings, maybe even a dominating voice. As insolvency and restructuring proceedings frequently involve a multitude of creditors, their participation is commonly organised by convening general meetings of creditors (see below 4.2.1) and by establishing standing creditors' committees (see below 4.2.2).

4.4.1 General meetings of creditors

430. For insolvency proceedings, a general meeting of creditors is commonly[760] convened within a specified period of time after the commencement of proceedings.[761] Additional meetings (interim meetings) may be summoned at the court's discretion or at the (qualified) request of creditors.[762] Some jurisdictions also provide for a mandatory closing meeting at the end of proceeding to have the insolvency practitioner present his final report.[763]

431. A general meeting of creditors convenes all ordinary creditors of the debtor. Creditors with secured claims or preferences are frequently barred from such meetings or at least from voting.[764] The competences of such meetings encompass, *inter alia*, the verification of claims, the replacement of insolvency administrator, the appointment of a creditors' committee, the decision about a continuation of business activity, information inquiries, and the consent to a sale of debtor's business. Many jurisdictions also assign the central task of approving a restructuring or insolvency plan to the general creditors' meeting (for a detailed analysis see below chapter 8).

432. The general meeting of creditors makes a decision by casting votes. Where the meeting is also authorised to vote on a restructuring or insolvency plan, specific voting rules may apply (for a detailed analysis see below chapter 8). Other issues commonly require a majority of creditors holding more than 50 percent of the aggregate claims of the creditors present and voting at the creditors' meeting.[765]

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[760] Such rules reflect international standards, see UNCITRAL Legislative Guide (2004), Recommendation 128.
[761] See e.g. Austria, Germany, England & Wales (with different deadlines for the various types of proceedings available), Greece, Hungary, Italy (for the concordato preventivo), the Netherlands or Sweden.
[762] See e.g. Austria, Belgium, France or Germany.
[763] See Belgium or Germany.
[764] See Germany, Italy or England & Wales.
[765] See e.g. Austria, Germany, England & Wales. A remarkable exception is Belgium where no formal voting procedures exist, because no formal decisions are adopted in such meetings.

4.4.2 Creditors' committee

433. It is widely recognised that the interests of relevant creditors may be best served by coordinating their response to a debtor in financial difficulty through the establishment of (at least) one representative committee of creditors.[766] The establishment of such a committee is held to facilitate the active participation of creditors in insolvency proceedings[767], and to ensure fairness and integrity of proceedings.[768] They also contribute significantly to the supervision of the activity of the insolvency practitioner or debtor in possession, considering the progress and quality of their work while, at the same, time avoiding wasteful interferences.[769]

434. Considering the sometimes complexity of organising a creditors' committee and its potential costs, jurisdictions often only allow for the establishment of one committee[770] which again may be optional in smaller cases.[771] Only a few jurisdictions do not allow for such a committee at all[772] while some even provide for more than one committee in a case.[773]

435. If a creditors' committee is established, it commonly assumes the following rights and functions:[774]

- Providing advice and assistance to the insolvency practitioner or to the debtor (in possession);
- Assisting in the development of a restructuring or insolvency plan;
- Right to appear and be heard in proceedings, in particular concerning decisions out of the ordinary course of the debtor's business;
- Requesting relevant and necessary information from the debtor or the insolvency practitioner at any time during the proceedings.

436. Overall, the basic function of such committees is of a supervisory and advisory nature.[775] Only some jurisdictions extend the committee's role to decisions on substantive matters: under English law, the committee fixes and reviews the remuneration of the insolvency administrator. Following a German law tradition, the committee's approval of decisions or transactions which are essential for the course of proceedings is required in

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766 Principles of European Insolvency Law (2003), Principle 2.4; see also INSOL International Workout Principles II (2017), Principle 4, and Asian Bankers Association's Workout Guidelines (2013) for informal workouts.
767 UNCITRAL Legislative Guide (2004), Recommendation 129.
768 World Bank Principles (2016), Principle C7.1.
769 EBRD IOH Principles (2007), Principle 7(b).
770 See Austria, England & Wales, Germany, Hungary, Italy, Poland, Sweden (composition proceedings).
771 See Austria, France or Germany. See also chapter 10 for a specific treatment of small business cases.
772 See Belgium. Latvia and Spain. Here, private forms of creditor cooperation may exist (Latvia). In Greece, recent law reform lifted the requirement to install a committee, but allowed the general meeting of creditors to appoint one.
773 Under French law, two separate creditors' committee are established in bigger cases, one for financial and related credit institutions and another for the main suppliers of gods and services, with the possibility of a third committee for bondholders. In small cases, however, creditor interest is only represented by a creditors' representative appointed by the court.
774 UNCITRAL Legislative Guide (2004), Recommendation 133; see also World Bank Principles (2016), Principle C7.2.
775 In the Netherlands and Sweden, the role of a committee is confined to a consulting role.

Germany, Austria, Hungary and Italy, including a decision to sell or discontinue the debtor's business.

437. The members of the creditors' committee shall represent the whole body of creditors. In order to ensure a representative election of members, the appointment of committee members is either done by the court[776] or an election process in a general meeting of creditors.[777] Both appointment mechanisms are supported in international standards.[778] The number of members to be appointed must not only consider the wish for a representative group of creditors, but also aspects of cost-efficiency which has prompted most jurisdictions to limit the number of members from three to seven. Some require the representation of specific creditor groups like employees,[779] secured, preferential and ordinary creditors,[780] credit institutions or key suppliers.[781] Appointed committee members assume the duty to faithfully perform the functions of their office. In case of wrongdoing, most jurisdictions[782] allow for a personal liability[783] either based on express provisions in respective insolvency law or by applying rules of contract law[784] or rules for internal auditors.[785] The threshold of liability may vary as well.[786] In exchange for their efforts and liability risks, committee members receive a (modest) remuneration only in a few countries.[787] Most jurisdictions limit payments to the reimbursement of expenses[788] or provide for additional remuneration only in complex cases.[789]

4.4.3 Impetus for recommendations

438. Creditors should play a crucial role in insolvency and restructuring proceedings. After all it is their money which is at stake as they would receive a higher or lower payoff on their claims if proceedings are run well or badly. The widespread practice of respecting the common creditors' interest by establishing creditors' committees or mandating a general meeting is capable of securing a direct involvement of creditors in proceedings.

439. At the same time, such steps are not indicated in all proceedings. General meetings are only able to attract representatives from all creditor classes if all creditors feel that participating is in their best interest and worth the effort. If there is no expectation of a significant distribution on their behalf, it is rational for subordinated, unsecured or – in small cases – even preferential creditors to not participate at all because additional costs of participation would accrue no advantage. For the same reasons, the establishment of

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776 See Austria, Germany, the Netherlands, Italy or Sweden.
777 See England & Wales, Greece and Hungary.
778 See UNCITRAL Legislative Guide (2004), Recommendation 132.
779 See Germany and Sweden.
780 See Greece, but also Germany (for the participation of secured credit).
781 See France.
782 Exceptions to this rule are found in French and Swedish law.
783 This is in line with international standards, see UNCITRAL Legislative Guide (2004), Recommendation 135.
784 See Hungary.
785 See Italy.
786 From a liability for every type of negligence (e.g. in Austria or Germany) to a liability limited to cases of malice or gross negligence (see Greece)
787 See Germany, in particular. See also Hungary or Italy where creditors need to agree on a remuneration.
788 See e.g. Austria or England & Wales.
789 See Poland.

creditors' committees would not seem efficient if the overall costs of their involvement are not justified by the economic relevance of their decisions. Overall, a distinguished approach would seem best fitted.

440. In a (type 1)[790] pre-insolvency procedure (workout support proceeding), only affected creditors are involved to negotiate and to vote on a restructuring proposal. In such proceedings, a general meeting of all creditors, including not affected ones, does not seem appropriate. Setting up a creditors' committee is also not required if the group of affected creditors is small anyway (e.g. key financial creditors or lessors). In bigger restructurings, setting one or even more committees may be useful and should be an option in a workout. Still, they would not play a specific role in the short confirmation procedure in court.

441. In formal restructuring or insolvency proceedings, all creditors are affected. The collective nature of such procedures principally justifies securing the information and participation of all creditors by way of one or more general meetings. The issue of rational passivity of many creditors should be addressed by designing cost-efficient ways to attend such meetings. In small cases with a limited number of creditors, no physical meeting should be required. Instead, a meeting could be held in a conference call. If there is a physical meeting, creditors should be allowed and able to attend such meetings online including a remote vote. At the same time, setting up a creditors' committee would establish a standing creditors' body capable of directly interacting with and supervising the insolvency practitioner or debtor in possession. Such a committee could also approve sensitive decisions (e.g. a sale of significant parts of the estate[791] or a risky litigation); if so, committee members should not be liable for risk taking, but only for acts of bad faith or gross negligence. Committee members should also receive an adequate remuneration from creditors for their work, preferably by way of a preferential payment of adequate fees from the estate. In smaller cases with insufficient estates, creditor committees should not be established.

4.5. Recommendations

Recommendations on ranking of creditors

Recommendation 4.01: Member States should, in principle, respect pre-insolvency entitlements under their insolvency and restructuring law regimes unless there are legitimate grounds to a post-commencement preference.

Recommendation 4.02: Member States should ensure that classes of creditors are specified in clear terms, in particular identifying those creditors enjoying the right to be satisfied in a specified priority.

Recommendation 4.03: Member States should ensure the very commencement of orderly and efficient restructuring and insolvency proceedings by securing the payment of fees for the courts and insolvency office holders involved. While no assets cases should be financed by public funds, secured creditors should contribute to cover costs in other cases by

[790] See Chapter 1.2.

[791] See Chapter 9.

introducing a clear and predictable deduction rule, e.g. a general deduction up to 10 per cent.

Recommendation 4.04: Member States should refrain from granting additional general preferences for specific groups of creditors in favour of other means of protection of social interests (e.g. insurance or guarantee schemes, statutory liens on specific assets). The actual need for protection should be scrutinised thoroughly, in particular the protection of fiscal interests, and be primarily determined by their general impact on rescue efforts.

Recommendation 4.05: Member States should ensure that their insolvency and restructuring framework comprises sufficient means to restructure secured credit as well as unsecured credit, meaning that restructuring plans should be able to include and to modify the entitlements of secured creditors.

Recommendations on organisation of creditors

Recommendation 4.06: Member States should ensure that in workout-support proceedings a general meeting of creditors is not required and the establishment of creditors' committees is only an option in order to structure complex workout negotiations.

Recommendation 4.07: Member States should provide for a general meeting of creditors in formal restructuring or insolvency proceedings. Member States should allow for virtual meetings or online participation (including online voting).

Recommendation 4.08: Member States should secure the involvement of a creditors' committee in formal restructuring or insolvency proceedings provided that there are sufficient assets in the estate to justify the additional costs. Such a creditors' committee should not only have a supervisory function, but also be competent to approve decisions in the administration of the estate that may have a significant effect in the later distribution (except the decision about a restructuring or insolvency plan which is governed by separate rules).

Chapter 5:
Labour, benefit and pension issues

442. The insolvency of a business is a situation in which losses need to be distributed amongst creditors and stakeholders. While the possibility and probability of an insolvency is calculated and covered by some creditors, other creditors are hit harder by suffering a write-off on their claims in the course of an insolvency process. The latter is especially true for employees and pensioners depending on the solvency of their (former) employer. Their limited capacity to suffer losses has prompted a special treatment of these stakeholders and, therefore, requires a specific analysis.

5.1 Employment contracts

443. Employees comprise a special group of stakeholders in a business insolvency for several reasons. On the one hand, they are contractually connected to the debtor – their employer – and take the legal position of unsecured creditors if salaries were left unpaid prior to the commencement of legal proceedings. As creditors, employees are a peculiar group because, in general, their livelihood typically depends on their salary, which gives them little space for a write-off in rescue negotiations. Still, despite their dire interest in protecting their salary and their close – often personal – connection to their employer, employees are usually not in a position to negotiate any protection of their salary claims during the regular course of business (ex ante), which is why they remain in the vulnerable position of unsecured creditors in insolvency proceedings.

444. On the other hand, employees can also be considered as "investors" in the business as they adjust their skills, as well as their career plan, to the specific conditions and opportunities of "their" business and their individual workplace. Such an individual skill set may not be easily transferable to new employers at all or at the same level of wage which incentivises employees to cling to their contracts if possible.

445. The investor perspective may also prompt employees to actually invest in the business in terms of a management buy-out or financial investments, in particular in cases of small businesses.

446. The very specific connection to the business leads employees occupying a peculiar position in their employer's insolvency, one widely held to be worth specific statutory protection,[792] and it has been the European Union who picked up this task partially and provided for a minimum standard of harmonised protection across EU Member States in some aspects by way of directives. Due to this development, the treatment of labour contracts and claims in insolvency proceedings does show some level of harmonisation already.

[792] See World Bank Principles (2016), C10.4 and C12.4.

5.1.1 Special provisions for the treatment of employment contracts or collective agreements

447. While harmonised law is in effect in other areas of employee rights in insolvency, there is no harmonised law yet with regard to the treatment of employment contracts and collective agreements in insolvency or restructuring proceedings. Nonetheless, there are some common principles.

5.1.1.1 Protection and termination of the employment contract

448. As a basic rule in all analysed jurisdictions, the filing as well as the later commencement of insolvency proceedings does not automatically terminate employment contracts of the insolvent employer because such contracts are still pending performance from both sides at that moment. For that reason, they are executory contracts, and the legal regime governing such contracts in a respective jurisdiction applies.[793]

449. The initial insolvency remoteness of employment contracts does not mean, however, that such contracts enjoy a strong protection. Economic pressures that caused the distress of the business typically will influence the operations of the debtor and, thus, often require a reduction of the workforce according to the restructuring scheme. In case of a liquidation, all workforce is typically redundant. Insolvency laws in all Member States respond to this fact by authorizing the IP or DIP as part of their power to administer the debtor's estate to terminate employment contracts.[794] While some local insolvency rules provide for a limited period of time (Belgium: 15 days; UK: 14 days) for the IP/DIP (and the employee)[795] to decide about the ongoing continuation of employment contracts where no decision may be interpreted as adoption (UK) or rejection (Belgium) of the contract,[796] others order an automatic continuation (Germany) accompanied by the unlimited right to terminate the contract and a shortened notification period of a maximum of six weeks (Netherlands) or a one (Austria, Poland) or three month maximum (Germany).[797] Some jurisdictions provide for neither a termination no a notification period which means that the general rules under applicable labour or contract law apply (Belgium) or that terminations are effective immediately but depended on a prior court approval (Spain, France[798]). Under Greek labour and insolvency law, open-ended employment contracts may be terminated anytime by notifying the employee in writing and paying the statutory compensation – a preferential claim in a liquidation.

450. A recent empirical study of 26 cases in the Netherlands revealed that none of the cases examined had indicated that insolvency had been requested for the purpose of only a remediation of (part of) the staff. In only two of the 26 cases in this research (both

[793] See Chapter 3 for more details on executory contracts.

[794] This finding is in line with the Principles of European Insolvency Law (2003) that state in § 7.1: '*The administrator or the employee may terminate a contract of employment following special rules.*'

[795] In some jurisdiction exists specific termination periods for employees – see e.g. Austria.

[796] In France, it's a 15 days period starting with the termination order of the court; in a judicial reorganisation, there is no period but a consultation and court approval requirement for redundancies.

[797] In Germany, this right also extends to work place agreements ("*Betriebsvereinbarungen*") between the employer and all employees in an establishment (see German Insolvency Code s 120).

[798] Here, consultations and court approval for redundancies are required in advance in a reorganisation case.

companies were active in the secondment of staff) it was found that the employment status of employees had been decisive for the specific follow-up of the case. In the other cases, the problematic financial situation was caused by entirely different factors than labour costs.[799] However, the ability to release employees from work and to terminate employment contracts is an essential tool when winding up an insolvent business. It can, however, also be used to sell or restructure a business and continue it by doing so. Many of the analysed jurisdictions (see above) do not differentiate a liquidation with a going-concern sale from a piecemeal liquidation and generally suspend their labour law protection rules to a certain extent whenever an employment contract is being terminated by an insolvency practitioner in the course of formal insolvency proceedings. Some jurisdictions, however, limit the facilitated termination right of an IP to redundancies in discontinued parts of the business (Austria) or to piecemeal liquidations (Poland) in an attempt to strike a balance between the interests of a business rescue and those of dismissed employees. In others (Germany), statutory protection against unfair dismissal remains applicable in principle but is rendered ineffective in most liquidation cases where all jobs are lost and, thus, any protection against unfair dismissal is irrelevant.

451. During workout support and restructuring proceedings as well as at the implementation stage of a restructuring plan, however, labour law protections usually are in place unaltered.[800] This may restrict the capacity of the debtor to reduce the workforce in jurisdictions having restrictive labour law rules on termination rights (see complaints in e.g. Germany). Some jurisdictions allow for facilitated redundancies in discontinued part of the debtor's business in pre-insolvency proceedings (Austria). In France, the DIRECCTE administration agreed to grant temporary lay-off measures to companies undergoing safeguard or reorganization proceedings, as well as to business buyers, pending either a subsequent restructuring or a turnaround of the business further to the sale. Some jurisdictions allow for collective agreements outside of court proceedings that aim at a business rescue. In Italy, several tools like collective agreements ("*contratti di solidarietà difensivi*") or wage payments by an extraordinary wage supplementation fund ("*Cassa Integrazione Guadagni Straordinaria*") aim at overcoming a business crisis even before entering pre-insolvency proceedings. Polish labour law allows for the suspension of collective bargaining agreements in that very timeframe.

452. Some Inventory Reports[801] indicate that there is a practice to circumvent the rigidness of local labour law by using a contractual language that aims at not fulfilling the definition of an employment contract. Whenever this is successful under local jurisdiction, such contracts do not receive any specific protection in case of an insolvency.

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[799] L.G. Verburg, P.M. Veder et.al., *Ondernemingen in financiële moeilijkheden en de arbeidsrechtelijke positie van hun werknemers,* (Rapport aan het WODC uitgebracht door Onderzoekcentrum Onderneming & Recht, Radboud Universiteit Nijmegen, april 2016, Kenmerk WODC: 2599/624436/15). For a summary in English, see https://www.wodc.nl/binaries/2599-summary_tcm28-74090.pdf.

[800] See Belgium, Germany, Greece, France, England &Wales, basically also the Netherlands.

[801] See e.g. Poland. Based on our interviews and conference discussions, this issue appears to be a common problem.

5.1.1.2 Right to be informed timely

453. The business failure of their employer does affect employees not only as creditors but also as "investors". They invested their workforce and adjusted their skills to the need of their employer. If this investment becomes questionable due to the business failure, employees must be able to reconsider their investment decision. They must be able to test their chances on the job market and may consider to work somewhere else. They must also be allowed to reinvest in "their" business by negotiating new conditions to their employment contracts (lower wages, less additional benefits) or by negotiating direct contributions to their employers' business (management buy-out; financial investments). All such decision-making requires information being delivered fully, unconditionally and timely.[802]

454. In recognition of the overall importance of a timely notice about changes in the organisation of the employer's business, the EU has enacted two directives that provide for a minimum harmonisation of employee rights to be informed.

455. Under Directive 2002/14/EC,[803] Member States must "establish a general framework setting out minimum requirements for the right to information and consultation of employees in undertakings or establishments within the Community."[804] It would also cover a duty to inform about relevant changes in the economic situation of the business and "on decisions likely to lead to substantial changes in work organisation or in contractual relations,"[805] and, thus, contain a duty of the employer to inform in a practical way about an imminent restructuring or insolvency. However, the directive only applies to companies with more than 50 employees in one Member State or more than 20 employees in one establishment.[806] For smaller businesses, the right of employees to be informed individually by their employer about a business crisis or an imminent insolvency is not governed by the directive but left to the respective duties to inform a contractual counterparty under applicable contract law.

456. Directive 98/59/EC requires an employer to consult and inform the workers' representative in an establishment whenever collective redundancies are imminent.[807] As these requirements are not suspended in insolvency proceedings,[808] an IP or DIP must inform about and negotiate redundancies whenever the thresholds of the directive and the implementing national laws[809] are met. There is evidence that local rules implemented under the directive are note able to guarantee the early information of employees in

[802] This is especially important in jurisdictions that restrict employee right to terminate their contracts post-commencement (e.g. AT for one month).
[803] Directive 2002/14/EC of 11 March 2002 establishing a general framework for informing and consulting employees in the European Community [2002] OJ L80/29.
[804] Ibid, Article 1 (1).
[805] Ibid, Article 4 (2).
[806] Ibid, Article 3 (1).
[807] Council Directive 98/59/EC of 20 July 1998 on the approximation of the laws of the Member States relating to collective redundancies [1998] OJ L225/16.
[808] See ECJ Case C-80/14, *USDAW v WW Realisation 1 Ltd, in liquidation & Ethel Austin Ltd*.; David Reade, *Woolworths and the ECJ*, 13 ICR 69 (2016); Jennifer Gant, 'Collective Redundancies', eurofenix Summer 2015, p. 24 et seq.
[809] See e.g. German Insolvency Code s 121.

practice,[810] or, if they do, cannot necessarily prompt negotiations with the representatives that prevent or downsize the projected redundancies.[811] Overall, a continuous process of informing and mentoring all participants in a restructuring about how to prepare, communicate and cooperate when dealing with the social aspects of a restructuring still seems necessary and should reflect best practices collected in the European Commission's 'Quality Framework for Anticipation of Change and Restructuring'.[812]

457. Article 4 (1) of the directive also provides that "projected collective redundancies notified to the competent public authority shall take effect not earlier than 30 days after the notification […] without prejudice to any provisions governing individual rights with regard to notice of dismissal." This provision effectively orders a cancellation period of a minimum of 30 days irrespective of shorter periods under insolvency law whenever the directive is applicable.[813] The directive has been implemented in all analysed Member States.

5.1.1.3 Collective agreements and negotiations

458. The aforementioned directives refer to workers' representatives that are mandatory under national laws for companies with a larger number of employees. With such representatives present, employees are able to enter restructuring negotiations as well as negotiations for compensation in cases of collective redundancies. The participation in restructuring negotiations may be mandatory under national law establishing works councils in companies (Germany); it may also result from a participation of workers' representatives in a creditors' committee (Germany).

459. The commencement of insolvency or restructuring proceedings does not affect collective bargaining agreements per se. An IP or DIP may not terminate such (often statutory-like) agreements but terminate employment contracts which may produce the same result in case of collective redundancies. In restructuring proceedings, renegotiations with workers' representatives with respect to social benefits, wages and working hours are common which may result in a deviation from former collective bargaining agreements. Such agreements on work conditions should be part of the reorganisation plan which also means that they could be crammed down against the vote of employees. However, a judicial

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[810] See Dutch research in 2015 showed that in practice the Workers Council is often not consulted or informed; see Pam Hufman, *Arbeidsrecht in insolventie: een rechtsvergelijking* (2015), 285. Early 2016, the Dutch Social-Economic Council (SER, the prime advisory body to the government) published a flow chart that provides insights into what participation rights are applicable before and during bankruptcy. It is intended for workers, employers and insolvency practitioners. SER suggested in its opinion (i) to more explicitly pay attention to this issue in the training of insolvency practitioners, (ii) to have supervisory judges monitor compliance with the participation rules. See (in Dutch) SER, 'Stroomschema over medezeggenschapsrechten bij faillissement', 22 March 2016, available at http://www.ser.nl/nl/actueel/nieuws/2010-2019/2016/20160322-or-faillissement.aspx.

[811] See the result of consultations in the UK: The Insolvency Service, 'Responses to Call for Evidence on Collective Redundancy Consultation for Employers facing Insolvency', November 2015, at 7, available at https://www.gov.uk/government/consultations/collective-redundancy-consultation-for-employers-facing-insolvency.

[812] See European Commission, *EU Quality Framework for Anticipation of Change and Restructuring* (2012) COM(2013) 882 final. The paper followed from an earlier Green Paper; see COM(2012) 7 final; also see the accompanying Commission staff working document SEC(2012) 59 final.

[813] See for the UK: David Reade, 'Woolworths and the ECJ', 13 ICR 69 (2016).

confirmation of such a cramdown should only be available if the judge is convinced that negotiations were conducted in good faith and that the deviation is necessary to prevent further redundancies.[814] Where such agreements deviate from collective bargaining agreements which are generally binding on a national level (e.g. in Germany) and do not contain an exit clause, deviations under a reorganisation plan should de lege ferenda be allowed under the same restrictive conditions. The protection of competitors would, however, demand for a very limited period of relief (possibly limited to the immediate stage of the business turnaround and a maximum period of one year).

460. If the collective negotiations between the employer/IP and the workers' representative only concern a compensation for the termination of contracts in return for a waiver of job protection rights, some national law provides for a cap on such severance payments in order to balance the interest of employees with the interests of all creditors in a limited estate. Under German law, for instance, severance payment under a collective agreement may not consume more than a third of the estate to be distributed to unsecured creditors.[815]

5.1.2 Special tools for restructuring employment contracts or collective agreements

5.1.2.1 Additional tools in restructuring proceedings in general

461. If the business of the insolvent debtor is viable and (operationally) restructured in the course of (pre-)insolvency proceedings, a reduction of the workforce is a common tool to achieve such a restructuring. In such cases, a reduced protection of employment contracts by labour law provisions proves effective in limiting the costs of collective dismissals.

462. In formal insolvency proceedings, employment contracts can be terminated within a far shorter period than outside of insolvency proceedings in most jurisdictions that we analysed (see above). In addition, the costs and risks of litigation on the grounds of unlawful termination can be limited in some jurisdictions by a collective agreement between the IP and the workers' representative on a list of dismissed workers and a small severance payment (e.g. Germany[816]). Overall, the availability of less restricted termination rights is a powerful incentive to restructure a business by entering insolvency proceedings, resulting in a number of companies that have made strategic use of insolvency proceedings to restructure their workforce in times of a crisis.[817]

463. The framework of pre-insolvency proceedings does usually not provide for exemptions from labour law protections. Any redundancies would need to be done in accordance to applicable labour law (see above). As a result, pre-insolvency proceedings are commonly used to restructure the debt and capital structure of a business debtor rather than the operational structure of the business itself. Many pre-insolvency proceedings are explicitly designed for debt restructurings only (workout support proceedings).[818]

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[814] Such a procedure could avoid the pitfalls of a separate treatment of collective bargaining agreements as they are obvious in U.S. bankruptcy practice, see the ABI Report (2014), p. 156 et seq.
[815] See German Insolvency Code s 123 (2) 2.
[816] See German Insolvency Code s 125.
[817] See Gerrit M. Bulgrin, Die strategische Insolvenz, Diss. Hamburg, Mohr Siebeck 2016.
[818] See Chapter 1 at 1.1.2.

5.1.2.2 Special protection in case of a transfer of the business

464. The business of an insolvent debtor can also survive by being transferred on a going-concern basis to a new owner.[819] In such cases, employment contracts are, in principle, protected by the Acquired Rights Directive 2001/23/EC.[820] As the directive applies to any transfer of a business,[821] Article 3 (1) mandates that the transferor's rights and obligations arising from a contract of employment existing on the date of a transfer shall, on the basis of such a transfer, be transferred to the transferee. At the same time, Article 4 (1) bans any termination of such a contract on the grounds of the transfer. In principle, the transfer of a business as a going-concern will therefore always lead to the transfer of all employment contracts connected to the business. This, however, obviously constitutes a problem for insolvent companies that might only find a buyer with a reduced number of employees.

465. The European legislator responded to the special needs of insolvent businesses in the mergers and acquisitions ("M&A") market by enacting an exemption option in Article 5 (1) of the Directive which authorized Member States to choose whether the protection under Arts. 3 and 4 shall apply to a transfer of a business where the transferor is the subject of insolvency proceedings which have been instituted with a view to the liquidation of the assets of the transferor and are under the supervision of a competent public authority. That authority may be an insolvency practitioner authorised by a competent public authority. If Member States choose to protect their employees, they may limit the amount of transferred liabilities and allow for the consensual alteration of transferred contracts.[822]

466. The clear text of Article 5(1) only exempts transfers from an insolvent debtor as part of a liquidation procedure in formal insolvency proceedings. Transfers in pre-insolvency proceedings or formal restructuring proceedings are not exempted under a strict interpretation of the provision which means that any going-concern transfer of a business in such proceedings would include a transfer of all employment contracts.[823] Such a strict interpretation is favoured by the CJEU and enables the court to decide that an exemption under Article 5(1) is not even available for a pre-pack sale of the debtor's business[824]

[819] For more detail see the Chapter on going-concern sales (Q7).

[820] Council Directive 2001/23/EC of 12 March 2001 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses.

[821] Ibid, Article 1.

[822] Ibid, Article 5 (2).

[823] This is explicitly stated in the Belgian Inventory Report, Q5, under 5.1.2.

[824] See CJEU, 22.6.2017, C-126/16 - Federatie Nederlandse Vakvereniging, EU:C:2017:489. The underlying facts concerned the developing practice of 'Dutch pre-packs'. Such a 'pre-pack' is essentially a sale of the business assets as a going concern, but it needs to be prepared by an 'intended insolvency practitioner', under the supervision of '… an objective judge' with a restart of the operation performed after the opening of the insolvency liquidation proceedings. (see District Court Overijssel 28 July 2015, ECLI:NL:RBOVE:2015:3589). The practice of a Dutch pre-pack does not have any legal basis in the Netherlands Bankruptcy Act yet which led the Court of first instance for the Central Netherlands (24 February 2016, ECLI:NL:RBMNE:2016:954) refer a number of legal questions to the Court of Justice of the European Union. In the specific case, *Estro Group B.V.,* once the largest childcare company in the Netherlands with approximately 380 branches and 3,600 employees, was subject to bankruptcy liquidation proceedings opended on 5 July 2014. After the commencement, *Small Steps B.V*. acquired approximately 250 branches and 2,600 employees following a Dutch pre-pack. Approximately 1,000 employees would have lost their jobs.

although in such cases a formal liquidation proceeding is commenced and an insolvency practitioner is appointed in order to conclude the sale and process the transfer.[825]

467. Member States have used the option in Article 5 in a rather non-uniform way. Some jurisdictions like Austria, Belgium[826], Latvia, the Netherlands, Sweden or the UK exempted all transfers by an insolvency practitioner or in the course of "insolvency proceedings" from the protection under Arts. 3 and 4, others like Italy, Greece, Germany or Poland have not.[827] Under Italian law, only a transfer in one of the available pre-insolvency restructuring proceedings is exempted to the extent that the workers' representative agreed.[828] In Greece, a court may order the transfer of employment contracts on a case by case basis. In Germany, only the transfer of old employee claims is exempted while employment contracts are being transferred with the business even in insolvency proceedings; the same is being discussed in Poland. In jurisdictions that exempt transfers done by an IP, the exemption is sometimes also applied to restructuring proceedings that aim at a restructuring of the debtor and are administered by a debtor in possession (Belgium); sometimes the exemption is restricted to a transfer in a liquidation by an IP (England & Wales, Sweden).

468. In Germany, where the issue has not been addressed by the legislator, a decision by the *Federal Supreme Court* (*Bundesgerichtshof (BGH)*) affirmed that employment contracts are also protected in a business transfer in the course of insolvency proceedings[829] before later the Federal Labour Court, *Bundesarbeitsgericht (BAG)*, specified that, while employment contracts are transferred with the business, the transferee shall not be liable for any unpaid employment claims payable before the transfer.[830] The resulting protection of employment contracts in a business transfer led to a common practice that aims at terminating employment contracts prior to a transfer of the business. To achieve this, an insolvency administrator can either make use of the privilege of limited labour law protection under insolvency law, as discussed above. Or the administrator and the employees try to agree on a consensual solution. The latter way has become a common strategy in bigger German cases where the insolvency practitioner is able to negotiate a collective and consensual transfer of all employment contracts to a third company that is set up by unions and (partially) financed by the estate (and some public funding) specifically for the purpose of absorbing the employees of an insolvent business in order to allow the transfer of a business without any employment contracts. Employees usually agree to such a solution for two reasons: First, the transferee is allowed to re-hire former employees from the transitional company. Employees, therefore, may hope that their contribution to the survival of the business will eventually save their job under the new owner of the old business. Second,

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[825] For further details on a pre-pack sale, see below at 7.4.

[826] Belgian law explicitly allows the purchaser to decide which employees he is willing to transfer as long as his choice can be supported by technical, economic and organisational reasons without any discrimination of employees. In case of a transfer, the purchaser also assumes liability for unpaid salary and benefits.

[827] This reflects the standard set by the Principles of European Insolvency Law (2003) stating in § 7.4: '*If the enterprise of the debtor, or any part of it, is transferred, the contracts of employment are automatically transferred to the purchaser of the enterprise.*'

[828] There is a similar rule in Spain; see Inventory Report, Spain, Q5, under 5.1.2.

[829] See BGH NJW 1981, 1364, 1365, referring to German Civil Code s 613a that was enacted due to Council Directive 77/187/EEC of 14 February 1977 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses [1977] OJ L61/26, the predecessor of the current Directive.

[830] See BAG BAGE 132, 333 para.17 = NZA 2010, 461; BAGE 112, 214 = NZA 2005 408.

employees do not yet become unemployed when they leave the debtor for the transitional company. As such a transitional company is usually set up only for a year, it offers employees at least a limited timeframe where they do not yet receive unemployment insurance payments. At the same time, the objective of such a company is to re-orientate the employees for new jobs[831] and thus minimize the number of employees that would eventually be unemployed after the transitional period ends.[832]

5.1.3 Treatment of unpaid salary claims

469. The treatment of unpaid salary claims must be considered in the context of the background of the peculiar social situation of employees. As their livelihood typically depends on timely payments of the employer on behalf of these claims, a privileged treatment of such claims in insolvency proceedings is commonly a well-reasoned and understood approach.

5.1.3.1 Post-commencement claims

470. Employment contracts are typically not terminated automatically at the moment that insolvency proceedings are commenced. As shown above, their termination depends on a decision made by the IP/DIP under the applicable law on executory contracts. As a result, employment contracts may continue (especially in a business rescue); they may also be terminated after the expiration of an applicable cancelation period. Any salary claim that accrues after the commencement of proceedings commonly enjoys the privilege of ranking as an administrative expense or debt of the estate which means that they are usually paid in full as they fall due. This privilege does sometimes not include claims for severance payments or early termination damages that would result from the termination; such claims would be treated as unsecured.[833]

471. Post-commencement salary claims in pre-insolvency proceedings may also enjoy a privileged status in a subsequent bankruptcy if they remain unpaid (Belgium).

5.1.3.2 Pre-commencement claims

472. The cash limitations of a failing business quite commonly result in the non-payment of salary claims by the debtor on the eve of insolvency proceedings. As employees heavily depend on the fulfilment of their salary claims, statutory protection has been established across Europe to ensure that there is a high likelihood that employees do not suffer a substantial write-off in the course of insolvency proceedings. Basically, two ways of protection are common: a privileged treatment of these claims in insolvency proceedings and a third-party guarantee. In addition, some jurisdictions ban any restructuring plan

[831] The general challenge of organising an environment that facilitates the redeployment of released workforce was the subject of EC project that led to the collection of a toolbox of best practices across the EU; see European Commission, *European Restructuring Toolbox* (July 2010).
[832] For further details see Reiner Thum, 'Neue Spielregeln für die Zwischenschaltung von Transfergesellschaften?', BB 2013, 1525.
[833] See Austria, UK, Germany, Sweden, not, however, Belgium, Italy or Spain.

provision that contains a write-off for unpaid salary claims and benefits (Belgium) or allow only a voluntary participation of employees in such proceedings (Poland).

5.1.3.2.1 Preferential treatment

473. In many of the jurisdictions that we analysed, unpaid pre-commencement salary claims rank as preferred claims in the insolvency proceedings (see Belgium, Greece, Hungary, Italy, the Netherlands, Poland, Spain[834], Sweden[835]; not, however, Austria, and Germany[836]) to a certain, limited extend (time period before commencement and/or cap[837]).[838] As a result, privileged unpaid salary claims are paid from the estate if there are sufficient unencumbered assets to generate payments or a sufficient cash flow in a restructuring case.

5.1.3.2.2 Guaranty scheme

474. Following a European Council Directive from 20 October 1980[839], EU Member States have introduced an insurance-type of mechanism that guarantees the payment of outstanding salary claims.[840] Since 1980, it has been updated twice.[841] The mechanism that was promoted by the Directive followed predating German[842] and Dutch protection schemes.[843]

475. The directive requires all Member States to establish a body that guarantees the payment of outstanding claims to the employees concerned.[844] Article 5 of the Directive mandates that all Member States lay down detailed rules for the organisation, financing and operation of the guarantee institutions, complying with the following minimum standards:

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[834] In Spain, this includes unpaid salary from the last 30 days before the commencement.

[835] The preference does extent to post-petition salary claims.

[836] In (rare) cases where a "strong" preliminary IP is appointed following the petition for insolvency proceedings, unpaid post-petition salary claims are treated like post-commencement claims and paid as administrative expenses; see Inventory Report, Germany, 5.1.3.

[837] Greece: two years, claims are subject to the general preferential creditor's overall cap; Poland: three month, no cap; UK: four month, £800 cap; Spain: cap in the amount obtained by multiplying three times the minimum wage by the number of days of outstanding salary payment. No cap or limit was reported from Hungary and Italy.

[838] This reflects the standard set by the Principles of European Insolvency Law (2003) stating in § 7.2: *An employee has a preferential ranking in respect of certain insolvency claims for wages and other sums due under the contract of employment or arising from its termination.*

[839] Council Directive 80/987/EEC of 20 October 1980 on the approximation of the laws of the Member States relating to the protection of employees in the event of the insolvency of their employer [1980] OJ L283/23.

[840] This standard is also reflected by the Principles of European Insolvency Law (2003) stating in § 7.3: *A public fund is available to meet certain insolvency claims of employees for wages and other sums due under the contract of employment or arising from its termination. If the public fund pays the employee, it is subrogated in the rights of the employee.*

[841] See Directive 2002/74/EC of 23 September 2002 on the approximation of the laws of the Member States relating to the protection of employees in the event of the insolvency of their employer [2002] OJ L270/10, recently updated by the Directive 2008/94/EC from 22 October 2008 on the protection of employees in the event of the insolvency of their employer [2008] OJ L283/36 (current version).

[842] '*Gesetz über das Konkursausfallgeld*' of 17 July 1974, BGBl. I 1974, 1481.

[843] The salary over 13 weeks has been covered since 1968, presently under the wages guarantee scheme (loongarantieregeling) which is part of the Dutch Unemployment Act.

[844] Article 3; also see Recital 3 of Directive 2008/94/EC.

- Bankruptcy remoteness: The assets of the institutions must be independent of the employers' operating capital and be inaccessible to insolvency proceedings.
- Financed by employers' contributions: Unless it is fully covered by public authorities, employers must contribute to its financing.[845]
- Guarantee regardless of the payment of contributions: Though an insurance-like mechanism, payments to employees may not depend on the prior employer's fulfilment of their duty to contribute.

476. An employee under the Directive is defined as anyone with an employment contract, regardless of the employment being part-time or temporary (Article 2 (2)). Article 3 of Directive 2008/94/EC provides that Member States shall take the measures necessary to ensure that guarantee institutions secure the payment of employees' outstanding claims resulting from contracts of employment or employment relationships, including severance pay on termination of employment relationships, where provided for by national law. Based on this mandate, national legislators enacted provisions which gave employees a direct claim against the local guarantee institution (Austria, Germany). Any claim against the public fund requires outstanding claims resulting from contracts of employment or employment relationships and may include severance pay on termination of employment relationships if provided for by national law (Article 3 – which is e.g. not the case in German law[846]). In addition, the employer must be in a state of insolvency, which is defined as the time following a request to open insolvency proceedings[847] or other types of proceedings that refer to the inability of the employer to pay.[848]

477. Where these preconditions are met, unpaid salary claims are not guaranteed without a time limit and a cap as Article 4 of the Directive allows Member States to limit the liability of the guarantee institutions by:

- specifying the length of the period for which outstanding claims are to be met by the guarantee institution,[849] and by
- setting ceilings on the payments made by the guarantee institution.[850]

478. Referring to the social objective of the Directive, the ceilings set by national legislators must not fall below a level which is socially compatible with this objective,[851] and the time limit may not be shorter than a minimum period of three months in a reference period with a duration of not less than six months.[852] All national legislators in the jurisdictions that we

[845] See e.g. Germany where amount payable by the employer relates to the amount of an individual salary claim and is currently set to 0,15 per cent (German Social Code, Part III, s 360). The contribution is to be paid by the employer as part of the social security contributions of the employer (and the employee) that are connected to the salary claim (e.g. contributions for statutory health, unemployment and pension insurance) to a public authority (German Social Code, Part III, s 359(1)). From here, all contributions for the guarantee scheme are transferred to the government authority administering the funds, the *Bundesagentur für Arbeit* (German Social Code, Part III, s 359(2)).
[846] See German Social Code, Part III, s 166(1) No. 1.
[847] Article 2 (1).
[848] Article 2 (4).
[849] Article 4 (2).
[850] Article 4 (3).
[851] Article 4 (3) 2.
[852] Article 4 (2) subpara. 2.

analysed limited the liability of the guarantee institution, either by introducing time periods and/or caps.[853]

479. The guarantee institution, having paid a claim to an employee, is then subrogated to the rights of the employee against the employer. At this stage, insolvency proceedings are usually commenced, and the guarantee institution is now entitled to file all subrogated salary claims. In principle, the subrogated claim will not enjoy any special treatment. If employee claims are ranked as preferential under national insolvency law, the subrogated claim will usually also rank as preferential (France[854], UK). Under German insolvency law, however, Insolvency Code s 55(3) provides that a subrogated claim will always be treated as a general unsecured claim. As these claims usually receive a payoff of 0 to 10 per cent, the German guarantee institution (*Bundesagentur*) cannot expect a significant recovery in insolvency proceedings on behalf of subrogated employees' claims. As a result, guarantee payments to employees are mostly covered by permanent contributions of all employers to the public fund.

5.1.3.2.3 Overall level of protection

480. When combining both protective instruments, remarkable disparities arise from different fundamental opinions about how to adequately protect employees' pre-commencement claims in insolvency proceedings across Europe. In Germany, such claims are only protected by the guarantee scheme, meaning that these claims do not receive any preferential status in the ranking of unsecured creditor claims under insolvency law. Pre-commencement claims are general unsecured claims only. Here, German legal protection differs significantly from regimes in many other EU Member States where pre-commencement employee claims usually have preferential status. Under such regimes, the protection of employees is primarily assigned to the distribution in insolvency proceedings. The guarantee scheme only works as an additional tool within narrow statutory limits, consequently being of limited relevance in practice.

5.1.4 Impetus for recommendations

481. Inventory reports on national law indicate that the legal treatment of employees in insolvency and pre-insolvency proceedings follows very similar rules and principles across Europe. This convergence was not only initiated by several EU directives that have set minimum standards. Even beyond the scope of said directives, common ideas can be detected:

– Treatment of employment contracts under executory contract rules

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853 See Austria: six month before commencement and max of €9.300 per month; DE: three month and a monthly cap with the maximum reference for the calculation of social security contributions ("*Beitragsbemessungsgrenze*", currently approx. €6.000). Italy: three month, cap at 1,165.58 for 2014. Netherlands: 13 weeks, no cap. Poland: three month, no cap. Sweden: three month before petition (total max. of 8 month), cap at four times the price base amount pursuant to the Public Insurance Code. UK: four month, £800 cap. Spain: cap in the amount obtained by multiplying three times the minimum wage by the number of days of outstanding salary payment.

854 The French fund (AGS) will even rank first regarding claims for unpaid wages for the 60 days of work preceding the opening of reorganisation or liquidation proceedings.

– Termination rights and periods
– Need for timely information of employees
– Usefulness of workers' representatives and collective agreements
– Need for protection of unpaid salary claims
– The status of post-commencement salary claims
– The preferential treatment of pre-commencement salary claims.

That being said, there are still, however, a lot of differences in detail. In accordance with the ECJ approach,[855] the protection of employees in the event of collective redundancies should be fully harmonised to ensure comparable protection for workers' rights in the different Member States and to harmonise the costs which such protective rules entail for EU undertakings.

5.1.4.1 Termination rights and contract protection

482. Employment is essential for people to provide for their livelihood as well as for the personal fulfilment in life. The protection of employment contracts is, thus, justified from a social perspective. When a business fails, the social interest of the employees may conflict with the interest of the employer and investors to rescue the business by not only restructuring the balance sheet but also by reducing costs which usually means reducing the workforce as a main factor for costs. Restructuring plans usually provide for the restructuring of business operations that includes redundancies. In order to resolve the conflict, balanced rules and best practices can be identified from the analysis above.

483. Moreover, differences in detail in the implementation of the aforementioned Directives in Member States should be prevented in the interest of an equal treatment of employees who are usually in a vulnerable, financially dependent position. An unbalanced resolve of said conflict may have a negative effect on the morale of employees which may create an adverse effect on the chances of success of continuity of the business which has already enough obstacles to cope with.

484. As a basic principle, employment contracts are executory contracts and should be treated accordingly in a way that they do not end automatically when insolvency proceedings are commenced. Instead, the right to terminate would rest with the IP/DIP under insolvency law. In case of a business rescue, redundancies must be possible according to the business plan under a restructuring plan. Labour law restrictions should be exempted (with regard to termination periods but also to general termination protection laws with respect to the pregnancy, illness or social needs of an employee). In cases of a business transfer, EU legislator could clarify Article 5 of Directive 2001/23/EC and exempt all transfers in formal insolvency (reorganisation or liquidation) proceedings.[856]

[855] See ECJ Cases C-80/14 *USDAW v WW Realisation 1 Ltd, in liquidation & Ethel Austin Ltd*. EU:C:2015:291, para.62; C-383/92 *Commission* v *United Kingdom* EU:C:1994:234, para.16; C-55/02 *Commission* v *Portugal*, EU:C:2004:605, para.48; C-385/05 *Confédération générale du travail and Others* EU:C:2007:37, para.43.
[856] See also Pam Hufman, *Arbeidsrecht in insolventie: een rechtsvergelijking* (2015) 283, stating the disappearance of labour law protections in all formal insolvency proceedings.

485. In order to prevent solvent businesses from abusing such proceedings for the sole purpose of facilitated (low cost) collective redundancies,[857] the court that opens formal insolvency proceedings must scrutinize carefully whether the ground to commence proceedings is proven. A balanced approach with regard to employee interests may call for a narrow interpretation of an 'imminent insolvency' test. In addition, redundancies in a formal reorganisation procedure should only be privileged if they are based on the respective reorganisation plan which proves that the proposed redundancies are indispensable to the success of the reorganisation. If proven, the plan should provide for a reasonable and feasible compensation or severance pay.[858]

486. Finally, with the termination of the employment contract, every employee should be free to work for any new employer in the market. Neither contractual no-competition clauses nor statutory non-competition rules should restrict their freedom to choose a new employer unless the employee receives adequate protection or compensation.[859]

5.1.4.2 Timely information

487. Employees are investors and closely connected to their employer. They must be informed early about an imminent restructuring or insolvency in order to allow them to decide whether to stay with their employer (reinvest) or to leave. While there is a risk that primarily the key employees of a failing business might actually leave the troubled business which could endanger any rescue effort, the interest of all employees in making an informed decision should prevail.

5.1.4.3. Representing Employees Collectively

488. The representation of employees in insolvency proceedings has been welcomed because it facilitates negotiations where there are a larger number of affected employees.[860] Collective agreements may mitigate litigation risks following collective redundancies caused by a transfer of the business in return for severance payments to affected employees.

489. The subrogating of employee claims against an insolvent employer to a government agency under a guarantee scheme also results in a "representation" of these claims by a single person in the further course of insolvency proceedings. Because the guarantee institution is a creditor, it holds all creditor rights, such as the right to participate and vote in creditors' meetings or to vote on a rescue plan. This introduction of such a professional player can sometimes enhance rescue negotiations.

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[857] See O. Kimhi and A. Doebert, *Bankruptcy Law as a balancing system: Lesson from a comparative analysis of the intersection between labour and bankruptcy laws*, 23 ABI Law Review 2015, 491.

[858] See again Pam Hufman, *Arbeidsrecht in insolventie: een rechtsvergelijking* (2015) 284, arguing for a basic distinction between liquidation (including a business transfer) and continuity scenarios.

[859] The Dutch law seems to present the only exemption to this straight forward principle, see Pam Hufman, *Arbeidsrecht in insolventie: een rechtsvergelijking* (2015) 281, with her critique at 285.

[860] See Pam Hufman, *Arbeidsrecht in insolventie: een rechtsvergelijking* (2015) 285.

5.1.4.4. Preferring a Guarantee Scheme to Cover Unpaid Salaries

490. Unpaid salary claims of employees are either protected by enjoying a preferred ranking in the distribution or by a guarantee scheme, often by both systems. The level of protection under a preference rule is, however, questionable in practice as in many cases, especially SME cases, the administrator cannot generate sufficient money to even pay preferential creditors. In practice, a preferential payment is often uncertain and late.[861] Instead of addressing these weaknesses by super-prioritising employees claims to the disadvantage of secured creditors (see France), it seems preferable to develop the common guarantee scheme towards a level of protection (in terms of raising the cap and extending grounds and the time period covered) that fully addresses the needs of employees (see Germany).

5.1.4.5. Using the Guarantee Scheme Fund for Post-Petition Financing

491. The structure of the European guarantee scheme for unpaid salaries does not intend to give financial support to a failing business. However, German insolvency practice has mastered a use of the scheme that allows for an essential relief for business finances in the very crucial period after the filing but before the opening of insolvency proceedings, called "Insolvenzgeldvorfinanzierung". Under German law, insolvency proceedings are not commenced on the very day of a petition being filed. Instead, interim proceedings are initiated by the court in order to investigate whether the debtor is actually insolvent and whether there are sufficient assets to cover the costs of formal insolvency proceedings.[862] An interim insolvency administrator is usually appointed to investigate the debtor's financial status und to secure all assets from being dispersed or diminished.[863]

492. If the business of an insolvent debtor is still running after a petition has been filed, workers will have to be paid during interim proceedings in order to keep the business going. To meet their post-petition salary claims, the interim insolvency administrator usually contacts a bank and negotiates a collective purchase of all post-petition employee claims by the bank as far as they are covered by the guarantee scheme. In consideration to the collective subrogation of their salary claims, the banks pay the employees an amount equal to that claim as it falls due. In addition, the debtor pays a premium to the bank. After insolvency proceedings are opened, the bank turns to the guarantee scheme for payment because all acquired salary claims are still unpaid by the debtor and covered by the guarantee. The German guarantee institution would accept this request and pay if it had agreed to the transaction when it was negotiated. German law permits a subrogation only if it finds that the intended transaction would help to secure a "significant number of jobs" with such a business.[864] This provision is usually interpreted in a rather generous way. For example, the requirement to save a "significant number of jobs" is held to be met where about 10 per cent of the workforce is expected to stay with the business.

493. Bearing in mind the very limited recovery from the estate that the guarantee institution would usually receive, this practice forms a form of support for business rescues in

[861] See Pam Hufman, *Arbeidsrecht in insolventie: een rechtsvergelijking* (2015), 281.
[862] See German Insolvency Code, s 21 to 26.
[863] Ibid, s 22.
[864] German Social Code, Part III, s 170 (4).

insolvency by means of publicly administered funds. Such usage, however, could prompt legal issues because state aid is forbidden under European law.[865] It is easy to imagine that in 2009, the German legislator and German insolvency practitioners were relieved to learn that the European Commission did not find a form of forbidden state aid when evaluating the German practice.[866] Today, the tool is essential for preserving a rescue option for insolvent German businesses in the eyes of most experts. It seems worth to consider a widespread use of this tool which would, of course, require other jurisdictions to expend tight limits on claims covered by the guaranty and to ensure that the guarantee institutions will not enjoy preferential status with their subrogated claims.

5.1.4.6. Employee protection and the practice of self-employment

494. Any entitlement to employment protections depends on the determination that a contract qualifies as an employment contract. Such a determination is not always simple as employers have expanded the use of independent, self-employed workforce. Eventually, it is a matter of a Member States labour law to define its scope. From a European perspective, a harmonised approach seems preferable that considers the reality of the working relationship instead of simply referring to what an employer chooses to call someone who works for them.[867]

5.2. Pensions

495. Pension entitlements are at least as important as salary claims and the continuation of employment as they also provide for the livelihood of the pensioner. They may be even more important because pensioners are usually not capable anymore of substituting pension payments by earning an income on the employment market due to their age and health condition. The issue of pension protection does, therefore, have an enormous significance in a social security framework.[868]

5.2.1. Special treatment of pension of employees

496. All of the jurisdictions that we analysed have established a social security framework that secures the livelihood of pensioners through a state-run pension scheme. As entitlements in such a scheme are directed against a public agency with no insolvency risk (as long as there is no sovereign debt crisis), the respective insolvency law contains no specific provisions for an insolvency protection. Sometimes there is a preferential status

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[865] Article 107 TFEU.

[866] European Commission, Decision of 19 November 2009 – K(2009)8707.

[867] This approach is also reflected in Recommendation 6 of the UK *Government response to the joint House of Commons committees' report on the impact of the closure of City Link on employment* (2015).

[868] Since 2008, when the economic turmoil grew, the issue of basic financial security for retirement has become a major societal challenge all over the world. Still, the topic of pension (funds) deficits resulting from insolvent companies has not yet been studied closely by academia. The EU Commission only sponsored one study, see ESOFAC Belgium, *The protection of supplementary pensions in case of insolvency of the employer for defined benefit and book reserve schemes*, Study for the European Commission VC/2009/0336 (2009). For a rather general survey of 21 jurisdictions including non-EU countries, see INSOL International, *Pensions and Insolvency – An International Survey*, (London 2015).

given to contribution claims of the social security agency against an insolvent employer, either for pre- and post-commencement contributions (e.g. Greece, Hungary, Poland) or the latter only – especially due to a connection of contribution claims with wages claims (e.g. Germany).

497. In some jurisdictions, the state-run pension scheme has been complemented by a framework encouraging employers and employees to agree on additional individual or occupational pension schemes.[869] The existence of such a framework has usually prompted the legislator to specifically address the issue of insolvency protection.[870] Such a protection usually covers three topics: a) the guaranty of pension entitlements by imposing an insurance-type scheme or establishing a protection of employer's assets set aside to cover pension entitlements (in case of a direct pension scheme); b) the (preferential) treatment of premium or contribution claims in insolvency; c) the possibility to reduce the burden of pension-related payments for troubled businesses (see 5.2.2.).

5.2.1.1. The protection of pension entitlements

498. The most essential part of any pension protection framework is the protection of pension payments to the (later to be) pensioners. The common way is to separate the funds for those payments from the employers' estates and, thus, making them bankruptcy-remote. In a state-run social security scheme, the funds are administered by public agencies that are held to be solvent irrespective of future economic developments or the insolvency of a greater number of contributing employers. In an individual or occupational pension scheme framework, the same protection can be achieved by using a supervised insurance company or regulated pension fund entities to collect and administer funds for private pensions.[871]

499. As a result, the need to address private pension claims only exists where individual or occupational pension schemes are also common without involving third parties (book reserve or direct pension schemes – see Austria or Germany). Under such agreements, the pension entitlement is a claim against the estate and protected either by creating a special fund from assets set aside to cover pension payments (Austria; in Belgium also for indirect schemes), or by guarantying pension entitlements by a third party (pension guaranty agency – see Austria, Germany, Sweden, or UK.).[872]

5.2.1.2. The treatment of premium or contribution claims

500. Contributions to a social security framework, but also to an individual pension scheme are usually borne by the employer – either as a statutory part of wages agreements and

[869] See Austria, Belgium, Germany, Sweden, UK. For a general overview of the dissemination of such schemes across EU Member States, see ESOFAC Belgium, *The protection of supplementary pensions in case of insolvency of the employer for defined benefit and book reserve schemes*, Study for the European Commission VC/2009/0336 (2009) 9 et seq.
[870] See Austria, Belgium, Germany, UK. See also ESOFAC Belgium, ibid, at 28 et seq.
[871] See Austria, Belgium, France, Germany, the Netherlands, UK. The activities of such agencies are regulated by the Directive 2003/41/EC of 3 June 2003 on the activities and supervision of institutions for occupational retirement provision [2003] OJ L235/10.
[872] ESOFAC Belgium, ibid, at 36.

payments (non-wage labour cost or ancillary wage costs[873]) or based on an individual additional agreement (often a collective agreement on additional benefits like private pension entitlements). In the employer's insolvency, the respective claims may mature pre- as well as post-commencement of insolvency proceedings. Accordingly, their preferential status may differ (see above 5.2.1.). Non-payment of contributions to a social security framework due to insolvency does usually not disadvantage the pension entitlements of the employee (see e.g. France or Italy, but also Poland for the opposite). Omitted contributions to private schemes may diminish the value of pension entitlements, however, and the continuance of contributions despite of the insolvency of the employer is secured either by a third party stepping in (pension guaranty agency[874]) or a "super-priority" (UK) or at least the described preferential status of such claims (Hungary, the Netherlands, Sweden).

501. If premium or contribution payments have been covered by a pension guaranty institution, the respective claims are usually subrogated and the institution enters proceedings in the position of a (preferential) creditor. If the business is rescued and the debtor survives, the institution may be entitled to return all pension obligations to the debtor or a purchaser of the debtors business and employees (Germany).[875] In such cases, a prior restructuring of pension entitlements is to be considered.

5.2.2. Restructuring of pension entitlements in a business rescue

502. Pensioners depend strongly on their (future) pension entitlements which not only justify a widespread protection but also a very limited possibility to restructure pension entitlements and contributions by way of a haircut.

503. Pension entitlements against public agencies as well as contribution claims of these agencies against the employer are not subject to restructuring efforts in all of the analysed jurisdictions. There is no need for that because pension entitlements are borne by the public agency, and, as obligations of the restructured employer to pay contributions solely depend on the number of employees, the restructuring of these future obligations is done by way of redundancies. Unpaid contributions to the public scheme prior and during proceedings are, however, claims against the estate, sometimes subrogated to a public insurance agency under an applicable guarantee scheme, sometimes paid due to a preferential status (see above). Such unpaid claims may be restructured in plan proceedings (Germany, not Poland before 2016, disputed in Belgium).

504. Individual or occupational pension schemes resemble public schemes when they are done through third parties (insurance companies, pension funds). Here, the employer is not the debtor to pension payments and may terminate future contribution payments under applicable contract law (see e.g. Austria).

505. The scenario is different, however, whenever pension entitlements are directed against the employers themselves (direct pension schemes). Here, the debt burden caused by future pension payments and contribution can mount significantly and cause a viable business to

[873] See Belgium, France, Germany, Hungary, Sweden, UK.
[874] Austria, Germany, Sweden, also UK.
[875] See German Company Pensions Act, s 7 (4) and 9, and German Civil Code, s 613a.

become over indebted and, eventually, insolvent. While future contribution payments may again be dealt with based on contract law, future, but also current, pension payment obligations may be restructured under a restructuring plan in Germany[876] whereas all other analysed jurisdictions do not report specific legal provisions and authorisation. There are also no recommendations from international standard-setting organisations. The matter is obviously left to common contract and insolvency law. In Germany, such entitlements are, however, protected by a guarantee scheme which results in the guarantee institution substituting employees or pensioners and participating in the restructuring negotiations (adding a repeat player to the table). This very peculiar type of creditor would usually need to be placed in a separate class of creditors in a restructuring plan[877] which means that any plan that impairs pension entitlements or contributions would require the actual consent of this class or an applicable cram-down rule. Under these restrictions, any restructuring against the consent of the guarantee institution is very difficult to achieve which gives the agency a strong position in restructuring negotiations. Overall, the restructuring of individual pension entitlements or future pension scheme contributions is possible under German law but requires cooperation.

5.2.3. Impetus for recommendations

506. The protection of pension entitlements is well established in respect of social security schemes. Under such a regime, pension entitlements are not endangered by the employer's insolvency and omitted contribution payments are either covered by guarantee institutions or paid due to their preferential status. The risks for employees seem very well addressed.

507. The picture is not as clear with regards to individual or occupational pension schemes. Where such schemes are organised through a third party (insurance company or pension fund), pension entitlements are employer-insolvency-remote.[878] The issue of covering contribution payments has not yet been addressed in all jurisdictions. In those who did, guarantee schemes are common, often accompanied by preferential treatment of such claims. There is a tendency to protect such pension schemes similar to the public schemes in order to promote their use.

508. Pension agreements that contain a direct pension scheme between the employer and the employee are not available or protected everywhere. They should also enjoy insolvency-remoteness through a mandatory insurance scheme.[879] The debt burden resulting from such schemes may, however, give cause to restructuring efforts. While a specific legal provision for such restructuring proceedings was only reported for Germany, other jurisdictions seem to handle these cases by applying their common contract or restructuring law. Given the (growing) importance of individual pension schemes, such restructuring attempts should be protected by approving them expressively. At the same time, the specific importance of pension entitlements must be recognised by protecting pensioners' rights in such

[876] See German Company Pensions Act, s 7 (4) and 9 (4).
[877] See German Company Pensions Act, s 9 (4).
[878] The only issue here would be the insolvency or insufficient performance of the pension fund, possible in times of economic depression or little interest rates, see ESOFAC Belgium, *The protection of supplementary pensions in case of insolvency of the employer for defined benefit and book reserve schemes*, Study for the European Commission VC/2009/0336 (2009) 67-68.
[879] Ibid, at 8-69.

restructurings preferable by extending the coverage of guarantee schemes (following the German example).

5.2.4. Recommendations

Recommendation 5.01: Member States ensure that employees and workers' councils receive timely notice about an imminent restructuring or insolvency.

Recommendation 5.02: Employment contracts should not end automatically upon the commencement of (pre-)insolvency proceedings. Member States should ensure that such contracts enjoy full labour law protection outside of formal insolvency proceedings while being treated under the applicable rules for executory contracts in insolvency proceedings.

Recommendation 5.03: Member States provide for a default continuation rule combined with the right of the insolvency practitioner or the debtor in possession to terminate employment contracts within a short period.

Recommendation 5.04: Labour law protection, including special protection for pregnant or ill employees, should only be applicable outside of formal insolvency proceedings. In formal restructuring proceedings, any redundancies should be required to follow from the necessities of the rescue strategy pursued by the restructuring plan. The plan should, in principle, provide for severance payments.

Recommendation 5.05: Employees, whose employment contract was terminated in the course of formal insolvency proceedings, should be free to conclude a new contract with any employer available. Neither contractual non-competition clauses nor statutory non-competition rules should apply unless the employee receives adequate protection or compensation.

Recommendation 5.06: Member States should provide that, whenever a specific number of employees in an establishment are likely to be affected by a restructuring plan or a liquidation (including a business transfer), a representative should have a right to represent and to protect their interest by participating in formal restructuring and liquidation proceedings (e.g. in a creditors' committee).

Recommendation 5.07: The protection of unpaid salary claims can be achieved by treating them as preferred claims or even administrative expenses in a formal procedure. Where a cost-efficient guarantee institution exists, Member States should ensure rely on it and ensure that it covers as much unpaid salary as possible and allows for a timely payment to employees.

Recommendation 5.08: The European Commission is invited to conduct an overall comparative study on the laws relating to the treatment and protection of pension-related contribution and claims in case of an (imminent) insolvency of the contributing employer that includes all relevant aspects of EU rules as well as substantive national pension, labour, and insolvency law.

Recommendation 5.09: Member States should ensure that individual or occupational pension schemes are to be restricted to indirect pension schemes which either use (insolvency-remote) third parties or are protected by a guarantee scheme. The restructuring of pension entitlements from a direct pension scheme should only be possible where a guarantee protection scheme is in place.

CHAPTER 6:
Avoidance transactions in out-of-court workouts and pre-insolvency procedures and possible safe harbours

6.1. Introduction

509. They key questions analysed in this chapter are (i) whether there are avoidance powers available in the pre-insolvency proceedings or in the out-of-court workout procedures, and (ii) whether the national law of the countries surveyed provide any special protection from avoidance for agreements achieved in such proceedings or workouts. As an illustrative example: if, for instance, new finance is agreed, either by individual arrangement or as part of a restructuring plan, are these arrangements exempted, under specific circumstances, from avoidance actions?

510. All legal systems of the EU Member States addressed in this study have a set of rules regarding transaction avoidance. This observation is rather obvious. In 2004, the EBRD, in its Core Principles for an Insolvency Law Regime, considered at the outset, that '… [m]odern insolvency systems and debtor-creditor regimes are the cornerstone of sustainable economic development and provide a safety valve for financial failures'. In the field of insolvency, based on measurement against international standards (such as the UNCITRAL Legislative Guide and the World Bank's Principles), EBRD has defined a set of principles for a modern Insolvency Law Regime (ILR), intended to be the foundation of an ILR, called 'Draft Statement of Core Principles for an Insolvency Law Regime' ('Core Principles'). There are ten Core Principles in total, the seventh of them says:

> '7. The ILR should provide for the independent review of transactions and actions by the debtor and the imposition of sanctions in case of misconduct. An essential component of liquidation and re-organisation is the ability to impose sanctions upon parties who attempt to frustrate the insolvency process. This should typically include the ability to reverse fraudulent, below market or preferential transactions that occurred on the eve of the debtor's insolvency and the ability to sanction high-ranking officers and directors of the insolvent company for fraudulent or uncooperative behaviour.'[880]

[880] Bob Wessels and Gert-Jan Boon, *Cross-Border Insolvency Law, International Instruments and Commentary*, (2nd Ed., Alphen aan den Rijn: Kluwer Law International 2015), para.41. The Principles of European Insolvency Law (2003) state in § 8.1: A juridical act unfairly detrimental to the creditors performed by the debtor within a certain period of time before the opening of the proceeding, is subject to reversal. The administrator can recover or seek annulment of any benefit which has been obtained from the debtor.
Furthermore, § 8.2 adds to this that:
'Juridical acts subject to reversal include:
a) A transaction with the intent of defrauding creditors;
b) A transaction for inadequate countervalue;
c) A transaction with a creditor for which no enforceable obligation existed;
d) A transaction with a creditor after the filing of the insolvency application or in a situation of imminent insolvency;
e) The creation of a security right to secure a pre-existing obligation.'

6.2 Claw-back rules and safe harbours

511. Avoidance provisions can be described in a variety of ways. A pan-European description in the context of insolvency is the following: '(i) Provisions of the insolvency law that permit transactions for the transfer of assets or the undertaking of obligations, including the granting of security interests, prior to insolvency proceedings to be cancelled or otherwise rendered ineffective and any assets transferred, or their value, to be recovered in the collective interest of creditors'.[881] The UNCITRAL Legislative Guide (2004) clearly sets out the complexity with which transactions that may be eligible for avoidance should be approached and the interests that are at stake:

> '154. Avoidance rules are much discussed, principally as to their effectiveness in practice and the somewhat arbitrary rules that are necessary to define, for example, relevant time periods and the types of transactions that may be avoided. As is the case with a number of the core provisions of an insolvency law, the design of avoidance provisions requires a balance to be reached between competing social benefits such as, on the one hand, the need for strong powers to maximize the value of the estate for the benefit of all creditors and on the other hand, the possible undermining of contractual predictability and certainty. It may also require a balance to be reached between avoidance criteria that are easily proven and will result in a number of transactions being avoided and narrower avoidance criteria that are difficult to prove but more restricted in the number of transactions that will be avoided successfully. To minimize the potentially negative effects of avoidance powers on contractual predictability and certainty, it is desirable that as far as possible the categories of transactions to be avoidable (irrespective of whether they are broadly or narrowly defined), and the exercise of avoidance powers be subject to clear criteria that will enable business and commercial risks to be ascertained.'

The wider scope for 'avoidance' may extend to provisions within the general law of the national law system concerned.[882] It then means the 'avoidance' of a juridical act or legal relationship, being the process whereby a party or, as the case may be, a court invokes a ground of invalidity so as to make the act or relationship, which has been valid until that point, retrospectively ineffective from the beginning.[883]

6.2.1 Significant elements from National Reports

512. As said, all Member States surveyed contain in their insolvency laws transaction avoidance rules ('*actio Pauliana*', '*Insolvenzanfechtung*', etc.). These rules are rather

[881] See Common Frame of Reference (DCFR), the Study Group on a European Civil Code and Research Group on EC Private Law (Acquis Group), Principles Definitions and Model Rules of European Private Law, European Law Publishers (2009), Annex (Definitions),
p. 546.

[882] This wider mode of reference is employed by the terms 'act detrimental to all the creditors' in Article 13 EIR (2000) (ditto in Article 16 EIR (2015)).

[883] See Study Group on a European Civil Code and Research Group on EC Private Law (Acquis Group), Principles Definitions and Model Rules of European Private Law, European Law Publishers (2009), Annex (Definitions), p. 546.

differently formulated, contain different criteria and the rules on evidence, enforcement and persons eligible to invoke these rules differ quite substantially.[884]

513. Regarding the question whether there are avoidance powers available in the pre-insolvency proceedings or in the out-of-court workout procedures, nearly all correspondents of the Member States refer to the rules regarding 'avoidance' in the wider scope of the term: rules of that nature in general (civil) law (and also these rules are rather different). This is the case for Austria, Belgium, England and Wales, France, Germany, Hungary, Italy, Latvia, the Netherlands, Poland, Spain and Sweden.

514. Regarding the second question about safe harbours from avoidance for agreements achieved in pre-insolvency proceedings or workouts under national law, the most notable responses are from Belgium, England and Wales, France, Italy and Spain:

515. The Belgian Business Continuity Act (BCA) provides a 'safe harbour' for payments or performances made by the debtor under an amicable, out-of-court settlement agreement which is submitted to the clerk's office and stipulating that such agreement has been entered into with the purpose of a reorganisation of the enterprise or of its financial situation.[885] If such payments or performances were made during the suspect period (as determined by the court in a later subsequent bankruptcy), they cannot be avoided on the basis of Article 17, 2° Bankruptcy Act (with respect to payment of unmatured debts and payment of matured debts other than in money or commercial paper) or Article 18 Bankruptcy Act (with respect to all other transactions entered into during the suspect period which are detrimental to the bankruptcy estate and provided the counterparty had knowledge of the fulfilment of the bankruptcy conditions).[886]

516. In England and Wales the legislation does not contain safe harbours for out-of-court workouts or pre-insolvency proceedings.[887] The National Correspondents do however note that the court may not make an order in respect of a transaction at an undervalue if it is satisfied that the company carried out the transaction in good faith and for the purpose of its business and at the time there were reasonable grounds for believing that the transaction

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[884] See, comparing some ten countries, Christoph G. Paulus, 'Das Recht der Insolvenzanfechtung und Gläubigerschutz', in Marcus Lutter (Hrsg.), *Das Kapital der Aktiengeselschaft in Europa* (Berlin: De Gruyter, 2006), p. 434-450; R.J. de Weijs, E.J.R. Verweij, C. Bärenz and R.M.A. Connell, 'Financing in distress against security from an English, German and Dutch perspective: a walk in the part or in a mine field?', International Insolvency Law Review 1/2012, 21 et seq, and the comparative PhD research of R.J. de Weijs, *Faillissementspauliana, Insolvenzanfechtung & Transaction Avoidance in Insolvencies* (PhD University of Amsterdam; Serie Recht en Praktijk Insolventierecht, InsR1, Deventer: Kluwer 2010). This author also submits elements for a 'harmonised' European approach, see Rolef de Weijs, 'Towards an Objective European Rule on Transaction Avoidance in Insolvencies', 20 International Insolvency Review 2011, p. 219 et seq. See also Tuula Linna, 'Actio Pauliana – "Actio Europensis"? Some Cross-Border Insolvency Issues', 10 Journal of Private International Law 2014, p. 69.

[885] Article 15 BCA.

[886] There is, however, no protection against fraudulent transactions (actio pauliana, Article 20 Bankruptcy Act), and undervalue or gratuitous transactions (Article 17, 1° Bankruptcy Act). 'New' security rights granted for 'old' debts are not protected either (Article 17, 3° Bankruptcy Act). A similar set of rules apply to an amicable settlement agreement entered into during judicial reorganisation proceedings, under the supervision of the court (Article 43 BCA).

[887] Reinhard Bork, *Rescuing Companies in England and Germany* (Oxford University Press, Oxford 2012), para. 16-07.

would benefit the company.[888] They conclude that for this reason it may be difficult for the liquidator or administrator to challenge transactions that were entered into in the course of a legitimate rescue attempt. Furthermore, they similarly conclude that there will be no preference '… to the extent that the beneficiary provides the company with new value, as where a creditor is granted security for a contemporaneous or subsequent advance on the basis of an individual arrangement or as part of a comprehensive rescue plan.' The test of '… a desire to put the creditor in a better position'[889] will usually prevent transactions entered into in the course of a legitimate rescue attempt from being vulnerable as preferences.[890]

517. The correspondents for France explain the legal rules resulting in the situation that in the event that a *conciliation* procedure fails, the suspect period can only start before the agreement is ratified (*homologué*) by the court, and the guarantees undertaken in the agreement cannot be challenged. This safe harbour is only available to *conciliation* agreements that are formally ratified (*homologué*) by the court and do not apply to conciliation agreements that are merely recorded (*constaté*) by the President of the court, nor to any agreements that may be entered into in the context of a *mandat ad hoc* procedure.

518. Likewise in Germany there is a specific, distinct safe harbour, in that there is no privilege for performances received during the last three months prior to the insolvency application where the legal prerequisites are met[891], but that these performances are not deemed to be made with the intention to disadvantage creditors[892] if they have been fulfilled on the basis of a serious restructuring attempt.[893] In Germany this legal rule is referred to as the 'restructuring privilege'.[894]

519. The Italian Law 80/2005 contains a list of transactions, which are exempt from clawback actions:

a. payments for goods or services made in carrying on the ordinary business of the company in accordance with commercial custom;

b. banking remittances, except those that substantially and in a sustained manner reduced the indebtedness of the company to the bank;

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[888] UK Parliament: Section 238(5) Insolvency Act 1986

[889] UK Parliament: Section 239(5) Insolvency Act 1986.

[890] The provisions of the Act relating to preferences allow the office-holder to challenge the doing by a company or individual (or the suffering of anything by a company or individual) of an act which has the effect of putting a creditor (or guarantor) in a position which, in the event of the company going into insolvent liquidation or the individual entering into bankruptcy, will be better than the position he/she would have been in if that act had not been carried out. The ability of the liquidator or trustee to challenge such transactions is subject to time limits, the financial position of the company/debtor at the time of the transaction, the relationship between the company/individual and the beneficiary of the transaction and the purpose of the transaction. Further on this issue Reinhard Bork, *Rescuing Companies in England and Germany* (Oxford University Press, Oxford 2012), para. 16-07 et seq.

[891] §§ 130 and 131 InsO.

[892] § 133 InsO.

[893] See German Federal Civil Court (BGH), 12.5.2016, IX ZR 65/14, NZI 2016, 636 explaining a serious restructuring attempt would require a solid restructuring plan.

[894] See the chapter in Germnay, in Bob Wessels & Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming).

c. sales, at market value, of real estate which is used as the purchaser's home, or that of his relatives to the third degree;

d. acts, payments and security over the debtor's assets provided that these have been entered pursuant to a plan which appeared to be capable of turning around the company from its liabilities and ensuring the rebalancing of its financial situation and on which a 'reasonableness' opinion was given by an expert;

e. acts, payments and security entered into or given pursuant to a composition with creditors (including a pre-insolvency composition);

f. payment of salaries to employees and fees to consultants;

g. payments of due and enforceable debts made in order to obtain services necessary to accede to the composition with creditors and controlled administration procedure.

520. The exemptions under (d), (e) and (g) specifically represent, without any doubt, an encouragement to try to restructure businesses in financial difficulties. In particular, the exemption under (d) is of a paramount importance since it introduces the concept of a turnaround plan on the debt side which was new under Italian law. Only the debtor can promote a turnaround plan. No specific requirements are set forth as for the financial conditions of the debtor. The turnaround plan can be kept confidential since no disclosure whatsoever (e.g. to the courts or the Register of Companies) is required, save for listed companies. Along the same line is the exemption (e) which does not make the acts etc. mentioned subject to claw back actions.

521. Concluding, under Italian law, payments or guarantees made in performing a certified rescuing plan (*piano attestato*), a rescuing agreement (*accordo di ristrutturazione dei debiti*), a concordato preventivo with creditors (*concordato preventivo*) or following an application for it are exempted from claw-back risk in any subsequent insolvency. This safe harbour applies to loans made by lenders offering new finance in support of a rescue plan confirmed or authorized by a court (either through a *concordato preventivo* or through an *accordo di ristrutturazione*).[895]

522. From the National Reports it seems that Spanish law provides for the most favourable rules of safe harbours. Here, certain refinancing agreements are protected against a clawback. Pursuant to Article 71 of the Ley Concursal (LC), in general, upon the commencement of the insolvency proceedings, acts detrimental to the debtor's assets performed within the two years before the declaration of the debtor's insolvency may be avoided, even in the absence of fraud, in merits of the clawback actions. However, refinancing transactions, and specifically the security taken in such restructurings, can be excluded from a clawback should the debtor be put under bankruptcy protection within the two-year period after its execution. The correspondents sum up under which conditions Article 71(bis) LC exempt Refinancing Agreements reached by the debtor from avoidance rules. Exempted from avoidance actions are:

1) the arrangements that leave a significant expansion of credit available or provides for the modification or termination of its obligations, either through extension of its maturity or the establishment of other obligations contracted to replace those if they

[895] See Article 67 Italian Insolvency Law. See for more detail Allessandro P. Scarso, 'Avoidance claims and turnaround of distressed business from an Italian perspective', International Insolvency Law Review 4/2013, p. 398 et seq.

comply with a viability plan that allows the continuity of professional or business activity in the short and medium term. Another condition is that the agreement was signed by creditors whose credits represent least three fifths of the amount of the debt on the date of adoption of the Refinancing Agreement. In the case of group arrangements, the prescribed percentage is calculated both on an individual basis, in relation to each and every one of the companies concerned, and a consolidated basis, in relation to claims of each group or subgroup in both affected and excluding cases of computation of liabilities on loans and credits granted by group companies;

2) any other agreement that accomplishes all the following conditions:

a) To increase the proportion of assets over liabilities prior;

b) The resulting current asset is greater than or equal to current liabilities;

c) The resulting value of securities in favour of the creditors involved does not exceed nine-tenths of the value of the slope for the same debt, or the ratio of outstanding debt guarantees they had prior to the agreement;

d) The interest rate applicable to the surviving or resulting debt Refinancing Agreement in favour of the creditors involved or not exceed by more than a third the rate applicable to prior debt; and

e) That the agreement was formalized in a public instrument executed by all parties to the same, and expressly stated the reasons, from the economic point of view, the various acts and transactions made between the debtor and creditors involved, with special reference to the described conditions.[896]

6.2.2 Significant international tendencies

523. The UNCITRAL Legislative Guide (2004) contains more than ten recommendations on avoidance actions. A general statement forms the opening: '87. The insolvency law should include provisions that apply retroactively and are designed to overturn transactions, involving the debtor or assets of the estate, and that have the effect of either reducing the value of the estate or upsetting the principle of equitable treatment of creditors.' It then sums up three types of transaction as avoidable, with additional suggestions, specifications and arrangements for suspect periods. The Guide seems to leave room for including safe harbour provisions, as its recommendation 92 provides: '92. The insolvency law should specify the transactions that are exempt from avoidance, including financial contracts', further explained in recommendation 97: '97. The insolvency law should specify the elements to be proved in order to avoid a particular transaction, the party responsible for proving those elements and specific defences to avoidance. Those defences may include that the transaction was entered into in the ordinary course of business prior to commencement of insolvency proceedings. The law may also establish presumptions and permit shifts in the burden of proof to facilitate the conduct of avoidance proceedings.'

6.3 Impetus for Recommendation

524. In accordance with the findings in the National Reports, we hold that pre-insolvency procedures that function as workout support mechanisms (type 1 – procedure; see Chapter

[896] See also Agustín Bou, 'New refinancing proceedings under Spanish Law', 8 Insolvency and Restructuring International, September 2014, p. 39 et seq.

1.2) should focus on their core function and not provide for additional tools of insolvency law like their specific avoidance powers. Following the contractual nature of a workout and the purely supportive function of the court, contracts and transactions of the debtor can be held void under contract law, but not under insolvency law rules.

525. With regard to safe harbours for workout agreements and (financial) transactions under these agreements, we find a common principle according to which avoidance rules under insolvency law should not apply in subsequent formal proceedings if a transaction (i) is objectively fair ex post, or (ii) justified ex ante (under the given circumstances) by serving the goal of restructuring a business, which is in its core viable.

526. Any transaction that does provide value at least equal to an amount received by the estate in exchange does not impair the estate and, thus, the right of creditors if done in good faith ex ante. A sale of a business unit or inventory for a market value should, therefore, be safe from later avoidance actions.

527. Transactions in a restructuring attempt that ultimately failed, which in a subsequent formal procedure (ex post) prove to be useless or costly (e.g. transfers for a distressed price; credit under higher interest rates; additional security rights) can be safe from avoidance actions if they were done in good faith ex ante and part of a restructuring plan that meets specific thresholds to safeguard minimum standards of turnaround management were met when stakeholders trusted in a restructuring. Such thresholds may include a significant creditor support and a court confirmation of a plan's sincerity; it may also simply comprise of a professional standard for restructuring planning (see Germany). Eventually, the rules in question need to safeguard that a workout agreement or plan does not only reflect the interests of affected creditors or the debtor, but also the interest of all stakeholders in a potential subsequent plan failure by testing the principal ability of the workout to ensure the survival of the business.

528. The test of a sufficient justification for a payment by the debtor to a third party or to a creditor or the debtor's conclusion of an agreement should follow from the circumstances in which the payment is made, respectively within which the legal act has been performed (ex ante view). These circumstances should be assessed in the light of the reasons for the relationship of the other party with respect to the debtor. At a practical level this results in a rule of evidence. In later formal insolvency proceedings, the IOH will have to prove that the other party at the time the payment was made or the agreement has been concluded (ex ante) knew or reasonably could have known that the payment/agreement was either not included in the restructuring plan or that the plan would not meet professional standards, and that the transaction would result in a disadvantage for the estate and future creditors.

529. For the sake of incentivising stakeholders to participate in workouts or continue trading with a troubled business, predictability and legal certainty is of the essence. Any risk of avoidance keeps business partners from investing in their relationship with the debtor (see Chapter 1.1.). Thus, avoidance rules (but also rules on lenders' or directors' liability) must be clear and predictable for everyone asked to continue making business with a debtor in a workout or supporting court proceedings. Thus, no party should feel uncertain about the validity of payments and actions in the ordinary course of business in a potential future

insolvency. Good faith only ends where it is demonstrated that the restructuring has obviously failed or a formal insolvency has been opened at the time of the transaction. If it turns out that the debtor (or: the parties) have agreed on a restructuring plan which – sometimes with the benefit of hindsight – turns out to have been too optimistic, any fear for a successful action by the IOH should firmly be redundant.

530. It must also be stressed that clearly defined safe harbours for workout transactions cannot protect fraudulent stakeholders. If it can be established ex post that the other party knew or should have obviously known that insolvency is inevitable at the time of the transaction, and that the creditors will be affected by it, lawmakers must ensure that avoidance rules apply. Under such rules, the third party is commonly allowed to show that there was indeed a (sufficient) justification for a particular act under the given circumstances. This occurs for instance (i) in transactions falling within the normal course of business or (ii) are otherwise customary. Examples would be: normal supplies or services at (cash) payment by suppliers and service providers who are aware of the troublesome situation and know that, technically speaking, a payment leads to disadvantage to the creditors. Another example is payment of fees to the attorney representing the debtor to assist in his defense to an application for declaration of insolvency and being paid for it.

6.4 Recommendations

Recommendation 6.01: In workout support proceedings, there should be no room for applying avoidance powers.

Recommendation 6.02: Member States should allow safe harbours for transactions made in the ordinary course of a debtor's business when concluded with the debtor during a formal restructuring or insolvency proceedings, including interim proceedings.

Recommendation 6.03: Member States should allow safe harbour for transactions made outside the ordinary course, such as new finance or new security rights for new finance lenders, only under the condition that these transactions are part of a restructuring plan which was approved by creditors and confirmed by a court.

Recommendation 6.04: Member States should ensure that a safe harbour rule is not available for transactions done in bad faith that disadvantage creditors in a subsequent insolvency. Member States should always allow for the recovery of fraudulent transfers (transactions in bad faith), even if there were based on a (now failing) plan.

Recommendation 6.05: When considering whether bad faith can be established for transactions in the ordinary course of business, account should be given to all circumstances of the case, including (i) the fact whether the debtor has demonstrated an early engagement with creditors, employees, shareholders and other stakeholders in reaching a solution to its financial troubles, (ii) has taken every reasonable step to properly and diligently try to avoid destruction of value, and (iii) has sought advice from a person that might objectively be considered to have has suitable business or industry experience and expertise and (iv) that the debtor conscientiously acted on the advice received.

Recommendation 6.06: Any safe harbour rule should be clearly defined so that parties can assess them in a predictable way when dealing with the debtor as well as during the negotiations and conclusion of a restructuring plan.

Recommendation 6.07: When bringing forward an avoidance action, the burden of proof should always be on the party that alleges that a wrong has occurred. Such a party is either the insolvency practitioner (or supervisor) appointed or a public institution such as a fraud office or public prosecutor.

CHAPTER 7:
Sales on a going-concern basis

7.1. Introduction

531. For many entrepreneurs, selling your business is an unique, once-in-a-lifetime event. Selling or transferring one's business to a third party is in many ways radical. First, in a rather irrational way: selling your business means goodbye to what has been built or continued for several years or for decades. Second, more rationally, entering into a selling process brings its own dynamics: informally attracting candidate buyers or find candidates via public marketing, exchanging business information, negotiation phase, a letter of intent, including clauses on confidentiality, due diligence, valuation and price-setting and the role of certain conditions precedent and guarantees in the entire proces, and finally closing the deal and transfer the business. In addition to its specific contractual clauses relevant for each individual sales process, other legal issues surround such a sale and transfer. On the buyer's side for instance the way to finance the acquisition, antitrust pitfalls, stock listing requirements or requirements for transferring public law permits, certifications and licences[897] or the uncertainly relating to the possible loss of carry forwards against taxation that may require the consent of third parties to be transferred, if they can be transferred at all). Some complexities on the seller's side could include matters of corporate decision-making, legal representation and the applicability of capital maintenances rules, whilst restrictions and limitations on a sale are usually imposed by the debtor's financing arrangements, may flow from arrangements with prime suppliers or may follow from applicable legislation, such as rules related to the transfer of an undertaking and the consequences for employees.[898] In many countries other restrictions may apply where the transfer is an intra-group activity and also ordinary rules on avoidance of antecedent transactions may apply, in such a way that a possible buyer of a (near to insolvent) business from a debtor sometimes will prefer a sale in a formal insolvency process, where these restrictions or rules do not apply, or only to a limited extend.

532. Evidently, in the Member States with its free markets economies, a sale of a business is a possibility if parties decide to do so. Where insolvency does not loom, the principle of freedom of negotiating (many times referred to as the principle of freedom of contract) is the dominant legal guidance. In principle parties are free to negotiate and come to an agreement, at any moment, with every possible contents, in any form, as long as mandatory law is maintained. Generally, succession of businesses takes place in two forms: (i) selling of the shares of the company that operates the business, or (ii) by selling the whole business or a large part of it (a group of assets, including contract positions, and liabilities, with the goodwill that goes with it). The buying party could be another company (to which the business of the selling company provides another geographical market or the strengthening

[897] ELI Member Consultative Committee member Dr V. Rétornaz provided as examples licences for mining, for permitting the debtor to create an ecological risk or dealing with restricted goods, which can be revoked if the holder is no more in sound financial situation or they cannot be easily transfered to an acquiring/surviving company. In this chapter, we leave aside that these requirements could lead to prefering the transfer of the shares of the distressed company, which inherently leads to the transfer of all the companie's assets, but including its liabilities.
[898] See above at 5.1.2.2.

in sophistication of its products or services), the company's management (termed as: management buy-out) or an outside investor.

533. Selling of a business or of an independent part of it can also be a tool for a restructuring or reorganisation. In practice, selling and transferring a business is called a work-out or a private work-out, a private sale in the shadow of a looming insolvency (or: in the shadow of insolvency law). In general UNCITRAL terms, the term 'reorganisation' is used. The following definition is provided: a reorganisation is the process whereby the financial well-being and viability of a debtor's business can be restored and the business can continue to operate, using various means possibly including debt forgiveness, debt rescheduling, debt-equity conversions and, our focus in this chapter, sale of the business (or parts of it) as a going concern.899 Such a sale would effect a business rescue by separating the viable business (assets) from the debtor('s entity) which would result in old debt remaining with the debtor.

534. In this chapter the focus is on such sale as a going concern, in the meaning of the sale or transfer of a business in whole or a substantial part by way of an asset sale. This phenomenon is opposed to a share deal, which would affect the transfer of the debtor's entity with the business, and it is different to a sale of all assets of the business piece by piece, which typically is an activity in the area of insolvency liquidation. In practice this method is called piece-meal liquidation. Within insolvency practice in Europe, already in 2003, sales as a going concern has been detected as an activity available in several Member States. The Principles of European Insolvency Law (2003) state in § 12.1: 'If and to the extent that there is no reorganisation, the administrator converts the debtor's assets into money and distributes it among the creditors. The assets can be realised separately or together, whether or not as a going concern.'[900] Recently soft law rules have been developed for cross-border sales.[901]

7.2 Procedures for going concern sales in National Reports

535. In the Member States, the applicable restructuring and insolvency laws have different scopes. In some situations, the influence of insolvency law is limited, in other circumstances selling of a business can take place within a formal insolvency proceeding. We describe some examples.

536. The Business Continuity Act of Belgium (BCA) of 2009 offers a debtor in financial distress in principle three informal and formal reorganisation tools to restructure its

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[899] UNCITRAL Legislative Guide (2004), para. 12, under B, "Glossary, Terms and definitions". UNCITRAL Practice Guide (2009), under B "Glossary", in "2. Terms and explanations".

[900] It remains undiscussed here that the UNCITRAL Legislative Guide regards sales as a tool of reorganisation, whilst the Principles seem to separate both.

[901] The EU JudgeCo Principles (2015), Principle 21 states: 'Principle 21 Cross-Border Sales

21.1. When there are parallel insolvency proceedings and assets are to be disposed of (whether by sale, transfer or some other process), courts, insolvency practitioners, the debtor and other parties should cooperate in order to obtain the maximum aggregate value for the assets of the debtor as a whole, across national borders.

21.2. Where required to act, each of the courts involved should make orders approving disposals of the debtor's assets that will produce the highest overall value for creditors.'

business. These are: (i) an amicable settlement; (ii) a collective reorganisation plan or (iii) a transfer of the enterprise or of its activities, in whole or in part, to third parties under court supervision. Under the latter two a transfer of (a substantial part of) the business can take place. The national correspondents of Belgium have explained in particular the transfer of business under court supervision (Articles 59-70/1 BCA). In this tool, the court can order the transfer of all or part of the activity of the debtor either with or without the debtor's consent. A court representative will manage the sale and transfer. Once a reasonable offer for the business activities has been selected, the court will hear the various stakeholders, including the creditors, and will approve, where appropriate subject to conditions, or reject the sale. Following the completion of the sale of the business, the creditors will be entitled to exercise their rights on the sale proceeds and the moratorium will end.

537. It is worth noting that the Belgian judicial reorganisation is not only open for a debtor facing an immediate or imminent continuity threat of its business, but also to a debtor that actually meets the formal conditions of bankruptcy. It has been an explicite choice of the Belgian legislator that even in the case in which a debtor that fulfils conditions for opening bankruptcy proceedings (i.e. the debtor has ceased payments on a permanent basis and can no longer obtain credit), he is entitled to file a request to open judicial reorganisation proceedings in view of saving the business continuity, provided that the court has not opened the bankruptcy proceedings yet.[902]

538. In England and Wales, an administrator has broad powers to do, as the English correspondents express, 'anything necessary or expedient for the management of the affairs, business and property of the company.'[903] In particular, an administrator has the powers set out in Schedule 1 to the Insolvency Act 1986, which includes the power to sell or otherwise dispose of the property of the company by public auction or private contract.[904] It is reported that administrators commonly sell substantially all of the company's assets as a going concern and most often in practice this would be achieved by way of a 'pre-packaged' sale. The ongoing evaluation of the rules surrounding pre-packs will be subject for discussion in para. 556 et seq. below.

539. In France and Germany too, sale of a (large part of) the business is, in some form or the other, is available, too. In France, the sale of substantially all of the debtor's assets on a going-concern basis is only available via pre-packaged plan in *conciliation*. In formal insolvency proceedings the sale of substantially all of the debtor's assets on a going-concern basis is a possible outcome. Such a sale must achieve three objectives: (i) the continued operations of the transferred business, (ii) the preservation of jobs, and (iii) the repayment of creditors.[905] In *safeguard* proceedings, a sale plan can only concern a part of the activity of the company and can only occur with the consent of the debtor.[906]

[902] Article 23, §3 BCA.
[903] UK Parliament: Paragraph 59(1), Schedule B1, Insolvency Act 1986.
[904] UK Parliament: Paragraph 2, Schedule 1, Insolvency Act 1986.
[905] Article L 642-1 of the commercial code.
[906] Article L 626-1 of the commercial code.

In Germany, an asset deal is mentioned in s 160 (2) No 1 of the German Insolvency Act. Such a sale fits well with the Act's general purpose[907] as it is intended to liquidate the debtors' assets. The German correspondents note that in practice many IPs make use of their powers to carry out such an asset-deal restructuring, meaning that they separate the business from the debtor, transfer it to a buyer (rescue company or third party), and distribute the proceeds from the sale among the creditors via the insolvency procedure. They observe: 'Asset deals are heavily favoured in practice, as they are meant to be quick, enable the administrator to effectively separate the assets from the companies' liabilities, and ultimately rescue the business and the jobs it provides. Often the asset deal is negotiated by the preliminary administrator and then immediately put into effect once the insolvency procedure has been started.'

540. In Italy, Article 186-bis of the Italian Bankruptcy Law provides for a *concordato preventivo*, aiming at the continuation of the business. Here the plan would provide for the continuation of the relevant business activity by the distressed company, the transfer of the business itself or the contribution thereof in one or more companies (even though newly incorporated), without prejudice to the possibility to liquidate the assets which are not necessary to carry out the business. In 2015 the exclusive right of the debtor to propose a *concordato* was limited by the right for creditors to file competing proposals, but also so-called competitive bids. Underlying rationale is to maximise the value of the debtor's assets to be disposed of under *concordato preventivo*. The option of a competitive bid will be further explored below.

541. In Greece, in a special administration regime, the highest bidder acquires all assets free and clear of all claims. The auction proceeds are used for the satisfaction of creditors' claims.

542. Of course, a going concern sale of (parts of the) business is also used in other Member States (like e.g. Hungary, the Netherlands, Latvia, Poland, Spain, Sweden). Under certain circumstances, the sale may transfer also a part of the debtor's liabilities in order to write off for tax reasons or to convert them into equity (debt-equity swaps).

7.3 Significant international tendency: Chapter 11 U.S. Bankruptcy Code

543. In its origin and theoretical underpinning Chapter 11 U.S. Bankruptcy Code is a rehabilitation or reorganization procedure. As explained[908], during the last two decades within Chapter 11 the method of sales of all or substantially all the business has been developed. Chapter 11 allows for sales both in the ordinary course of business as well as outside the ordinary course of business under section 363 U.S. Code.[909] In these cases, commonly, some or all of the debtor's property is encumbered or subject to the liens,

[907] § 1 InsO states, that the '… insolvency proceeding(s) shall serve the purpose of collective satisfaction of a debtor's creditors by liquidation of the debtor's assets and by distribution of the proceeds, or by reaching an arrangement in an insolvency plan, particularly in order to maintain the enterprise'.

[908] See Intro re Chapter 11.

[909] Parts of the text that are based on: Rolef J. de Weijs and Bob Wessels, 'The Reform of Chapter 11: Its Process and the Recommendations Made', in Bob Wessels and Rolef J. de Weijs (eds.), *International Contribution to the Reform of Chapter 11 U.S. Bankruptcy Code* (European and International Insolvency Law Studies 2, The Hague: Eleven International Publishing 2015), p. 3-40.

interests, and claims of various stakeholders. The holders of these liens, interests, and claims will obviously have rights under non-bankruptcy law or prepetition agreements that make the transfer of the debtor's assets difficult or less attractive to prospective lessees and purchasers. Moreover, these liens, interests, and claims can be rather broad. They may include mortgages, security interests, easements, or successor liability claims.[910] Under the current section 363(f) of the U.S. Bankruptcy Code, a debtor in possession (DIP) may sell its assets '… free and clear of any interest in such property of an entity other than the estate' under certain conditions.[911]

544. Section 363(f) is limited to '… any interest in such property.' In their interpretation U.S. courts generally follow two ways of interpretation: (i) the 'narrow' view, limiting the application of section 363(f) to liens, security interests, mortgages, and money judgments, and (ii) a 'broad' view of interests which also captures claims against the debtor or the estate property, including successor liability claims, discrimination claims and personal injury claims. The broader approach is by some seen as necessary to facilitate sales under section 363(f) and to achieve the underlying policy objectives of the Bankruptcy Code.

545. As the ABI Report of 2014 explains, U.S. bankruptcy courts have been increasingly willing to approve expedited sales of all or substantially all of a debtor's assets,[912] which can be regarded as a de facto liquidation of the company. Several recommendations in the ABI Report seek to increase creditor protection against possible suboptimal sales under section 363. The suggested renewals have led in the ABI Report to suggest a draft section 363x. The underlying rationale is that it makes little sense to provide ample creditor protection in coming to a reorganization plan under the traditional Chapter 11 approach, while excluding such protection from a sale of all or substantially all assets. Such a sale will be equally decisive for the final outcome for creditors as any plan.[913] Generally, the ABI Commission suggests in its recommendations that such a draft section 363x sales must (i) be in the best interests of the estate, (ii) comply with other applicable provisions of the Bankruptcy Code, (iii) be proposed in good faith and not by any means forbidden by law, (iv) satisfy in full certain allowed administrative expenses and claims (unless the holder of such claim agrees otherwise), and (v) provide for the payment of all court and IP fees.[914]

546. The concept of selling a business 'free and clear of any interest' deserves attention as – as demonstrated above – in the practice in quite in some EU Member States it is preferred to buy any business out of a formal insolvency proceeding instead of purchasing the business directly from a distressed debtor himself, since for instance any risks for claims arising out of transaction avoidance are excluded if the business is bought out of a formal proceeding. In the U.S., Chapter 11 can serve a similar purpose, but in addition to removing any concerns as to the avoidability of the sale itself, it also serves the purpose to ensure a sale 'free and clear' of all possible interest.

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[910] Successor liability claims are 'interests', see *In re Chrysler LLC* 576 F.3d 108 (2d Cir. 2009); U.S. Court of Appeals of the Second Circuit (*In re Motors Liquidation Co*., 2016 U.S. App. LEXIS 12848 (2d Cir. July 13, 2016).

[911] For an overview, see Kelly E. Porcelli, 'Finality of of Section 363 Sales in the Face of an Upset Bid', 24 ABI Law Review, Summer 2016, p. 497 et seq.

[912] Report, at p. 84.

[913] Report, at. p. 84.

[914] Any reimbursements or payments of costs and expenses incurred in connection with the sale (for example, to the buyer's advisors) must be subject to the approval of the bankruptcy court as 'reasonable'.

The ABI Commission recommends following the broad view (as explained above) to section 363(f). They submit two reasons: it fosters more competition for the debtors' assets and it is likely to enhance the value of the assets sold through the section 363(f) sale process. The ABI Commissioners further considered whether any particular liens, interests, or claims should be excluded from section 363(f) under this broad approach. They decided that the DIP should be able to transfer property free and clear of all liens, interests, and claims, including without limitation: civil rights liabilities; successor liability in tort; and successor liability in contract. In the context of the suggested draft section 363x sale, a trustee should be able to sell assets free and clear of any successor liability claims (including tort claims) other than those specifically excluded from free and clear sales by these principles. The Commission however also concluded that the DIP should not be able to transfer property free and clear of the following: '… easements, covenants, use restrictions, usufructs, or equitable servitudes that run with the land; environmental liabilities and related social policies that run with the land; successorship liability under federal labour laws; and partial, competing or disputed ownership interests'.[915]

547. As to the timing of a section 363 sales, the ABI Commission agreed that in many cases 363 sales occur too early and that such a sale can have three negative effects. Such a sale: (i) may not facilitate a robust action, (ii) may not allow the debtor sufficient time to explore restructuring alternatives, and (iii) may take advantage of bad market conditions. Because prospective purchasers (or lenders, or other parties in interest) may otherwise impose upon the debtor a requirement to obtain approval for a proposed sale within just a few weeks (or even within days, in some cases), the Commission proposes to bar these quick auctions and sales unless the debtor or a party in interest '… demonstrates by clear and convincing evidence that there is a high likelihood that the value of the debtor's assets will decrease significantly' within 60 days. The commission thus recommends a 60-day moratorium on selling all or substantially all of the assets, unless there is really a clear case of rapid value decrease, also referred to as 'the melting ice-cube'. Only on the basis of clear and convincing evidence detailing extraordinary circumstances, will an earlier sale be allowed by the court.[916]

548. From all the other recommendations the ABI Commission makes in this Report we focus on two of these: (i) the approval of a 363 sales, and (ii) the pay out of a Redemption Option Value to those creditors who would otherwise be 'out of the money'.

Creditor involvement in section 363x sales

549. Concerns regarding section 363 sales in present practice in the USA are that these sales bypass the notice and due protection that a plan under Chapter 11 provides and also that these 363 sales often are pursued before parties in interest which have adequate

[915] Moreover, the Commissioners recognised that a debtor in possession should not be able to sell or transfer assets under section 363(f) in a manner that violates or impedes the police or regulatory power of the federal government or a state government to the extent that such government could enforce those rights against the debtor in possession or estate property during the case.

[916] Report, at p. 86-87. For a Dutch approach to melting ice-cube cases see J.M. Hummelen, 'Het verkoopproces in een pre-packaged activatransactie', Tijdschrift voor Insolventierecht 2015/2.

information to assess the sale and will generally be informed on a debtors' restructuring alternatives[917] or the lack of these. The ABI Commission observes that such a practice is disadvantageous to creditors, as these sales may determine distributions to creditors without creditors having a vote or the protection of the fair and equitable standard which is applicable under a normal plan procedure.[918] In addition to the 60 day moratorium recommendation (mentioned above), the recommendation is made to put in place requirements for courts to lend their approval to such sales. In short, the Commission recommends that in case of a 363 sale, creditors should have similar protection as under adopting a reorganisation plan under section 1129.[919] For example, to sell all or substantially all of its assets, the debtor would be required to make certain evidentiary showings, provide broader notice to creditors, and pay certain administrative expenses, all similar to a plan proponent's obligations under section 1129(a).[920]

Redemption option value

550. In U.S. practice, after a reorganisation, there is hardly any money left, if at all, for the unsecured creditors. The ABI Commission recommends allocating some value to the unsecured creditors. The class that just misses out is referred to as the 'immediately junior class.' The basic idea of the recommendation here is that the immediately junior creditors are entitled to the value of a redemption option. This option seeks to recognize that the immediately junior class might have been in the money or at least would have received a greater recovery if the business had been valued at a later date.[921] The immediately juniors would be entitled to the value of the option, regardless of whether there would be an actual plan adopted or whether a 363x sale would be conducted.[922] Thus, the ABI Commission introduces an entitlement of the immediately junior class to the amount that reflects the value of a redemption option. The redemption value option seeks to remedy the divergence of interests between creditors or at least appease the immediate out of the money group of creditors and thereby prevent lengthy and costly litigation. The value of the option would need to be calculated as (a) what a party would pay if he could buy all the assets in three years' time against paying in full the senior class[923], and (b) the value should be provided not by the buyer, but by the higher ranking creditors or at least paid out of the estate.[924] The 'value' in any given case may be negligible or non-existent; it does not provide for a percentage or fixed payment to junior creditors.[925]

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[917] Report, at p. 202.
[918] Report, at p. 202.
[919] Report, at p. 206
[920] See M. Harner. 'The Melting Ice Cube Fallacy', Credit Slips, January 25, 2015, available at http://www.creditslips.org/creditslips/2015/01/the-melting-ice-cube-fallacy.html.
[921] ABI Report (2014), at p. 214 and 218.
[922] ABI Report (2014), at 224. However, SMEs are excluded in the recommendation.
[923] The redemption price of the option would therefore be the full face amount of the claims of the senior class. ABI Report (2014), at p. 221.
[924] ABI Report (2014), at p. 223. The Commission expects that any redemption option value would not be in the form of an actual option, rather in the form of cash, debt, stock or warrants (with the form of such consideration being at the sole election of the senior class being required to give up such value) and that the redemption option value in any given case may be negligible or non existent, as it is not a percentage or fixed payment to junior creditors.
[925] ABI Report (2014), at p. 208. In an example the Commission explains where the redemption value does come into play a situation where secured creditors receive 90%. Depending most notably on the actual

551. A likely argument against the redemption option would be that if the valuation has actually been subject to competitive market testing, all future market developments should indeed already have been actually factored in.[926] The Commission seeks to counter this argument in advance by submitting that the economy shows cycles of three to five years, and that the fixed redemption period of three years should therefore adequately address potential unfairness.[927]

552. In European literature it has been submitted that the recommendation on the redemption value option provides a remedy for a different problem than the problem identified by the Commission.[928] The following quote best captures the underlying rationale of the Commission proposing the redemption option: 'Outside bankruptcy, the secured lender may have considerable difficulty capturing anything above liquidation value. If the bankruptcy process itself allows the recovery of more value, why should all of that bankruptcy-enables excess go to the secured lender.'[929] The authors mentioned submit that the real problem is not so much the realisation of value and the timing thereof, but rather the general spread of secured credit increasingly leaving too often unsecured creditors with nothing at all. If this view is correct, the much easier way to remedy this would be to go back to the debate about a full application of the APR – an ongoing debate conducted in the US for some twenty years now.[930] The question of full priority turns on whether secured creditors in all circumstances receive 100% of the encumbered assets up to the value of their claims. It would be conceptually and practically much easier to limit secured creditors claims to a certain ceiling, say, 90% and always providing a part for the estate to be distributed. A fixed percentage as prescribed part would adequately and under all circumstances provide for a sharing in the benefits of the bankruptcy process.

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recovery rate of the senior class, the option value would be higher or lower. The higher the pay out to secured senior creditors, the more valuable the redemption option. Given a certain market volatility of 15% and a specific risk free rate based on the US Treasury rate of 2.2%., the Commission calculates the value of the redemption option under a 80% recovery on senior debt to be 2% of the reorganisation value, increasing to 5.3% of the reorganisation value in case of a recovery rate of 90%. The sums of money involved might be significant. In case of a reorganisation with assets worth € 200 million, € 10 million would go to unsecured creditors if the senior creditors receive 90%. In the bigger picture, the redemption option however does not provide a real shift in the relative positions of secured and unsecured creditors, especially not since the option only comes into play in case of high pay outs to secured creditors.

[926] See also the Commission itself with an immediate rebuttal (ABI Report (2014), at p. 214): 'Although the price being offered for a debtor's assets in a section 363 sale arguably reflects the current market value of those assets, to the extent the market is dysfunctional at the time of the sale, or economic or industry factors are negatively impacting valuations, the debtor's estate may be monetized at value far below what the estate could be worth at a later date to the prejudice of stakeholders lower in the pecking order of priorities.'

[927] ABI Report (2014), at p. 220.

[928] Rolef J. de Weijs and Bob Wessels, 'The Reform of Chapter 11: Its Process and the Recommendations Made', in Bob Wessels and Rolef J. de Weijs (Eds.), *International Contribution to the Reform of Chapter 11 U.S. Bankruptcy Code* (European and International Insolvency Law Studies 2, The Hague: Eleven International Publishing 2015), p. 3-40.

[929] See Commission (ABI Report (2014), at 223) quoting C.J. Tabb, 'The Bankruptcy Clause, the Fifth Amendment, and the limited rights of secured creditors in Bankruptcy', Illinois Law Review 2015, p. 5. At the moment of finalising the report this article was forthcoming.

[930] See most notably L.A. Bebchuk and J.M. Fried, 'The Uneasy Case for the Priority of Secured Claims in Bankruptcy', 105 Yale Law Journal 1996, p. 857 and 'The Uneasy Case for the Priority of Secured Claims in Bankruptcy: Further Thoughts and a Reply to Critics', 82 Cornell L. Rev. 1997, p. 1279. For the current debate, see Douglas G Baird, 'Priority Matters, 165 U. Penn L. Rev., (forthcoming), also available at https://ssrn.com/abstract=2767055.

553. In North-American literature also other proposals have been made to allocate a certain portion of value to a group of persons in interest. We focus on two of them.[931] Where the ABI Commission tries to counterbalance to chosen time of valuation, Jacoby and Janger[932] propose to address concerns with the amazing speed these 363 fire sales have, to the detriment of certain interests. These authors submit that a court should routinely withhold '… a portion of sale proceeds from claimants who would otherwise receive a distribution – usually, but not always a secured creditor.' These authors certainly wish to retain quick 363 sales as a useful tool to preserve value in moments of true crisis, but they propose an 'Ice Cube Bond' to address the concerns mentioned, to preserve the opportunity for judicial and stakeholder deliberation to ensure that value is maximized and properly allocated.[933] Looking for a justification, the authors regard a quick all-asset sale under section 363 as a procedurally irregular disposition of the estate. A pre-packaged plan with votes already solicited early in the process of case without disclosure or actual voting, serves as a 'rebuttable presumption of being a procedurally irregular sales.'[934] The buyer then can rebut the presumed irregularity if he can show that the irregularity did not depress the sales price. The Ice Cube Bond essentially mirrors this approach for a quick all-asset sale under section 363. A portion of the quick-sales price could be reserved as presumptively unencumbered funds, to preserve issues of valuation and allocation for later determination. The suggested method, the authors argue, separates negotiations towards a plan that is final and results in the purchase of clear title to the assets, and on the other hand the method of distribution, and therefore reflects a separation between governance and value maximisation. The authors acknowledge that the Ice Cube Bond needs the determination of a certain percentage to hold back. Having a post-judicial determination, including at what moment and how to release the fund covered, the authors predict that post sale negotiations will dispense with many of these issues. Moreover, it should be noted that the cost of the Ice Cube Bond can be avoided entirely: the debtor (and its lenders behind the scenes) simply must conduct the sale pursuant to a plan, pre-packaged or otherwise.

554. Another view has been developed by Harner. It is not related to the time of valuation of the assets or the procedural speed of the sales process, but to the value itself as mirroring the price paid by the buyer. She has asked herself the question: when a company is worth more as a going concern than on a liquidation basis, what creates this additional value? Her answer suggests several sources of it: 'Is it the people, management decisions, the simple synergies of the operating business, or some combination of these types of soft variables? And perhaps more importantly, who owns or has an interest in such soft

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[931] Critique also has led to an alternative, an 'automatic bankruptcy procedure' that gives senior creditors an option to restructure the firm's debt or sell its assets at any time after a contractual default. Under this procedure, restructuring occurs in bankruptcy, but sales do not. Sales are either subject to warrants (which give junior stakeholders a claim on future appreciation) or are subject to judicial appraisal (which forces senior lenders to compensate junior stakeholders if the sale price was too low). See Anthony J. Casey and Edward R. Morrison, 'Beyond Options', available at https://ssrn.com/abstract=2855954, draft chapter to be published in Barry Adler (ed.), Corporate Bankruptcy Handbook, Edward Elgar Publishing (forthcoming in 2017).

[932] Melissa B. Jacoby and Edward J. Janger, 'Bankruptcy Sales', available at http://ssrn.com/abstract=2809764, draft chapter to be published in Barry Adler (ed.), *Corporate Bankruptcy Handbook* (Edward Elgar Publishing, forthcoming in 2017).

[933] The authors explain that the concept is standard practice in non-bankruptcy cases in the USA for courts to require an injunction bond to help preserve issues for later litigation.

[934] Jacoby and Janger compare this notion with the irregular sales of personal property collateral under Article 9 of the Uniform Commercial Code (UCC).

variables?'[935] Harner explains that in corporate reorganisations, where a company's liabilities frequently exceed the value of its assets, the value available to satisfy creditors' claims is limited. It is her opinion that these 'soft variables' contribute meaningful value to the operation of a company as a going concern but are often overlooked or undervalued in corporate reorganisations. In her opinion ignoring soft variables not only does a disservice to those working hardest to save the company but also arguably steals value from the company and those constituencies. If a company's soft variables do not hold such value, it may indicate that a chapter 7 liquidation is the more appropriate resolution for the company, Harner argues, stating that if the company invokes the chapter 11 process and the resolution generates value above liquidation or book value, the court and the parties should identify the relevant soft variables and allocate value accordingly.
In her opinion in the context of a going concern sale or reorganization some portion of the value derives from variables which value is not included in the prepetition collateral package: 'A company's people, and their ideas, decisions and relationships – soft variables – are not property of the debtor and should not be subject to a secured creditor's security interest unless and until value is generated by those variables. If that value is triggered by an event outside of bankruptcy, that value is personal property to the company and may be subject to an after-acquired property clause. To the extent that value is triggered after the filing of a bankruptcy case, however, that value should be unencumbered subject to the caveats discussed above. Moreover, an allocation scheme that distributes such value to parties contributing to its creation – a contributory priority scheme – likely would align the incentives of the company, the secured creditors, and those responsible for generating value from soft variables to maximize the value of the company. In those cases, where a company's soft variables increase the value of the going concern, the people and the process have done their job and should be rewarded accordingly.'

555. Finally, a suggestion made by the ABI Commission in the context of Chapter 11 proceedings, but of importance to the sales process: the availability of basic information. The ABI Commission stresses that a debtor's timely and full disclosure is a necessary component of the Chapter 11 process. Without this basic information, the court, the U.S. Trustee, and parties in interest cannot assess the debtor's reorganization efforts and make meaningful decisions in the case. We submit that the same is true for a sales process. Under current U.S. law, a debtor is required to file some, but not necessarily the most relevant financial data early in the chapter 11 case. It is, however, possible that the court orders otherwise. The ABI Commission suggests for companies that do not categorise as a small or medium-sized enterprise, that the debtor should compile a "valuation information package" ("VIP") containing the following information: (i) tax returns for the previous three years (inclusive of all schedules); (ii) annual financial statements (audited if available) for the prior three years (inclusive of all footnotes); (iii) most recent independent appraisals of any of the debtor's material assets (including any valuations of business enterprise or equity); and (iv) to the extent shared with pre-petition creditors and existing or potential purchasers, investors, or lenders, all business plans or projections prepared within the past two years. As a general rule within 60 days after the petition date (or date of the order for relief,

[935] See Michelle Harner, 'The Value of Soft Variables in Corporate Reorganizations', 2015 Ill. L. Rev. 2015 U. Ill. L. Rev. 509.

whichever is later), the debtor should file with the court a list of the information included in its VIP, unless the court orders otherwise for cause.[936]

7.4 Pre-packaged sales

7.4.1 Introduction

556. A second question posed to the National Correspondence to the project has been: is it possible for a 'pre-packaged' sale to be achieved? The Questionnaire generally describes a 'pre-packaged' sale as a method in which the contract for sale is negotiated confidentially prior to the commencement of an insolvency procedure, without consultation with all creditors, which takes effect immediately on the commencement of the formal proceedings.

557. With more detail a pre-pack (or: pre-packed sales) is the name for a figure announcing the intention to sell a business (or a substantial part of it), including all assets (or those related to the substantial part). This is laid down in an agreement fully agreed by the debtor and a third party. The agreement is concluded before the date of opening formal insolvency proceedings. On the opening of these proceedings an IP will be appointed (which generally is the person that assisted in the negotiations up to the agreement). Because everything is prepared properly, well 'pre-packed', it is possible that within 24 or 48 hours after the formal commencement of the proceedings the appointed IP sells the business in conformity with the applicable rules of the insolvency legislation and the terms in the agreement and that the third party is able to continue the company with 'business as usual'. In result, generally, it is the same business (minus some liabilities), but now run by another entrepreneur.

558. The advantages are clear: a 'pre-pack' is very effective and framed in a relatively short process to get the best deal for the creditors, which in many legislations is the main task of an appointed IP. In addition to being quick and smooth, a rescue in the form of a passing over of the business to a third party is beneficial for the continuity of the company, without interruption of its pending (and remaining in force) contacts with suppliers and service providers[937], as well as its customers. Employment is maintained and, just as important, the continued payment of the company's taxes (such as corporate tax and VAT) is upheld. Furthermore, a pre-pack will result in a reducing of the costs of formal proceedings and offers deal-certainty. It will minimise the erosion of supplier, customer and employee confidence that is inevitably caused by formal insolvency proceedings, as the business is transferred into new ownership before news of the debtor's insolvency is made public.

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[936] ABI Report (2014), p. 42 et seq. A party in interest may request a copy of the VIP for a proper purpose, which includes the evaluation of the pending motion or proposed plan. The ABI Commission suggests that unless the court orders differently, the debtor should provide a copy of the VIP promptly to any such requesting party, provided that the party executes a confidentiality agreement and, to the extent that the VIP contains material non-public information, agrees to restrict its trading activity in the debtor's claims, interests, and securities. The debtor should be able to redact or withhold information otherwise included in its VIP to the extent that the debtor determines in good faith that such redaction is necessary to prevent harm to the estate, unless the court orders otherwise.

[937] It is of course required that counterparties agree with such a transfer.

559. It is noted that a pre-pack has similar characteristics as a negotiated (private) workout. The key difference is that in the pre-pack sales process a third party is involved. As an example we use the involvement of a court as in a pre-pack the sales process must be checked on requirements such as (i) has a majority of creditors been informed in time and with sufficient information, (ii) has the business been marketed to interested third parties, but also (iii) can after the formal commencement of insolvency proceedings the court assess and/or decide on privileges available for assets sales, such as a safe harbour from avoidance actions. A pre-pack functions similar as a pre-insolvency procedure or hybrid procedure. It deserves support for its positive effects, but also scrutiny for the price a buyer pays.

7.4.2 Significant elements from National Reports

560. In Austria, in Reorganisation Proceedings and Reorganisation Proceedings with Self-Administration, it is possible that the debtor together with a potential investor/acquirer contacts (a limited number of) creditors prior to the opening of insolvency proceedings and negotiate a deal involving the sale and the approval of a reorganisation plan beforehand. The formal requirement is that there is a required majority to approve such reorganisation plan. However, there would still be the risk that the insolvency court does not confirm the reorganisation plan approved by the creditors in case that the reorganisation plan is contrary to the mutual interest of the creditors or in case other mandatory prerequisites are not met. In Belgium a rather similar situation exists. Its legislation does not provide for specific rules on pre-pack deals, except for the rule that a proposal of potential buyers who enjoy specifics rights which are crucial for the business activity (e.g. IP rights), can only be taken into account when such rights are made available by the debtor under the same conditions to other potential buyers. A pre-pack is possible, however it will be difficult to construe because the representative appointed by the court needs to search the market – preferably by using a tender mechanism – for the best offer available to sell the business. Furthermore, the Belgian correspondents report that there is no guarantee that this representative is will be convinced that this offer it to its satisfaction.

561. In England and Wales a pre-pack sale is not possible in a contractual workout, scheme of arrangement or company voluntary arrangement as these proceedings are all pre-insolvency. However, when combined with an administration process, a pre-pack is available and their use in administration is growing. English courts have recognised that a 'pre-packaged' sale is a legitimate restructuring tool in appropriate circumstances.[938] It is reported that administrators commonly sell substantially all of the company's assets as a going concern and most often in practice this would be achieved by way of a pre-packaged sale.[939]

In the English practice, the role of practitioners in achieving reliable and successful pre-packs is eminent. English administrators are subject to professional guidelines that relate specifically to 'pre-packaged' sales. The well-known Statement of Insolvency Practice 16 (SIP 16) sets out required practice for administrators who are acting on pre-packaged sales. SIP 16 was introduced in 2009 in response to concerns expressed by creditors about these types

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[938] *DKLL Solicitors v Revenue and Customs* [2007] EWHC 2067 (Ch).

[939] See also John Wood, 'The Sun is Settting: Is it Time to Legislate Pre-Packs?', August 1, 2016, available at https://ssrn.com/abstracts=2852318.

of transactions. These concerns included: (i) lack of transparency of the sales process and the lack of accountability by the administrator, (ii) failure to maximise returns for unsecured creditors, and (iii) the inherent conflict of interest of the proposed administrator. SIP 16 sets out a detailed list of the information which the administrator should disclose to creditors where there has been a pre-packaged sale. Although SIP 16 is not legally binding, failure to comply with it could result in an administrator facing regulatory or disciplinary action. The Insolvency Service monitors the reporting by insolvency practitioners of pre-packaged sales to creditors, with a view to ensuring compliance with SIP 16. Some of the Insolvency Service's proposals to improve the pre-pack administration process will be discussed below.

562. In 2014, in France, it is reported, that in *conciliation* proceedings a 'pre-pack' is an option for the conciliator, upon request by the debtor and after consultation with the creditors. He then can arrange a partial or total sale of the business which could be subsequently implemented in the context of further safeguard, reorganisation or liquidation proceedings.[940] The contract for the sale plan is therefore negotiated during the *conciliation*, and when ready, the *redressement judiciaire* is opened so that the sales plan can be adopted by the court. The conciliator may, at the request of the debtor and after hearing the opinion of the participating creditors, be entrusted with the mission of actually organizing a partial or total sale of the business of the company. Any offers received in this context by the *mandataire ad hoc* or the conciliator may be directly submitted to the court in the context of reorganization or liquidation proceedings, subject to the supervision of the public minister whose opinion shall be requested. It enables the conciliator to directly submit to the court once the *redressement* or liquidation is opened the offer made by the identified buyer. It is subject to the supervision of the public prosecutor whose opinion needs to be requested.

563. After some two years of practice the following advantages have been acknowledged: (i) the reduction of the length of the proceeding, (ii) the avoidance of the risk of depreciation of the value of the assets, (iii) the involvement of creditors in the process, and (iv) the possibility to get better bids. However, downsides were noted too: (i) the method is not suitable where dismissal of employees is required, and (ii) the risk of opacity regarding the selection of bidders.[941]

564. A similar arranged pre-packaged sale is available in Spain[942] and in Sweden, although in the latter country the exception exists regarding movable property which, as a rule of thumb, is to be sold at auction without any specific permission from the creditors, except in those cases where there is a likelihood of a higher price being realised by way of a direct or 'pre-packaged' sale, which has been approved by the bankruptcy regulator.

565. In Germany, interim proceedings are commonly used by the interim administrator to pursue a bidding process and negotiate a business (asset) deal within the three months of such proceedings. Thus, on the very day of commencement of regular insolvency proceedings, the newly established creditors' committee is asked to approve the deal and the "pre-pack" is closed.

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[940] Article L 611-7 of the commercial code.
[941] Speakers A and B during a discussion on this theme in Leiden, 16-17 November 2016.
[942] Article 191 ter.2 LC.

566. For Italy it has been reported that it is very unlikely that a sales contract is negotiated confidentially prior to the commencement of an insolvency procedure, without consultation of all creditors and that such a contract takes effect immediately on the commencement of the formal proceedings. Usually the debtor enters a business lease contract either prior to admission to the *concordato preventivo proceeding*, without consultation with creditors; or following admission to the *concordato preventivo proceeding*, subject to the authorisation of the competent court or of the deputy judge. The business lease contract usually contains a put option in favour of the debtor, subject to verification of the concordato preventivo proposed to the creditors.[943]

567. Another tool (named 'competitive bid') is available, too,[944] and governs a pre-pack in which the proposal for the agreement already acknowledges the existence of a prior bid (negotiated prior to the commencement of the procedure) submitted by a specifically identified third party for the purchase or lease (*affitto di azienda*) of the business, or part of the business, or an offer to acquire one or more assets. The Court must provide for competitive biddings (*procedimento competitivo*) and decide on it.[945] The auction must terminate before the creditors vote for the plan. Also creditors who represent at least 10% of the overall indebtedness can file a proposal and a plan for the rescue of the business if, according to the plan of the distressed enterprise, the unsecured creditors (*creditori chirografari*) will receive less than 40% of the overall credit. In order to present the plan, creditors must receive all the relevant information from the Insolvency Practitioner (*Commissario giudiziale*).[946] All the proposals and plans are voted by the creditors. The 2015 reform in Italy also introduced a minimum cap in case of preventive settlement with creditors aimed at the liquidation of the business (*concordati preventivi liquidatori*): the plan of liquidation must grant to the unsecured creditors (*creditori chirografari*) at least the payment of 20% of the credit of unsecured creditors.[947]

568. In other countries, a pre-pack itself is not available. Pre-commencement agreements may be subject to the full application of rules on avoidance (Germany, Hungary) or suffer ineffectiveness (Poland). In Greece, a pre-pack is available only as a possible recovery measure, is subject to all recovery proceeding requirements and takes effect only upon ratification. In Latvia it is only possible to sell the business two months after the commencement of the insolvency proceedings and after the plan of sale has been presented to all creditors.

7.4.3 Significant international tendencies

569. A 'pre-pack' as such has not been included in international reports that focus on formulating recommendations for national legislators. What can be seen as significant is that

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[943] Article 186-bis of the Insolvency Act of Italy prescribes in quite some detail what a proposed plan should entail.

[944] Governed by Article 163-*bis* of the Insolvency Act and introduced by Article 2 of Decree-Law 83/2015.

[945] See for the way the court has to set rules for competitive bidding Bob Wessels & Stephan Madaus (eds.), *Business Rescue in Europe, Vol. I. National Reports and International Recommendations* (publication forthcoming).

[946] Article 165.

[947] Article 160.

practitioners involved in preparing and concluding pre-packs do exchange views as we have noticed, for instance, for practitioners in the Netherlands and England & Wales.

570. As an example the situation in the Netherlands is explained. The practice of the use of pre-pack started in 2013, without a clear foundation in the Dutch Bankruptcy Act, but with the support of eight (out of eleven) district courts. This remarkable split was a signal of the not uncontroversial nature of the 'Dutch pre-pack'.[948] In literature and practice it has been reported that (i) the negotiation process before the opening of formal proceedings is not transparent; it is unclear whether smaller creditors are informed or involved. It is also unclear (ii) how the choice is made with regard to the people who will continue their job and those that are fired, (iii) there are concerns for 'phoenix sales'. A phoenix company that acts as third party buyer could have close ties with the owners (shareholders) of the selling company, actually be the 'OldCo' owners themselves, represented in the buyer (a 'NewCo'). For this reason (iv), it is possible that a distortion of competition may occur. There are plenty of normal market forces to determine the value and price paid by the successor who is not a 'phoenix' (the debtor, but now in form of buyer).[949]

571. Illuminating the UK discussion: It is acknowledged that for other Member States the English pre-pack practice has served as a practical and useful example for selling a business in the vicinity of insolvency, with the appropriate protection of the interests of stakeholders, in particular creditors. In describing the practice in England and Wales mention was made of the practical and forceful meaning of the (non-binding) rules in the English Statement of Insolvency Practice 16 (or: SIP 16). As per 1 November 2013 new (non-binding) rules in SIP 16 have come into effect. The leading principle is that insolvency administrator should be transparent in every aspect of a pre-pack administration sales. He or she should give a clear, full and timely (7-day notification limit) statement. SIP 16 also contains pre- and other post-appointment duties.

572. In June 2014, the British Government published the findings and recommendations of an independent review into the practice of pre-pack administrations.[950] According to the report, on the positive side the result was that a pre-pack: (i) can preserve jobs; (ii) can be cheaper than formal insolvency proceedings (such as a scheme of arrangement); (iii) may well succeed where a purchaser pays for the business over a period of time, rather than on the date of the purchase.[951] The report also notes the downsides of a pre-pack, such as (i) pre-packs lack transparency before the sale as the parties work to secure the future of the business without risking the confidence of creditors, customers and employees, (ii)

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[948] Leaving aside that the premise of a pre pack of value creation or value preservation of the company and continuation of employment, as far as we know, never has been empirically investigated.

[949] Other questions: is a practitioner appointed by the court to assist the debtor during its negotiations for a pre-pack, when during formal proceedings the courts appoint will appoint him as insolvency office holder, sufficiently independent (in both capacities)? Can the appointing judge, act as a judge in a subsequent formal insolvency proceedings. Is he or she sufficiently independent? Regarding the 'phienix syndrome', see Bo Xie, *Comparative Insolvency Law: The Pre-pack Approach in Corporate Rescue* (Edward Elgar Publishing 2016), 122 et seq.

[950] The review was carried out by Teresa Graham CBE, available at https://www.gov.uk/government/publications/graham-review-into-pre-pack-administration.

[951] The Graham report also mentioned that the UK economy may profit form pre-packs Overseas companies may seek to move their 'centre of main interests' (COMI) to the UK in order to avail themselves of the flexible restructuring, insolvency and company legislation in the UK.

marketing of pre-pack companies for sale is insufficient, (iii) more must be done to explain the valuation methodology, and (iv) there is insufficient attention to the viability of the purchaser.[952]

573. The report presents six recommendations, four of them being substantial in nature. These are in short the following:

> *1. Pre-pack pool*
> It is suggested to create a pre-pack pool of experienced business people where, on a voluntary basis, details of a proposed sale to a 'connected party' could be disclosed to an independent person prior to the sale taking place, the aim being to increase transparency and give greater confidence to creditors that the deal has undergone independent scrutiny.
>
> *2. Viability review*
> Request connected parties – on a voluntary basis – to complete a 'viability review' for the new company, stating how the company will survive for at least the next 12 months. A short narrative will also be provided, detailing what the new company will do differently from the old company in order that the business does not fail again.[953]
>
> *3. Good marketing*
> All marketing of pre-pack businesses should to comply with six 'good marketing' principles in order to maximise sale proceeds and that any deviation from these principles be brought to creditors' attention.[954]
>
> *4. SIP 16 amendment*
> SIP 16 should to be amended to require valuations to be carried out by a valuer who holds professional indemnity insurance ('PII'), to increase confidence that the sale is for a fair price.[955]

574. At this juncture, we just touch upon the Small Business Enterprise and Employment Act 2015, which came into legal effect in the United Kingdom in May 2015.[956] From the many topics it covers, for present purposes it suffices to mention that Part 10 of the Act creates a reserve power to make regulations to either prohibit administration sales to connected parties or make regulations to impose conditions or requirements to allow a connected

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[952] 'The insolvency practitioner has no legal requirement to look at the future viability of the new business emerging from a pre-pack sale. His/her only legal responsibility is to the creditors of the old business. However both public perception and our research suggest that future viability, especially in the case of connected party pre-packs, is a concern for both transferring suppliers and new ones. Again … more could be done to demonstrate the potential viability of the new business/company emerging from the pre-pack.'
[953] According to the Graham report, a new company in a connected pre-pack is more likely to fail than a new company unconnected with those controlling the old company. Empirical evidence shows that there is a clear link to future failure in connected party cases.
[954] The report contains (p. 12) a set of 'Six Good Principles of Marketing'.
[955] The report suggests an adaption procedure for a redrafted SIP statement and suggest monitoring of these statements to be taken away from the Insolvency Service to be picked- up instead by the recognised professional bodies (RPBs).
[956] For its text, see http://www.legislation.gov.uk/ukpga/2015/26/contents/enacted. See Sacha Stiegler, 'Der britische Small Business, Enterprise and Employment Act 2015', ZIP 38/2016, p. 181 et seq.

party administration sale to proceed. Should the non-legislative solutions in respect of administration sales to connected parties recommended by the independent Graham review not change behaviour/increase confidence in such sales, it may be necessary to exercise the power.[957]

7.4.4 Impetus for Recommendations

575. Any business rescue by going concern sales requires (1) a bidding process, (2) a tool to leave debt behind (asset deal free and clear, or share deal in a restructuring plan – see Ch. 8 for latter), and (3) a tool to test the agreed price (court scrutiny of the bidding process or creditor approval of the price). Pre-packs use these effects in an accelerated manor and with reduced transparency which results in more doubts on the adequacy of the price, in particular in case of an insider deal.

576. Taking into account the developments described above, we are convinced that any restructuring and insolvency framework must comprise a robust going-concern sale option. Such a sale could form the core of a rescue plan (share deal), but it can also – and often even more efficiently – be done in an auction. While the latter option has received support recently,[958] we hold that any restructuring and insolvency framework should make both options available.

577. An asset deal in such a framework must leave 'old debt' behind by having it remain with the debtor (sale free and clean). This, however, also means that contracts of the debtor would only be assigned to the buyer if counterparties in these contracts actually agree.[959]

578. A going concern sale in such a framework will inherently impair the rights of creditors as it deprives them of the debtor's assets while leaving them only the purchase price. As a minimum requirement, we suggest that an independent expert should be in charge to supervise the auction process and to ensure a market price. This could be an independent insolvency practitioner, appropriately regulated[960] and appointed by the court, or a third party instructed by the court. In addition, it seems appropriate to require the creditors to

[957] For a House of Commons briefing paper (Number CBP5035) of 20 January 2016, on Pre-pack administrations and the changes Small Business Enterprise and Employment Act 2015 has brought, go to: www.parliament./uk/commons-library, or try: http://researchbriefings.files.parliament.uk/documents/SN05035/SN05035.pdf. For a discussion of the six recommendations in the Graham report, see John Wood, 'The Sun is Settting: Is it Time to Legislate Pre-Packs?', August 1, 2016, available at https://ssrn.com/abstracts=2852318. See for an overview: Paul J. Omar and Jennifer Gant, 'Corporate rescue in the United Kingdom: Past, present and future reforms', 24 Insolvency Law Journal 2016, p. 40 et seq.

[958] See G. Ray Warner, 'Reimagining Rescue: The View from the United States', in Rebecca Parry and Paul Omar (eds.), Reimagining Rescue, INSOL Europe, Nottingham Paris 2016, p. 175-186; Horst Eidenmüller and Kristin van Zwieten, 'The Future of Restructuring Law in Europe: Greater Harmonisation, but at What Cost?', Oxford Business Law Blog, 2016, available at https://www.law.ox.ac.uk/business-law-blog/blog/2016/12/future-restructuring-law-europe-greater-harmonisation-what-cost, criticising the Proposal Restructuring Directive (2016) for the disregard for this latter option.

[959] See for employment contracts Chapter 5.

[960] See above at 1.1.4.

approve such a sale through their representative, usually the creditors' committee (as it is being done in Germany).[961]

579. The basic rationale of a pre-pack can wholeheartedly be supported. A pre-pack speeds up the restructuring process, reduces costs and – in general – on a macro level is supportive to general welfare, as it maintains continuous tax payments to the State and saves employment, as the business continues with hardly any interruption. The disadvantages have been displayed. These downsides of a pre-pack must be addressed by reporting duties (about the transparency of bidding process and availability of concurring purchaser) to the stakeholders who get to decide on the sale: a court or, preferably, the creditors themselves (committee or meeting).

7.4.5 Recommendations

Recommendation 7.01: Member States should ensure that every restructuring and insolvency framework is grounded on an efficient liquidation process that comprises both the options to sell the debtor's business (or parts of it) as a going or to sell individual assets (piecemeal liquidation) – depending on the best return for creditors.

Recommendation 7.02: Member States should ensure that their restructuring and insolvency framework includes the option for an accelerated liquidation, in particular when the debtor or a party in interest demonstrates by clear and convincing evidence that there is a high likelihood that the value of the debtor's assets will decrease significantly within 30 days ('melting ice cube' situation).

Recommendation 7.03: Member States should make a prepack sale available in their restructuring and insolvency framework. Rules should include the involvement of an independent insolvency practitioner, appropriately regulated, to supervise the sales process and safeguard minimum transparency. In addition, creditor approval for such a sale should be mandatory and given through their representative, usually the creditors' committee.

Recommendation 7.04: Member States should, preferable in consultation with associations of practitioners, set standards and practice rules in relation to the transparency of the negotiation process before the opening of formal proceedings, the information to and degree of involvement of all creditors, the identity and background of the buyer, the professional standard of the actors involved, and, if deemed necessary, the valuation of the assets included in the sales.

Recommendation 7.05: Member States should evaluate rules governing a prepack sale, including standards and practice rules, on a regular basis to ensure the integrity of the process.

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[961] If creditors representatives get to decide on the sale, their acceptance justifies any sale, including a sale to insiders or connected parties regardless of an independent valuation of the business or the purchase price.

CHAPTER 8:
Rescue plan issues: procedure and structure; distributional issues

580. A business rescue in insolvency can be achieved in two ways: by either selling the business (usually an asset sale transferring the business as a going concern) or restructuring the business. Both options require cooperation – often within the parties of proceedings (creditors, debtor, management), but also with outsiders (investors, customers). Here, the need for cooperation in case of a sale is fairly limited in most jurisdictions because selling the business is simply a way to liquidate the debtor's assets which may only require a qualified purchaser and a confirmation by a court or even by an administrator (usually an insolvency practitioner; see Chapter 7 for more details).[962] Much more cooperation is usually required where a business must be restructured. If a plan does not only provide for the adjustment of old debt and security rights (financial restructuring), but also for an adjustment of vital credit lines, supply or employment contracts (operational restructuring), a larger number of stakeholders must be brought together. The resulting complexity is further multiplied in cases of corporate debtors if the restructuring would also affect their capital structure (e.g. in the course of a rearrangement of a complex structure with several layers of debt, equity and collateral) which usually requires the involvement of shareholders. Add an insolvent corporate group with subsidiaries and establishments in several jurisdictions to the picture and the need for efficient cooperation is at peak level. That does not mean that a business transfer is always simple. Where essential contracts, licenses or concessions must be transferred to a purchaser, stakeholders may need a more sophisticated solution than a simple auction in a formal liquidation as well. A possible share deal, spin-off or merger solution would mostly require a level of coordination amongst stakeholders that is similar to a restructuring.

581. The common way to incentivise coordination amongst stakeholders in insolvency, but also to structure their negotiations and to facilitate the success of such negotiations is to provide for a composition or plan procedure.[963] Such a plan provides for all those measures that are required to achieve the aspired outcome (e.g. a restructuring or transfer). Conventionally, such a plan or composition binds all parties to the proceedings qualifying it as a collective agreement amongst parties to insolvency proceedings. Modern workout support proceedings also allow for plans to affect only a specific group of creditors or stakeholders (see above Chapter 1 at 1.2), which even more reveals the nature of a plan being a multi-party agreement. The single reason why the rather obvious contractual nature of such plans may be disputed derives from the fact that their conclusion would usually not require the actual consent of all affected parties. Ever since the Roman law,[964] jurisdictions

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[962] In Germany, the consent of the creditors' committee or (especially in cases of an insider deal) of all creditors by a majority vote in a general meeting would be required; see Insolvency Code s 160-164. Therefore, the level of cooperation is a little higher.

[963] Terminology has changed from the term "composition" (see US Bankruptcy Act 1898, s 12) or "Zwangsvergleich" (see German Bankruptcy Code 1877, s 160) in statutes of the 19th century to "reorganization plan" (US Bankruptcy Code 1978) or "Insolvenzplan" (German Insolvency Code 1999) in more recent statutes. In earlier statutes, they were also referred to as a "concordat" (see e.g. the French Code de Commerce 1807 and the subsequent Code des Faillites et Banqueroutes 1838). The purpose of these types of agreements (or accords) has not changed, however.

[964] See C.7.71.8 for the "cession bonorum", an agreement between an insolvent debtor and all his creditors transferring all assets which was binding after a majority of creditors accepted the debtor's proposal.

have facilitated plan solution in insolvency by allowing for a plan to be binding for all parties if a stipulated majority of creditors actually voted in favour of it and a court confirmed that the plan does not discriminate against the minority. The later introduction of court-centered insolvency proceedings has resulted in a now common practice of plan proceedings which are initiated by a plan proposal, provide for court hearings including the casting of votes, and end with a decision on the confirmation of an accepted plan. Thus, for the dissenting minority a plan is a dictated agreement, but nonetheless a contract in its legal form.[965]

582. While the basic Roman law structure of plan procedure is common to all modern insolvency laws including all jurisdictions that we covered for this report, the available tools to facilitate a plan solution in such procedures differ significantly in detail.

8.1 Tools for achieving a plan

583. As recommended by international standard setting organisations,[966] all of the jurisdictions covered in our report provide for a plan option in their insolvency framework. In jurisdictions with a statutory pre-insolvency framework (see Chapter 1), a reorganisation plan is also available in these types of procedures. However, the coercive elements of a plan procedure are not available without court involvement, meaning that a pure out-of-court workout always requires the consent of all affected parties.

584. Some jurisdictions limit their plan proceedings to the sole purpose of a restructuring of the debtor, thus excluding the possibility of a liquidation plan there (e.g. Latvia, Poland, and UK). A restructuring plan may, however, also allow for a transfer of shares if the infringement of shareholder rights is permitted (see further at 8.2.2.).

585. The list of available tools for succeeding with a plan in plan proceedings commonly comprises:

- Binding dissenting parties to a majority vote;
- Immediate court review (sanctioning or confirmation hearing and decision);
- Limited effects of appeal; and
- Protection for all subsequent objections.[967]

586. In addition, common effects of commenced (pre-/insolvency) court proceedings ensure a stay, court supervision, and often an insolvency practitioner acting as a supervisor or administrator. In pre-insolvency proceedings, the appointment of a mediator is an option in some jurisdictions (see e.g. France, Spain or Belgium).

[965] For a more detailed discussion, see Stephan Madaus, *Der Insolvenzplan* (Mohr Siebeck 2011), p. 142-159 (on the US discussion) and 173-432 (on the German discussion).
[966] See World Bank Principles (2016), Principle C14.1; see also UNCITRAL Legislative Guide (2004), Recommendations 139 and 140; Principles of European Insolvency Law (2003), § 11.1.
[967] Meaning that a final and effective plan cannot be challenged on grounds that were heard or could have been heard in confirmation and appellate hearings (e.g. errors in procedure or class design etc).

8.2 Scope of plan

587. It follows from the purpose of a plan (debt restructuring) that it affects the claims of creditors primarily. A plan may also contain binding (payment) obligations for the debtor which is why the debtor is bound, too. In case of a corporate debtor, the plan may further provide for an infringement of shareholder rights in some jurisdictions (e.g. Germany, England & Wales or the US).

588. Where a plan aims at the involvement of creditors beyond their old claims or the involvement of third parties, e.g. if the plan puts a new obligation on them, their actual consent is indispensable. Lacking such consent, a plan may only contain non-binding measures like, for instance, an offer, an option, a release or an authorisation provided that such measures do either not affect the rights of creditors and the debtor, or have found their support. Thus, any third party release (e.g. from director's or shareholder's liability or surety claims against all creditors) that constitutes a disadvantage to creditors' rights requires their actual individual consent (if it is permitted by general civil law at all).[968]

8.2.1 Creditors

589. Restructuring an insolvent debtor or a debtor in financial difficulties means restructuring debt. As a consequence, all jurisdictions allow for a plan to be binding on the debtor's creditors.

Definition and types of a creditor

590. Someone is usually held to be a creditor as soon and as long as they have a claim against the debtor, meaning that the claim must exist in the moment of the commencement of proceedings. A contingent or unmatured claim commonly suffices. In addition, a future claim can satisfy this threshold in many jurisdictions if the legal basis for the claim is present at the moment of the commencement of proceedings.[969] Thus, future claims (e.g. claims for damages from product liability like asbestos claims) can be covered by a plan.

591. Traditionally, the effects of a composition in insolvency proceedings were limited to unsecured creditors. As they are to be treated equal in insolvency proceedings, they can agree to a treatment or distribution according to a composition or plan.

592. Today, many jurisdictions (Germany, Greece, France, Hungary, Italy, Spain), yet not all (Austria; Belgium[970], Latvia, Poland, Sweden, England & Wales[971]) also allow for plan provisions in insolvency proceedings that impair the security rights of secured creditors. The

[968] For the disputed issue of a non-debtor release in a non-consensual US Chapter 11 plan, see e.g. Ralph Brubaker, 'Bankruptcy Injunctions and Complex Litigation: A Critical Reappraisal of Non-debtor Releases in Chapter 11 Reorganizations', University of Illinois Law Review, (1997), p. 959.

[969] See e.g. UK Insolvency Rules 1986 r 12.3(1); for case law in Germany see BGH NZI 2012, 24 Rn. 7.

[970] In Belgium, a plan may only provide for a stay of enforcement of up to 24 months. Any other infringement of security rights requires the explicit consent of the secured creditor.

[971] The law of England and Wales provides a diverse picture. While a Scheme of Arrangement may also bind secured und preferential creditors, a CVA may not.

extended scope of a plan follows from the experience that secured credit has become a dominating practice leaving little unencumbered assets for unsecured creditors in insolvency proceedings. As a consequence, a solid restructuring often requires the involvement of creditors with their security rights.[972]

593. With regard to preferential creditors, all jurisdictions provide for the preferential treatment of post-commencement claims against the estate while at the same time denying any restructuring plan the capability to infringe these claims.[973] When considering pre-commencement claims, many jurisdictions in our report have insolvency law provisions that order the preferential treatment of specific claims, often tax or social security claims (France and Spain), employment salary or compensation claims (see chapter 5), claims from financing pre-insolvency rescue plans (France) or claims of specific types of creditors (for a full discussion on privileges, see Chapter 4). Such a privilege extents in some (France, Latvia, the Netherlands), but not all (see e.g. Spain[974]) of these jurisdictions to a protection against coercive[975] impairments in a restructuring plan.

594. After all, a (restructuring) plan in formal insolvency proceedings may often affect all classes of pre-commencement creditors. However, the scope of plans in pre-insolvency proceedings may be more limited, especially in the case of workout support proceedings (or type -1 proceedings; see chapter 1.1.).

Classification of claims

595. Traditionally, a composition only involved the claims of unsecured creditors. As these creditors were to be treated equally as a group under common insolvency law principles (par condition creditorum), statutes used to require all unsecured creditors to vote on a plan as one class. We still find such rules in plan proceedings whose scope is limited to unsecured claims.

596. Under modern restructuring laws and their broadened scope, creditors with significantly different interests and expectations regarding the recovery of the business may be affected by a plan (secured, unsecured, preferential, junior). A specific plan proposal may, therefore, be a welcome solution to one group of creditors (e.g. secured creditors) while another group would reject it (e.g. unsecured or preferential creditors). A traditional voting rule, that collects the votes of all creditors, would ignore these differences and allow the major creditors (usually secured) to determine the plan content as they could dominate the vote. In order to prevent such domination, insolvency frameworks that expand their scope

[972] See also Commission's Recommendation (2014), para. 16, arguing in favour of including secured creditors to the scope of plans.
[973] A narrow exception to this rule can be found in the German Insolvency Code, s 210a, where a plan may bind post-commencement preferential creditors only after the determination that the remaining assets are insufficient to cover claims of such creditors.
[974] Since Decree No. 9/2015 of 25 May 2015, preferential creditors, now divided into four classes (employees, public creditors, financial creditors, and other creditors), may be affected by a plan.
[975] Any preferential creditor may, of course, agree to be bound by a plan or waive the preferential status.

to all types of creditors would introduce a system of classes for claims (not creditors[976]) that reflects the differences.[977]

597. Claims with different legal status must be placed in different classes and, in addition, claims representing different economic interest can be put in different classes. With respect to the differences that allow for the classification, the equal treatment of creditors principle only applies to claims within each class itself. Beyond this background, a majority of creditors with similar legal status accepting the plan does provide for a sufficient legitimate ground to assume that all creditors of the class are treated fairly under the plan which again justifies binding the dissenting minority. The introduction of creditor classes is supported by a sound idea of equal treatment and fairness that is not only applicable to the legal environment of the United States where the practice of a classification of claims originated.[978]

598. A number of national reports show that their insolvency law does allow for a classification of claims, usually without giving a minimum or maximum number of classes. Only in France and Spain, the number and types of classes are determined by law (see e.g. French law distinguishing financial and trade creditors from bondholders and other creditors). Other jurisdictions allow for any classification that respects the differences and common interests of creditors. Here, a separate class may be required by (case) law for:

- (every[979]) security right of a secured creditor if the plan intends to impair it (e.g. Germany, Latvia, Poland, also UK Scheme of Arrangement);
- preferential claims like tax claims or unpaid salary claims of employees (e.g. also Germany for employees); and
- subordinated claims, unless the law assumes that these claims are written off (see Germany).

599. Additional particular classes are accepted for:

- employee claims (Germany, Poland);
- farmer claims (Poland); and
- small claims.

600. In practice, it is the creation of non-mandatory classes that allows a plan design which secures a majority in disputed classes or a cross-class cramdown against a dissenting class. In addition, as an equal treatment of creditors is only required in each class, a strategic classification can also enable a distribution of plan payments that considers the relevance of creditors for the continuation of the business.

[976] It is important to stress that the classification refers to the creditors' claims instead of them as an individual. This is why the same creditor can appear in one class with one of their claims and in another class with a different claim.

[977] This approach conforms to an international standard already formulated in Europe in 2003, see Principles of European Insolvency Law (2003), § 11.3 c).

[978] See US Bankruptcy Code, s 1122. For a brief overview of a larger number of jurisdictions worldwide, see INSOL International, *Claim Priorities in Restructuring Proceedings Worldwide*, 9 Dec 2016 NAV (FINAL)

[979] In principle, each security right provides for a significantly unique legal position and must, therefore, be put in a separate class. This would, however, allow every secured creditor to veto the plan unless a cross-class cramdown is available against him.

601. Classification is key to a modern plan procedure and the supervising court is asked to scrutinize a plan design for the proper classification of all claims. This usually follows a two-step-approach: First, a court needs to examine whether all classes in a plan are well and legally defined. In a second step, the court looks at the individual claims and their proper classification under the plan (if the plan specifies them individually).

602. Under such a regime, the protection of special types of creditors like secured or preferential creditors follows from the requirement to put their claims into separate classes in connection to the rules of voting and sanctioning a plan. Because a majority in each class is basically required to accept a plan, such creditors cannot be outvoted by creditors in other classes. And even if they find themselves in a minority position within their own class,[980] the "no creditor worse off" principle (or "best interest test") allows them to veto the confirmation of the plan if they would receive less individually than in an alternative liquidation of the debtor's assets (for further details see 8.5.).

603. The resulting far reaching veto power of secured and preferential creditors forces plan proponent to either leave secured or preferential claims unimpaired by the plan or involve such creditors rather early and prominently in any plan negotiation. There is, however, one weakness in the vetoing power of these creditors: a possible cross-class cramdown if provide for by law. Under such provisions, the court sanctioning the plan may ignore the veto and confirm the plan if the veto represents an abuse of right (for further details on the requirements of local insolvency law see 8.5.).

8.2.2 Shareholders

604. In case of a company debtor, it can be argued that a restructuring plan should not only affect creditors' claims but also the company's shareholders' rights. After all, both groups of stakeholders could be considered investors to the firm. In addition, the cash flow of the business can be spared if plan payments to creditors are made in company shares rather than in cash. Such a plan solution would be facilitated if a plan could provide for all aspects of a required debt to equity swap including the decision making of shareholders.

605. Beyond this background, the extension of the scope of a plan to shareholders has been discussed with intensity recently and yet we still found a rather homogenous picture in our survey. Only English law allows a pre-insolvency procedure, a scheme of arrangement, to directly bind a class of shareholders. Commonly, however, a plan in both pre-insolvency and formal insolvency proceedings is able to outline a solution that also contains changes in the capital structure of the debtor company (e.g. a debt to equity swap, a transfer of shares or the issuing of new shares). Still, even such a plan may neither include the shareholders' decision making required for the implementation of said measures under company law nor bind the shareholders to decide in the prescribed way.[981] Instead, shareholders are asked to

[980] This is not happening if each secured creditor is put in a different class. If secured or preferential creditors are joining a single class, there might be higher thresholds to outvote a dissenting minority than in classes of unsecured creditors under local law, e.g. in Spain. For more details, see 8.4.

[981] See the French Commercial Code, Article L. 626-15 and 626-16, introduced on March 12, 2014, according to which a sauvegarde plan is only able to describe the required modifications in the capital structure of a company. See also the Spanish Insolvency Code, s. 100 (2), providing that shareholders need to implement a debt to equity swap according to the applicable Spanish company law.

implement the plan by taking these measures under applicable company law. The only, yet prominent exceptions to this rather common standard come from German, Greek, English and French law.[982]

606. The widespread reluctance to include ways to coercively infringe shareholder rights in a pre-insolvency framework rests on the assumption that the company is not yet insolvent which means that even in a pure economic view shares still have a value and the company is still 'owned' by its shareholders, not creditors.[983] The directors of the company must still act in the interest of the company and its shareholders. Any infringements of shareholder rights must, therefore, comply with the shareholders' freedom to conduct a business, the freedom to set up and govern a company and to the right to property guaranteed in different degrees in national constitutions as well as in the Charter of Fundamental Rights of the European Union.

607. Once the company is insolvent, there is the economic argument that the company's assets now fully belong to their creditors (as they could collect them under enforcement law) from which would follow that they now virtually 'own' the firm. Such virtual ownership would include the power to decide on how to restructure the company's financial structure. As shareholders would not receive any value due to their subordination in a liquidation, it is held that they should not be able to veto any plan solution that allows for a reorganisation of the company debtor. Following this line of thought which is fully based on an economic valuation of stakeholder rights and originates in the restructuring laws of the United States, a Chapter 11-style model about how to treat shareholders in insolvency plan procedures has been adopted in Germany in 2012[984] including a cross-class cramdown against a dissenting shareholder class.[985] Under these rules, their veto can be ignored in the interest of creditors if (1) they receive under the plan at least as much as they would have received in an alternative liquidation (which usually is zero), and (2) if the plan provides them with a fair share of the reorganisation value which is to be determined applying the absolute priority rule (APR). Under this rule, value is to be distributed according to the pre-insolvency priority of stakeholders (senior creditors, unsecured creditors, junior creditors, shareholders). Thus, shareholders may only claim value after all creditors are paid in full.[986] In the end, shareholders may usually not veto any plan in a US-style plan procedure.

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[982] Compare Anja Droege Gagnier and Julian Dust, 'Der Debt-to-Equity Swap in französischen Insolvenzverfahren – ein Rechtsvergleich', NZI 22/2014, 942 et seq. Valeria Confortini, 'Privatautonomie and Corporate Reorganisations: Legal Treatment of Shareholders under Insolvenzordnung and Italian Insolvency Law', IILR 2016, 6, 8 distinguishes "exclusive" from "inclusive models".

[983] The related problems are the focus in recent studies, see e.g. Michael Burkert, *Der Debt-to-Equity Swao im Spannungsverhältnis von Gesellschafts- und Insolvenzrecht* (Baden-Baden: Nomos 2014); P.H.N. Quist, 'Conversie van aandelen. Enige opmerkingen bij een ongeregeld verschijnsel', Tijdschrift Ondernemingspraktijk 2014/502; Jonas Schwarz, *Der Debt-Equity-Swap als Instument der Unternehmentssanierung nach deutschen und englishem Recht* (Frankfurt: Peter Lang 2015); Carsten Schäfer, 'Zur Einbeziehung der Anteilsinhaber in den Insolvenzplan', ZIP 40/2016, p. 1911 et seq.

[984] See Insolvency Code, s 217, 225a.

[985] See US Bankruptcy Code s. 1129(b) for the original provisions in US Chapter 11. See German Insolvency Code, s. 245 (3) for the German adaption. Reasons for the strong impact of US Chapter 11 to German insolvency legislation are given by Manfred Balz, 'Market Conformity of Insolvency Proceedings: Policy Issues of the German Insolvency Law', 23 Brook. J. Int'l L. 167 1997-1998.

[986] See again US Bankruptcy Code s. 1129(b); for a history of the APR, see e.g. Douglas G. Baird, 'Present at the Creation: The SEC and the Origins of the Absolute Priority Rule', 18 Am. Bankr. Inst. L. Rev. 591 2010; Stephen J.

608. The same result can be achieved by transferring the right to vote on a plan in a restructuring from (vetoing) shareholders to a special agent.[987]

609. English law has developed a case law variation of the US/German approach including the APR. With the Scheme of Arrangement, English company law offers a procedure for solvent as well as insolvent companies to restructure that may include any modification of the capital structure and, in that case, bind shareholders. Such a scheme requires shareholder participation in the process: shareholders form a separate class and get to vote. Though such a scheme may be proposed for solvent and insolvent companies alike, shareholders can only be forced to accept a scheme (cross-class cramdown) if their class has 'no real economic interest in the company's undertaking.'[988] In such a case (only), their vote against the scheme should be disregarded. Thus again, the valuation of a distressed company is key as it shows whether a class of shareholders (or junior creditors) is still 'in the money' (receive value in a liquidation). The critical value of the business would is, in contrast to German (but not US) law, the existing (present) going concern value of the company's business, which, after all, is the value the proposed scheme is intended to both preserve and apportion.[989] Beyond this background, solvent schemes are usually negotiated in close consultation with the primary shareholders and backed by a positive vote of their class. However, if the valuation shows that the company is actually balance sheet insolvent, shareholders (and junior creditors) have lost their 'real economic interest in the company' and the court may sanction the scheme against their dissenting class. The same is possible if the company is also formally insolvent and subject to an administration. Here, a company voluntary arrangement (CVA) may include a modification of the firm's capital structure which entitles shareholders to vote in a separate shareholder meeting.[990] If a CVA finds the support of creditors but is rejected by shareholders, English law assumes that shareholders have no real economic interest in the insolvent company and allows a court to sanction the CVA against the objection of shareholders[991] unless the arrangement 'unfairly prejudices the interests'[992] of a member of the company, or that there has been some 'material irregularity'[993] at or in relation to the shareholder meeting.[994] There is no case law indicating that any infringement of a shareholder in an insolvent company constitutes an unfair treatment. Overall, English law gives shareholders of insolvent companies a role in the process by allowing them to vote but eventually offers no protection for dissenting shareholders. As such, it differs little from the US/German approach.

610. Whether such a strict treatment with no substantial protection against any plan infringement is in line with the Member States' constitutional protections of the right to

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Lubben, 'The Overstated Absolute Priority Rule', 21 Fordham J. Corp. & Fin. L. 581 (2016); see also the original decision in e *Case v. Los Angeles Lumber Products Co.*, 308 U.S. 106, 115-119 (1939).

[987] This can be done by court order in Greek recovery and reorganization proceedings according to Article 101 and 120α Greek Bankruptcy Code.

[988] See *In re Tea Corporation Ltd* [1904] 1 Ch 12; *In re Oceanic Steam Navigation Company Ltd* [1939] Ch 41.

[989] See M. Crystal and R.J. Mokal, 'The Valuation of Distressed Companies: A Conceptual Framework', ICR 2006, 123, 126. For an example of a valuation dispute, see *Re Bluebrook Ltd* [2009] EWHC 2114 (Ch).

[990] See Insolvency Act 1986, s 3 and s 4A (3).

[991] See Insolvency Act 1986, s 4A (2)-(6).

[992] See *Prudential Assurance v PRG* [2007] EWHC 1002 (Ch).

[993] For a general explanation of this standard, see e.g. *Re Gatnom* [2010] EWHC 3353 (Ch).

[994] See Insolvency Act 1986, s 6 (1).

property of shareholders, but also with their right to establish and run a company (protected e.g. by the German Constitution[995]), has been subject to a debate.[996] It let the French legislator to a rather restricted rule that found approval by the French Constitutional Council.[997] Since 2015, the court in a judicial reorganisation procedure (upon the insolvency practitioner's request) may appoint a judicial representative in order to convene a shareholder meeting or to transfer shares to a third party in order to implement a plan provision concerning the capital structure of the debtor company, if

- the debtor (or the corporate group the debtor belongs to) has more than 150 employees;
- the loss of the company, as a debtor, would cause a serious disruption to the economy and to the local employment area; and
- the restructuring of the debtor's capital structure proposed by the plan is the only solution to avoid such disruption and to allow the continuation of its activity, even after examining the possibilities of totally or partially selling the debtor.[998]

611. Affected shareholders would be compensated by the beneficiaries of the transfer if the shares had a value which should be determined by an independent expert appointed by the court. It is obvious that the French approach differs significantly from the US and German model by limiting coercive measures against shareholders to rather exceptional circumstances.

8.2.3 Content of plan

612. From the scope of a plan also follows that a plan may only contain measures that affect participating parties. Commonly, a plan may provide for any treatment of creditors' claims (e.g. a suspension of payment or a write-off, but also a debt to equity swap) and for the way to handle the debtor's estate (business) in order to achieve it. Many jurisdictions also allow for modifications of their security rights (see above 8.2.1.). In Germany and England, a plan may also provide for any change of the rights of shareholders legally possible under German or English Company law.[999] Any impairment of third party rights would require their actual consent in all jurisdictions. In Germany, a (liquidation) plan may, in principle, also set new rules for certain aspects of the remaining insolvency proceedings; still, a number of procedural insolvency rules and guarantees are still not accessible for plan proponents ('plan proof' rules).[1000]

613. In addition to these limitations, local insolvency law may provide for additional restraints. Commonly, the plan must treat creditors with similar rights equal which means

[995] See German Fundamental Law (Grundgesetz), Article 9 (1).
[996] For German law, see e.g. Stephan Madaus, *Keine Reorganisation ohne die Gesellschafter*, ZGR 2011, 749.
[997] Constitutional Council, Decision No. 2015-715 DC, 5 August 2015, §145.
[998] See Commercial Code, Article L. 631-19-2, introduced on August 6, 2015. For details see C. Ottaway and F. Seroka, 'The Impact of the "Macron" Law on French Insolvency Procedure', 13 Int. Corp. Res. 2006, p. 48.
[999] See German Insolvency Code, s. 225a (3). The construction of this new provision is still being discussed, see Horst Eidenmüller, 'Der Insolvenzplan als gesellschaftsrechtliches Universalwerkzeug', NJW 2014, 17, but also Stephan Madaus, 'Möglichkeiten und Grenzen von Insolvenzplanregelungen', ZIP 2016, p. 1141, 1142.
[1000] See BGH ZIP 2009, 480, 482, Rn. 25, confirmed in BGH ZIP 2010, 1039, 1040; see also Stephan Madaus, ibid, at p. 1144.

that all creditors in a class must receive the same treatment under the plan.[1001] In Austria, a plan must provide unsecured creditors with at least 20% or 30% of their claims; Swedish law requires a plan to pay 25% equally to all unsecured creditors within one year.[1002] In other jurisdictions (e.g. Germany), a plan must offer any parties at least as much as they were to receive in an alternative liquidation of the estate ('no creditor worse off' or 'best interest' test) unless every party receiving less actually accepts the plan (see 8.4. for confirmation standards).

614. Insolvency law often also contains detailed requirements on the structure of the plan, especially about the way to deliver all the information required to vote, in order to ensure an informed decision of all parties.[1003]

615. Finally, the deviation from statutory rules provided for in a plan provision may not be allowed under other compulsory local law. Such 'plan proof' rules can be found where a statute provides for mandatory minimum standards or guarantees like procedural rights (fair trial, right to be heard) or social security.

616. Especially labour law rules are often held to be mandatory which would also include that they are plan proof. As a consequence, a restructuring plan cannot provide, for instance, that a workers' council can be excluded from its 'right to advice' under labour law, although they will be informed. However, a plan may not be required in order to escape hindering labour law provision in a restructuring as a number of insolvency law provisions may allow for a deviation from otherwise mandatory labour law (see chapter 5) anyway. For instance, collective bargaining agreements which were concluded only between the debtor and their workforce can be terminated by the administrator under insolvency law.[1004] If, however, collective bargaining agreements are applicable which govern the working conditions for a whole industry or trade sector (e.g. with respect to salary, social security, vacation or working conditions),[1005] neither the local administrator nor the parties of a restructuring plan usually have the right to renegotiate these terms. The modification of the terms of a collective bargaining agreement (usually including lower wages, more working hours, less vacation, less pension claims) would require the conclusion of a new agreement under labour law (negotiated and concluded by the workers' representatives or unions and the debtor) provided that applicable industry-wide collective bargaining agreements allow for such deviations from their minimum standards.

[1001] See e.g. German Insolvency Code, s. 226 (1). In jurisdictions with no classification of claims, the 'par conditio creditorum' principle usually requires the equal treatment of all unsecured creditors, see e.g. Austria. Only Belgian law seems to follow a less strict line here, see Belgian Insolvency Act, Article 49 and 49/1, as well as the practical difficulties reported in the Belgian National Report.

[1002] A similar provision in Greek law (Bankruptcy Code, Article 100) that required a reorganisation plan to pay at least 20% within one year, was abolished in 2015.

[1003] These requirements may include a description of the business development and plan strategy as well as detailed information about the estate and the creditors. See e.g. Belgian Insolvency Act, Articles 47-52; German Insolvency Code, s. 219-230. They reflect international standards, see UNCITRAL Legislative Guide (2004), Recommendation 144; see also the Commission's Recommendation (2014), para. 15.

[1004] See e.g. German Insolvency Code, s. 120.

[1005] Such type of agreements are common e.g. in Germany.

8.3 Proposing and negotiating a plan

8.3.1 The right to present a plan

617. The right to propose a plan is commonly assigned to the debtor. Where a restructuring plan is the sole purpose of either specific (pre-insolvency or formal) reorganisation proceedings or a plan option in consolidated insolvency proceedings, the debtor usually owns this right exclusively[1006] or for an exclusive period of time[1007]. Only the new French law allows for a competing plan of a member of the creditors' committee in a Procédure de Sauvegarde and empowers the court to decide which plan to confirm.[1008] The Swedish law is peculiar in this respect as its reorganisation procedure is based on the assumption of a cooperation between the debtor and the insolvency practitioner which results in the exclusive right of the insolvency practitioner to propose a rescue plan.[1009]

618. In contrast, where proposing a plan is an option in consolidated insolvency proceedings to not only avoid but also improve a liquidation, the right to propose a plan may not always be reserved for the debtor. The idea of initiating a competition for the best possible allocation of the debtor's assets results in providing for a proposing right for the insolvency practitioner[1010] (Germany;[1011] Sweden) and all creditors (Spain;[1012] Italy;[1013] Greece;[1014] see also US Bankruptcy Code s 1121).

619. In jurisdictions which allow for more than one plan proposal, the issue of competing plans arises. It is obvious that eventually only one plan can actually govern the future of the debtor's business. The rules about how to determine the prevailing plan differ significantly if such rules exist at all.[1015] French law only mandates the equal procedural treatment of both plans. In contrast, Spanish law[1016] provides for a preferential treatment of the debtor's plan that will be deliberated and voted first. Only if the debtor's plan is not accepted or confirmed, the competing creditor plan becomes relevant. Under US law, all competing plans are put to vote equally and, if more than one plan was accepted, the court may only

[1006] See Austria, Belgium, Spain, Hungary, Latvia, the Netherlands, Poland, England & Wales.

[1007] See the Greek Bankruptcy Reorganisation Procedure where the exclusivity period ends after three month to be extended for an additional month. See also US Bankruptcy Code s 1121 (minimum of 180 days).

[1008] See Commercial Code, Article L. 626-30-2, introduced on March 12, 2014. See also Ernst Degenhardt, Die Reform des französischen Insolvenzrechts vom 12.3.2014', NZI 2014, 433, 436.

[1009] See also Marie Tuula-Karlsson, 'The Swedish Business Reorganisation Act and SAAB', Scandinavian Studies in Law 2015, p. 329, 336-337.

[1010] See also the Principles of European Insolvency Law (2003), § 11.2: 'A reorganisation plan can be presented by the debtor or the administrator'.

[1011] See Insolvency Code, s 218.

[1012] See Insolvency Code, Article 113 (1) providing for a right to file a rescue plan for creditors representing at least 20% of total liabilities.

[1013] The Law Decree No. 83/2015 of 27 June 2015 introduced a right for creditors that represent at least 10% of the creditors to file a competing plan if the plan presented by the debtor does not ensure payment of at least 40% of the unsecured creditors.

[1014] According to the Greek Bankruptcy Code, creditors representing 60% of all claims (including 40% of the secured creditors) against the debtor have the right to file for a recovery agreement or a reorganization plan.

[1015] German law, for instance, does allow for competing plans but does not describe how to handle the resulting competition.

[1016] See Insolvency Code, Article 121 (2).

confirm one of them. In making the decision, the court 'shall consider the preferences of creditors and equity security holders'.[1017]

8.3.2 Negotiations about a proposed plan

620. The plan proponent is responsible for organising sufficient creditor support for his proposal. Negotiations with key stakeholders would usually start before a plan is formally filed which results in an out-of-court element of plan negotiations that involves only critical stakeholders, usually major lenders, key suppliers and employee representatives[1018]. Such preparatory negotiations are often confidential. If they are successful in establishing sufficient support for a specific plan, a formal plan proposal is filed.

621. As a plan commonly requires the acceptance of affected parties by voting, an acceptance or voting hearing is commonly summoned by court in formal insolvency proceedings but also in collective pre-insolvency proceedings (see e.g. a Scheme of Arrangement or a Procédure de Sauvegarde). Here, all parties entitled to vote (see 8.4. for further detail) must be noticed[1019] and invited individually about the meeting, usually including a copy of the proposed plan. In addition to individual notice, the voting hearing is usually publically announced either through newspapers, legal gazettes or online. Here, the plan proposal is either made available directly (online[1020]), usually in summary (Austria, Germany[1021]), or the publication refers to the court where the plan is available in the clerk's office (Belgium, Germany). There is no formal requirement of a U.S.-type 'disclosure statement' to be produced with the plan.[1022]

622. Often, the court hearing on the plan proposal offers the only opportunity to formally object to plan provisions and suggest their alteration before the plan is put to vote[1023] (see e.g. Germany[1024]). In practice, however, the proposed plan solution has often already been negotiated in advance with key stakeholders and secured the required support which means that there is little left to negotiate for minor stakeholders in the meeting. In addition, these stakeholders only have a very limited period to actually examine the plan as they are only informed with the invitation to vote.[1025] As a result, minor parties may only have limited expectations to actually reopen substantial negotiations and to significantly modify a proposed plan.

[1017] US Bankruptcy Code s 1129(c).

[1018] For further details on employee rights in restructurings, see Chapter 5.

[1019] Only in Hungary, the right to notice is extended to creditors with no right to vote on the reorganisation plan.

[1020] Member States have developed online registers or databases for insolvency cases – see e.g. the Austrian insolvency database.

[1021] Only mandatory for publicly traded companies – see Insolvency Code, s 235(3)4.

[1022] See UNCITRAL Legislative Guide (2004), Recommendations 142, 143.

[1023] This level of involvement is also stated in the Commission's Recommendation (2014), para. 24.

[1024] See Insolvency Code, s 235, 240.

[1025] See e.g. Belgian law (Article 45 BCA) that guarantees only a deposition of the plan at the clerk's office for a minimum of 20 days before the hearing. In an English CVA, the law only provides for a 14 days' notice – see Insolvency Rules 1986, Rule 1.9. Hungarian law only provides for a 5 days' notice, see Insolvency Code, s 17. § (3).

623. In non-collective pre-insolvency proceedings, the plan only affects a specific group of stakeholders and, thus, only requires negotiations and a vote amongst this group. As a consequence, these participants are all notified and involved in negotiations before a vote. If a plan confirmation is required, the commencement of the respective court proceedings may be published (see also para. 1.1.2.d)).

8.4 Voting rights and procedure

624. In all jurisdictions (except for SME cases in France), a restructuring plan may only affect the parties' right after it has been accepted by a stipulated majority of them. The actual acceptance of creditors is essential. In order to determine the actual opinion of creditors about a proposed plan, they usually get to vote on it. The allocation of voting rights and the exclusion of particular stakeholder groups from voting shapes the whole plan process.

8.4.1 Voting rights and voting rights disputes

625. As a basic rule, all parties directly affected (bound) by a plan get to vote on it. If a creditor's claim is left untouched by the plan, it generates no voting right.[1026] Depending on the legal scope of a plan in a jurisdiction (see above at 8.2.), the right to vote may principally be limited to unsecured creditors (see Austria), some creditor classes (see e.g. Belgium), or even extended to all classes of creditors and shareholders if the plan actually impairs their legal position (see e.g. Germany, England & Wales, also US Chapter 11[1027]).

626. The individual right to vote depends on the status of a person of being a creditor or a shareholder. Whether a person has a claim against the debtor up to the specified amount, or whether a person hold equity in the debtor company are facts that, in case of a dispute, cannot be finally stated in the short timeframe of plan proceedings. Most jurisdictions have, therefore, developed rules that allow the court to preliminarily determine disputed voting rights. Commonly, only creditors actively participating in the proceedings earn a right to vote. Creditors have to file their claims (either within a specific period or until the day of the vote). Then, undisputed non-contingent claims provide for a right to vote accordingly.

627. In case of a disputed or contingent claim, it is the supervising court[1028] that usually determines the right to vote following a prima facie test of the claim (see Austria, Belgium, Germany[1029], France, Italy, Latvia, Poland). Such voting rights dispute may delay a vote on the plan in some jurisdictions (like e.g. in Germany) which can be avoided where the law allows any filing creditor to vote while postponing any court decision on voting rights to the

[1026] This principle reflects an international standard, see UNCITRAL Legislative Guide (2004), Recommendation 147.

[1027] See US Bankruptcy Code s. 1126.

[1028] In the Netherlands, the administrator determines the right to vote. In English CVA proceedings, the chairman decides subject to appeal to the court, see Insolvency Rules, Rule 1.17A(3).

[1029] Under German law, the court will only decide about voting rights if the creditor cannot reach an agreement about it with the administrator during the creditors' meeting; see Insolvency Code, s. 237, 77 (2).

confirmation hearing. Here, the dispute would only be reconsidered if the disputed votes are essential for plan acceptance (see e.g. Austria, England & Wales, Greece, Poland).[1030]

628. In contrast, pre-insolvency frameworks, especially those who allow for out-of-court voting, (and some formal insolvency procedures, e.g. in Belgium) entrust the debtor to present a list of creditors and shareholders who need to be contacted for voting and who may contest the accuracy of the voting process in court (see e.g. England & Wales).

629. In jurisdictions with several classes of claims, a claim only provides for a voting right within the class it belongs to. Thus, the vote of a secured creditor may not only count with the value of the security right in the class of secured credit but also with the value of a (probable) deficiency claim in the class of unsecured claims[1031].

630. A particularly different voting scheme was reported for France. In French reorganisation proceedings (Procédure de Sauvegarde as well as Redressement Judiciaire), having a creditors' vote on a plan is only mandatory for larger cases.[1032] Even here, only creditors that comprise a 'committee of financial creditors', a 'committee of the main trade creditors' or, if existing, a 'committee of bondholders' get to vote on a rescue plan. Other creditors are not entitled to vote (and not bound). As such a mandatory 'one size fits all' classification does not reflect differences in ranking or legal status of affected claims, it has become the task of assigning different voting weights to reflect such differences since a law reform in 2014. Now it is possible to give subordinated bonds less weight than senior bonds, for instance. However, the transfer of ranking issues to the assignment of voting rights may cause disputes amongst parties that could potentially delay French proceedings significantly.[1033]

8.4.2 What modes of voting are permissible?

631. Votes in formal insolvency proceedings are commonly casted in a creditors' meeting summoned and directed by the court. Every stakeholder entitled to vote is required to be either present or represented by proxy. Distance voting modes (e.g. by letter, email or online) are not yet allowed under many insolvency laws covered by our report,[1034] but obviously are already permissible in French and Polish procedures;[1035] some jurisdictions allow for casting a written vote[1036] instead of having a meeting which can be done by either mailing the ballots or proxies to creditors and asking them to return their votes within a specific timeframe,[1037] or a circulating list of creditors that each creditor has to sign[1038].

[1030] Jurisdictions like Hungary where disputed claims give no right to vote until they are proven in a civil law litigation invite debtors, but also insolvency practitioners, to wilfully dispute a claim if there creditors is expected to oppose the plan. Such rules should be amended.

[1031] See e.g. German Insolvency Code, s. 237 (1).

[1032] See Commercial Code. Article L626-29.

[1033] See Ernst Degenhardt, 'Die Reform des französischen Insolvenzrechts vom 12.3.2014', NZI 2014, 433, 436.

[1034] There are, for instance, not permitted in Austria, Belgium, Hungary, the Netherlands, and Sweden.

[1035] This reflects the standard set by the Commission's Recommendation (2014), para. 19.

[1036] See Germany, Italy, Latvia or Spain.

[1037] See e.g. the practice in English schemes of arrangements reported by our National Correspondents.

[1038] This practice was reported by our Greek National Correspondents to be common to set up Greek recovery agreements.

8.4.3 Do trading claims ban new creditors from voting?

632. The commencement of insolvency proceedings does not bar creditors from selling their claims to third parties and there is a vital market for distressed debt, especially in bigger cases. When selling his claim, a creditor sells all rights attached to the claim which includes the voting rights connected to it. A constantly changing demographic of creditors has become a significant obstacle in negotiating restructuring plans because new creditors often buy distressed debt following a particular strategy. Some may wish to take over the debtor company by way of a debt to equity swap in a restructuring plan. Others may expect a short time profit from a distribution that exceeds the price they paid significantly and try to veto a proposed plan in order to achieve a quick liquidation or a high distribution under the plan.

633. Although anecdotal evidence suggests that claims trading is quite common in bigger cases, yet only some jurisdictions in the Report have already developed specific rules to address the negative side of distressed debt trading, and they did so in quite a diverse manner. Austrian and Polish law reportedly do not ban claims trading but preclude any post-commencement purchaser of a claim from voting on a plan. Spanish law limits such a ban to a post-commencement purchaser that has a special relation to the debtor (insider). Italian law may exclude creditors from voting that acquired the claim within the last year before filing.[1039] Latvian law bars new creditors from voting if they acquired the claim within two years before the vote. In many jurisdictions, however, the acquirer of a claim is assuming all rights connected to the claim including voting rights (see e.g. Belgium, Germany,[1040] France, Hungary, the Netherlands, or England & Wales). Only in out-of-court workouts, a standstill agreement usually includes a prohibition to sell claims unless the acquirer agrees to the terms of the standstill.[1041]

8.5 Confirmation and cramdown

634. A restructuring plan commonly requires the confirmation or sanctioning of a court before entering into force.[1042] Only a company voluntary arrangement under English law can be implemented without a confirmation if no creditor applies to court. When confirming a plan, the court verifies that

- the plan has been accepted according to the applicable rules;
- the content of the plan meets all legal requirements; and
- the plan is fair and equitable against dissenting creditors.

[1039] This exclusion applies only to credit purchased from certain creditors, such as relatives or members of the same corporate group.

[1040] German case law does, however, prohibit a purchase offer to some but not all creditors that pays more than the proposed plan for a claim. Such unequal treatment of creditors invalidates the plan but also the purchase agreement. See BGH NZI 2005, p. 325.

[1041] The practice was reported for an English scheme of arrangement by our National Correspondents.

[1042] A confirmation requirement, in particular for non-consensual plans, reflects international standards, see UNCITRAL Legislative Guide (2004) Recommendations 151, 152. See also Commission's Recommendation (2014), para. 6 (d), 18, 21, and Recital 19.

8.5.1. Plan acceptance

635. Historically, a composition was a product of the parties' autonomy. Creditors (with a stipulated majority vote) and the debtor agreed to accept a specific performance of the debtor on their outstanding debt in order to complete insolvency proceedings.[1043] From this background, it is no surprise that most modern insolvency laws require a plan to be supported by a stipulated majority of creditors if it is to be confirmed by a court.[1044] Commonly, creditor support is demonstrated by a voting process (see 8.4.). Only French law allows for the confirmation of a plan without any demonstration of creditor support if the debtor's business is too small to meet certain thresholds.[1045]

636. Commonly, the debtor is also required to support a plan, either by proposing the plan (for their often exclusive right to propose a plan, see chapter 8.1.3.) or by accepting a plan presented by a creditor or by the administrator (e.g. Germany).

637. Where creditors (and shareholders) get to vote, a plan does not need to find the support of every vote. Instead, the acceptance of a stipulated majority in a stipulated voting entity commonly suffices. The deviation from a full consensus has a long tradition and results from the fact that it is close to impossible to negotiate an agreement that everyone agrees with in a larger group of people with different aims and interests. At the same time, the actual support of a majority of stakeholders with similar legal and economic interests suggests that the proposed solution does not discriminate unfairly against the dissenting minority. Immediate court review provides for additional protection. Following this line of thought, the jurisdictions in our report require the actual support of a majority of voting creditors – often provided that certain quorum is given – with the threshold set between a simple majority (>50%), 60% or 66% up to 75% in value of voting claims (see table 9). Where shareholders of the debtor company are entitled to vote (like Germany or England & Wales; see 8.2.2.), the same threshold applies for their class.

Member State	Procedure	Voting entity	Quorum of total votes	Required majority
AT	URG Proceedings[1046]	Every affected stakeholder	100%	100%
	Reorganisation Proceedings	Meeting of unsecured creditors	1 vote	>50% in value of voting creditors'

[1043] Roman law already allowed for a composition in case of an insolvent inheritance; see Dig. 2.14.7-10. Justinian's Codex allowed for the 'cessio bonorum'; see C. 7.71.1. Compositions got introduced in the medieval bankruptcy laws of many mercantile cities in Italy, Holland, Germany and Spain, see Josef Kohler, *Lehrbuch des Konkursrechts* (1891), p. 446 et seq. Such compositions could only prompt a discharge since such a rule was introduced in England in 1705, see Charles Jordan Tabb, 'The History of Bankruptcy Laws in the United States', Bankr. Inst. L. Rev. 1995, p. 10.

[1044] The traditional voting requirement also represents international standards, see World Bank Principles (2016) C14.5; UNCITRAL Legislative Guide (2004) Recommendation 150; Principles of European Insolvency Law (2003) § 11.3. It is also part of the Commission's Recommendation (2014), para.18.

[1045] See Commercial Code. Article L626-29. See also Alexandra Kastrinou, 'Comparative Analysis of the Informal Pre-Insolvency Procedures of the UK and France', 25 Int. Insol. Rev. 2016, p. 99, 108.

[1046] Reorganisation proceedings under the Business Reorganisation Act (Unternehmensreorganisationsgesetz).

				claims
BE	Judicial Reorganisation	Meeting of creditors	1 vote	>50% in value of voting creditors' claims, and >50% in value of all claims
DE	Insolvency Plan Proceedings	Classes of creditors	1 vote	(in each class) >50% in value of voting creditors' claims, and in number of voting creditors
		Class of shareholders	None[1047]	>50% in value of voting shareholders' shares
	Bond term restructuring	Bondholder meeting	50% of all bonds[1048]	75-100%[1049] in value of voting bondholders' bonds
EL	Recovery Procedure	Creditors, as listed on creditor list provided by the company	None	>60% in value of voting creditors' claims, and >40% in value of secured claims of voting creditors
	Bankruptcy Reorganisation Procedure	Meeting of creditors	None	>60% in value of voting creditors' claims, and >40% in value of secured claims of voting creditors[1050]
ES	Judicial Homolgation	Financial creditors	>50%	>50% in value of all financial debt[1051]
	Bankruptcy Reorganisation Procedure (convenio)	Meeting of creditors	>50% of all ordinary and preferential claims[1052]	a)[1053] >65% in value of voting creditors' ordinary claims, and >75% in value of voting creditors'

[1047] Insolvency Code, s. 246a provides that in cases where no shareholders actually votes the class is deemed to accept the plan.
[1048] The German Bond Act, s 15, allows for a second meeting if the first one is postponed because it lacked a quorum. A quorum of the second meeting is given when at least 25% of all bonds are represented.
[1049] The applicable majority depends on the bond terms, see German Bond Act, s 5.
[1050] Non-participating creditors are deemed to vote in favour of the plan, see Greek Bankruptcy Code, s 116.
[1051] See Jose Maria Mesa Molina and Alberto Alvarez Marin, 'Court Approval of Refinancing Agreements in Spain', eurofenix Spring 2015, p. 35.
[1052] See Spanish Bankruptcy Code, s 116 (4), see also Laura Ruiz, 'Spanish Insolvency Act: The Legislation Created by the Crisis', Insolvency and Restructuring International 2015/25, p. 26.
[1053] Applicable if the plan provides for a moratorium or a swap into a new loan lasting 5-10 years or a debt cancellation above 50%.

				preferred claims in each class[1054] b)[1055] >50% in value of voting creditors' ordinary claims, and >60% in value of voting creditors' preferred claims in each class c)[1056] value of ordinary claims of creditors voting in favour of the plan exceeds the value of those voting against it
FR	Procédure de Sauvegarde, Redressement Judiciaire	Committee of main trade creditors, of financial creditors and of bondholders	None[1057]	In each committee >66% in value of voting creditors' claims
HU	Reorganisation Procedure	Meeting of creditors	None	>50% in value of voting creditors' claims in both the class of secured and unsecured claims
	Liquidation Procedure	Meeting of creditors	None	(in each class) >50% in value of voting creditors' claims, and >66% in value of all registered claims
IT	Accordi di ristrutturazione	Affected creditors	>60% in value of affected claims	>60% in value of affected claims
	Concordato and (c. preventivo)	Meeting of all creditors, or Classes of creditors	-- -- --	>50% in value of all claims eligible to vote[1058] (in all classes)
LV	(Out-of-court or ordinary) Legal Protection	Classes of unsecured and secured creditors	--	>50% in value of all unsecured claims >66% in value of all

[1054] Preferential creditors are divided into four classes: employees, public creditors, financial creditors, and other creditors.
[1055] Applicable if the plan provides for a moratorium or a swap into a new loan lasting up to 5 years or a debt cancellation below 50%.
[1056] Applicable if the plan provides for the full payment of all ordinary claims with three years, or a debt cancellation below 20% while immediately paying the remaining 80% as they are due. Preferential creditors are not affected.
[1057] Commercial Code, Article L. 626-30-2 requires no quorum.
[1058] Non-participating creditors are deemed to vote in favour of the plan.

	Procedure			secured claims
NL	Composition in Suspension of Payments, and Bankruptcy Procedure	Meeting of creditors	--	>50% in value of voting creditors' claims, or >75% in number of all voting creditors[1059]
PL	Arrangement Approval Proceedings	Affected creditors	>66% in value of affected claims	>66% in value of affected claims[1060]
	Arrangement Proceedings and Bankruptcy Proceedings	Meeting of all creditors, or Classes of creditors	--	>66% in value of voting creditors' claims (in each class) [1061]
SE	Company Reorganisation (composition)	Meeting of unsecured creditors	--	>60%[1062] or >75%[1063] in number of creditors and in value of all claims
UK	Scheme of Arrangement	Meetings of creditors and of shareholders	Represen-tative number [1064]	(in each class) >75% in value of voting creditors' claims
	CVA	Meetings of creditors and of shareholders	1 vote	>75% in value of voting creditors' claims, and >50% in value of voting shareholders' shares

Table 9 – Pre-insolvency proceedings (type, court involvement, available tools)

8.5.2 Content, feasibility and purpose of a plan

638. The legal content of a plan has been discussed above (see 8.2.). The court needs to check all legal, substantive and procedural requirements including, for instance, a proper classification and voting, equal treatment of creditors, mandatory minimum plan distributions, mandatory disclosure, or limits in scope.

639. Some also ask the court to review
- the feasibility of the accepted plan,[1065] or

[1059] In this case the court would assess whether the dissenting creditors – taking all circumstances into account, in particular what they had received in a liquidation – had good reason to reject the plan, see the Dutch Bankruptcy Act, s 146 for bankruptcy, and s 268a for suspension of payments.
[1060] Non-participating creditors are deemed to vote in favour of the plan.
[1061] Non-participating creditors are deemed to vote in favour of the plan.
[1062] If the composition offers to pay 50% or more of all unsecured debts.
[1063] If the composition offers to pay less than 50% of all unsecured debts.
[1064] See *Re T&N Ltd (No. 3)* [2006] EWHC 1446 (Ch).
[1065] See Austria, France, Greece, Italy (only in the case that a qualified creditor or percentage of creditors contest the concordato preventivo proposal), the Netherlands or Poland.

- in the case of an individual, the eligibility of the debtor (their full cooperation, no criminal record etc.),[1066] or
- whether the plan was presented in good faith (e.g. not only to delay proceedings, no fraud, no insider deals),[1067] or
- whether its content is detrimental to the common interest of creditors[1068] or public policy.[1069]

640. With respect to timing, some jurisdictions (like Germany) allow the court to already review the plan content ahead of the voting in order to save the costs of a meeting if the plan could not be confirmed. Other jurisdictions (e.g. Austria) create a potential delay by conditioning any plan confirmation to the prior payment or collateralisation of administrative expenses or preferential claims (e.g. the administrators' remuneration).

8.5.3 Fairness and cramdown

641. Before confirming an accepted plan, the court is not only asked to review the plan content and the voting process. In order to bind dissenting creditors (and shareholders), the judge must order them to accept the plan. While for the majority voting to accept a plan the binding power of the plan can be justified with their actual will, any dissenting creditor is only bound if a court orders him to do so. In a doctrinal view, the court's confirmation order states and enforces an obligation to conclude a contract under applicable (pre-)insolvency law.[1070] In order to do so, judges must not only find that the plan is legal and all votes were cast following legally, they must also ensure that in the absence of a plan that everyone actually agreed on, no dissenting creditor (or shareholder) is being discriminated against by the plan. It is a matter of protecting minority rights and usually a discussion of fairness or a "fair and equitable" treatment follows. Here, two levels of protections are to be distinguished.

Fair treatment of every single dissenting creditor (or shareholder)

642. Every single dissenting creditor or shareholder may commonly object to a plan arguing that the plan would treat their claims or rights in an unfair way. As a general concept of fairness or a fair treatment is very difficult to define,[1071] all jurisdictions have developed specific tests that a plan must pass, usually a combination of content- and debtor-related threshold (see above 8.5.2.) and a fairness test.

643. The most common fairness test of the plan treatment of each individual creditor or shareholder follows from the idea that there is no rational to reject a plan that pays at least

[1066] See Austria or Poland.
[1067] See Austria, Greece, Hungary, the Netherlands, or Sweden; see also US Bankruptcy Code s 1129(a)(3).
[1068] See Austria, France, Greece, Hungary, Poland, or Sweden.
[1069] See Belgium. Under US Bankruptcy Code s 1129(d), a plan cannot be confirmed if the only purpose of the plan is tax avoidance.
[1070] See Stephan Madaus, *Der Insolvenzplan* (Tübingen 2011) 261 et seq., also p. 327 et seq.
[1071] See Sarah Paterson, 'Debt Restructuring and Notions of Fairness', Modern Law Review. 2017. See also *Re TDG plc* [2009] 1 BCLC 445; *Re Telewest Communications Ltd (No. 2)* [2004] EWHC 1466 stating that a scheme is fair if,an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve' it.

the value that a dissenting creditor (or shareholder) would have received in the scenario without the plan, usually a liquidation. This idea can be traced back to the U.S. Bankruptcy Act of 1874 (s 5103 A) where it was held that confirming such a plan is for "the best interest of all concerned".[1072] In Europe, the test is usually referred to as the "no creditor worse off principle".[1073] It is common in many of the jurisdictions of our report (see Germany, Greece, Spain, Italy, Poland, England & Wales) and sometime applied ex officio (see England & Wales, US; also Greece), sometimes only upon the request of a dissenting creditor (see Germany, Italy). In the latter, a creditor may only to object if he had actually voted to reject the plan; other creditors, including non-participating creditors, are not heard.[1074]

Fair treatment of dissenting classes (cross class cramdown)

644. Jurisdictions that allow for the classification of creditors (and shareholders) commonly require all classes to accept a plan under their voting rules. Thus, a plan that did not find the support of a majority in one class, cannot be confirmed in principle. The resulting veto power of this unanimity rule may, however, lead to undesired consequences because it allows senior or secured creditors to veto a plan even if the plan pays them as much as they could expect in a liquidation. It also allows classes like junior creditors or shareholder classes to veto a plan that gives them nothing even though they could not expect to receive more in a liquidation.

645. In response to these disadvantages, jurisdictions that introduced classes of creditors allow the court to confirm a plan ignoring the dissent of a class if the plan (1) actually finds sufficient creditor support (either by other classes or creditors in total), and (2) treats the creditors (or shareholders) in the dissenting class in a fair and equitable way.

646. The 'actual support' criteria is handled differently across these jurisdictions: in Germany a majority of classes in number must actually vote to accept the plan[1075] while in Poland a veto of a dissenting class can be ignored if the plan was supported by the votes of creditors representing at least two-thirds of all voting creditors' claims. The U.S. model where the actual support of a single class suffices[1076] has not yet been adopted in Europe.

647. The 'fair treatment' criteria is again substantiated by specific tests. Some jurisdictions, for instance Poland, again apply the 'no creditor worse off' principle. Others, like Germany[1077] or Italy fully adopted the U.S. model by complementing this test with a second test: the 'absolute priority rule' (APR).[1078] This test was design by the U.S. Supreme Court[1079]

[1072] See also Jonathan Hicks, 'Foxes Guarding the Henhouse: The Modern Best Interests of Creditors Test in Chapter 11 Reorganizations', 5 Nev. L.J. 820, 822 et seq. (2005); Charles Jordan Tabb, 'The History of Bankruptcy Laws in the United States', Bankr. Inst. L. Rev. 10, 21 (1995).

[1073] See e.g. Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms (BRRD) [2014] OJ L173/190, Recitals 5, 73, 111, Articles 36 (8), 74; Hodge Malek QC and Sarah Bousfield, 'Bad Banks and the "No Creditor Worse Off" Compensation Scheme', (2016) 6 JIBFL 339; see also Commission's Recommendation (2014), para.22 (c).

[1074] See German Insolvency Code, s 251 (1) No. 1.

[1075] See German Insolvency Code, s 245 (1) No. 3.

[1076] See US Bankruptcy Code s 1129(a)(10).

[1077] See German Insolvency Code, s 245 (1) No. 1 and 2.

[1078] For the English law variation of the APR ('no real economic interest in the company'), see above 8.2.2.

[1079] *Northern Pacific Railway Company v. Boyd*, 228 U.S. 482, 502 (1913).

in response to the common practice of (railroad) company reorganisations in Equity Receivership proceedings in the late 19th and early 20th century. In these proceedings, the assets of insolvent companies were sold in court to a purchasing company who was usually set up by senior lenders and old shareholders. In this way, old equity used to receive a share in the restructured business while unsecured creditors often got paid little to nothing.[1080] The Supreme Court responded by adopting the ranking in a bankruptcy liquidation, where shareholders are residual claimants, to a reorganisation in Equity Receiverships and invalidated a plan that distributed value to shareholders before paying all creditors.[1081] The New Deal legislation in the 1930's introduced this rule to the U.S. Bankruptcy Act 1938 (s 77B). The current Bankruptcy Code 1978 contains the modern version of the APR in section 1129 (b) (2).[1082] Today's APR requires full payment to a dissenting class of secured creditors if any distribution to more junior classes (unsecured or junior creditors, shareholders) is scheduled under the plan. The same applies to the lower ranks. As a result, plan distributions to shareholders cannot be confirmed against a vetoing class of (even junior) creditors. A strict construction of the APR would, thus, require all creditor classes to accept a plan that only leaves shares with existing shareholders.[1083] Recently, a number of scholars have become sceptical of such a strict concept and tried to develop a more flexible rule, a relative priority rule.[1084] A sceptical view of a strict APR can also be found in the Report of the Commission to Reform Chapter 11.[1085]

8.5.4 Appeals and stay pending appeal

648. The confirmation order is a judgement of the court and as such subject to the rules of civil procedure on appeals in most jurisdictions.[1086] These rules may include stipulated periods or permissions for appeals. Only the confirmation of a Latvian reorganisation plan, a Spanish Refinancing Agreement in a Judicial Homolgation procedure, and a (pre- insolvency) recovery plan under Greek law are not subject to an appeal.

[1080] For a detailed description of Equity Receivership practice, see e.g. E. Merrick Dodd jr., 'Equity Receiverships as Proceedings in rem', 23 Ill. L. Rev. 105 (1928); Garrard Glenn, 'The Basis of Federal Receivership', 25 Colum. L. Rev. 434 (1925); Stephan J. Lubben, 'Railroad Receiverships and Modern Bankruptcy Theory', 89 Cornell L. Rev. 1420 (2004); James N Rosenberg, 'A New Scheme of Reorganization', 17 Colum. L. Rev. 523 (1917); Jacob Trieber, 'The Abuse of Receiverships', 19 Yale L. J. 275 (1910).

[1081] *Northern Pacific Railway Company v. Boyd*, 228 U.S. 482, 508 (1913).

[1082] For a more detailed description see Douglas G. Baird, *Elements of Bankruptcy* (5th edn. Foundation Press 2010) 72; Elizabeth Warren, *A Theory of Absolute Priority*, 1991 Ann. Surv. Am. L. 9 (1991).

[1083] The U.S. Supreme Court introduced the idea of a 'new value exception' to the APR in the 1930s arguing that distributions to shareholders were valid as long as shareholder provide new value to the company of (at least) the same amount, see *Case v. Los Angeles Lumber Co.*, 308 U.S. 106, 121 f. (1939). However, the court has not yet applied this exception to current law, see *Norwest Bank Washington v. Ahlers*, 485 U.S. 197 (1988), and *Bank of America Nat'l Trust & Say. Ass'n v. 203 LaSalle St. Partnership*, 526 U.S. 434 (1996); see also Edward S. Adams, 'Toward a New Conceptualization of the Absolute Priority Rule and its New Value Exception', 1993 Det. C.L. Rev. 1445 (1993).

[1084] See Douglas G Baird, 'Priority Matters: Absolute Priority, Relative Priority and the Costs of Bankruptcy', 165 U. Penn L. Rev. 785 (2016); Anthony J. Casey, 'The Creditors' Bargain and Option-Preservation Priority in Chapter 11', 78 U. Chi. L. Rev. 2011, 759; Edward Janger, 'The Logic and Limits of Liens', U. Ill. L. Rev. 2015. 589; Stephen J. Lubben, 'The Overstated Absolute Priority Rule', 21 Fordham J. Corp. & Fin. L. 2016, 581.

[1085] ABI Commission to Study the Reform of Chapter 11 (2014), p. 213: 'inflexible and often a barrier to a debtor's successful reorganization'.

[1086] This reflects international standards, see UNCITRAL Legislative Guide (2004), Recommendation 153, and was also part of the Commission's Recommendation (2014), para. 24.

649. The right to appeal an order confirming a plan is commonly granted to any dissenting creditor (or shareholder), sometimes also to the administrator (Spain, France), a joint debtor (Austria), works councils (France), the public prosecutor (France), or preferential creditors who are not affected by the plan directly but have not yet been fully paid by the estate (Austria).

650. The right to appeal an order denying the confirmation of a plan is commonly granted to the debtor as well as all parties to the plan (Germany) or at least those who supported the plan (Austria). Where a jurisdiction extends the right to third parties (see France), they may also file an appeal.

651. In most jurisdictions, the filing of an appeal does not stay the effectiveness of a confirmed plan unless such a stay is requested and granted[1087]). In jurisdictions with an automatic stay pending appeal, the law often[1088] provides for means to quickly overcome an automatic statutory stay, either by short deadlines for judicial review (Hungary: 8 business days) or by granting a relief lifting the stay if the interests of all parties involved seem superior to those of the appellant (Germany[1089]).

8.6 Effects, modification and termination

652. Once confirmed, a plan is binding the debtor and on all affected (classes of) creditors (and shareholders).[1090] This includes all those who voted against the plan as well as those who did not vote.[1091] In most jurisdictions, a plan covers even creditors who did not receive notice or were yet unknown at the time.[1092] The latter effect is essential when insolvency plans are asked to rescue a business from the devastating effects of an event creating mass tort claims (e.g. product liability claims).

653. The plan is also binding on third parties if the plan contains any provision regarding them and they agreed to be bound (e.g. 'plan proof' preferential creditors, or plan guarantors).

[1087] See Austria, Belgium, Spain, France, Italy, Poland, and England & Wales. In the Netherlands a plan may be implemented while an appeal is heard, but only a final plan binds dissenting creditors.
[1088] Only the Swedish Inventory Report did not refer to any means of preventing unnecessary delay.
[1089] See German Insolvency Code, s 253 (4).
[1090] In line with this principle, a French reorganisation plan adopted in a Procédure de Sauvegarde or a Redressement Judiciaire is only binding on all creditors of the mandatory committees (financial creditors, Main trade creditors, bondholders). Other creditors are not affected; the court may, however, order their claims to be paid over a period of up to 10 years without any plan proposal if such an order is deemed necessary to rescue the business.
[1091] This represents international standards, see World Bank Principles (2016) C14.5; UNCITRAL Legislative Guide (2004) Recommendation 167; Principles of European Insolvency Law (2003) § 11.4. See also the Commission's Recommendation (2014), para.25, 26.
[1092] An exemption is Hungary where only registered creditors are bound by a plan, while creditors who received notice and yet failed to register are barred from subsequently enforcing their claims.

654. In addition, the discharge of the debtor does not extend to joint debtors or guarantors[1093] who remain liable to their secured creditor. However, the plan's discharge does prevent these co-debtors from recourse against the debtor (see Austria or Germany, but also see Italy for a different approach[1094]).

655. The measures described in the plan, in particular plan distributions and modifications of the capital structure of a company, are to be performed by the debtor. German law also allows a plan to authorise the administrator to act on behalf of the debtor.[1095] The question whether and how to supervise the debtor's performance under the plan is answered quite differently in Europe In some jurisdictions, supervising the debtor is optional,[1096] depending on a specific provision in the plan itself (see e.g. Germany) or the debtor's request (Spain). In others, supervision is mandatory for a specific period after the adoption of the plan which means that some (often the court[1097] or only the insolvency practitioner[1098]) or even all officeholders including the court remain in charge (Italy[1099], France[1100], also Romania[1101]).

656. If a debtor is not able to implement all plan measures or make all distributions under the confirmed plan, only a few jurisdictions allow for a simplified modification of the plan.[1102] In France and Poland, for instance, the court may adapt the plan to new circumstances upon request.[1103] In Greece, a plan cannot be amended after its judicial ratification in principle except that in recovery proceedings the agreement can be amended by the bankruptcy court, but only once, based on a subsequent agreement concluded by all the contracting parties and as long as specific conditions are met.[1104]. In many other jurisdictions, where a simplified modification is not available[1105], the debtor is forced to reinitiate plan proceedings and it takes another plan procedure, if available at all, to replace an overly ambitious plan with a new plan.

657. Without a modified plan, any significant default by the debtor commonly leads to a plan failure which then results in the nullification of the plan. As a consequence, all creditor claims are fully reinstated. In a subsequent insolvency (or restructuring) procedure, creditors

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1093 In Germany such contractual security rights providers are to be distinguished from jointly liable partners in a partnership. Here the plan discharging the partnership also releases the partners from their personal liability.

1094 In Italy, the co-debitors and the guarantors who have paid the creditor after commencing the proceeding are allowed to recourse against the debtor only after the secured claim is fully paid.

1095 See German Insolvency Code, s 221.

1096 Such a supervision reflects international standards, see World Bank Principles (2016) C14.4; UNCITRAL Legislative Guide (2004) Recommendation 157.

1097 In Belgium, the court may decide to supervise the debtor ex officio or upon a creditor's request. In Portugal, the court has an annual option to scrutinize the debtor.

1098 An English CVA's implementation is supervised by the insolvency practitioner administering the case.

1099 The supervising judge continues his task until all plan measures are implemented and payments are done.

1100 The insolvency practitioner remains in charge for up to 10 years.

1101 For a mandatory supervision period of 3 years, the insolvency practitioner has to report about the implementation of the plan every 3 month.

1102 Such a modification option reflects international standards, see World Bank Principles (2016) C14.4; UNCITRAL Legislative Guide (2004) Recommendation 156.

1103 French Commercial Code L.626-26; L626-45. Polish Insolvency Code Article 173.

1104 See Article. 106b para. 11.

1105German law, for instance, only allows for correcting obvious errors in a confirmed plan, but not for adapting the plan content to a new scenario; see German Insolvency Code, s 248a.

participate with their original claims. In Belgium, a second plan may not provide for cuts below the level which was guaranteed to a creditor under the first plan.

8.7 Impetus for recommendations

658. Where the rescue of a business requires more cooperation and coordination than a simple sale of the assets of the debtor's business, the negotiation and conclusion of an agreement that binds all parties who must cooperate has proven to be the best way to establish a solid basis for the implementation restructuring measures. If such an agreement cannot be achieved voluntarily with all parties, the process of negotiating and concluding an arrangement should not be replaced (e.g. by a court order or an administrative act). Instead, it is common standard to allow a plan to be binding on all parties if it receives sufficient actual support of the affected stakeholders, and if a court confirms (ex officio or upon request) that the plan complies with all legal requirements and does not discriminate against the dissenting minority.

659. It is essential to test the actual support of a plan for two reasons. First, it assigns the decision whether it is good to rescue the business of an insolvent debtor to those stakeholders that actually invested value (money, time, effort) in the business and who are asked to do so again under the conditions of the plan. The decision about the feasibility and success of a plan restructuring is a decision under uncertainty because success depends on number of uncertain and yet unknown factors in the future. Being a prediction, no one else should be asked to make the decision than those directly affected by a plan's success or failure. The prediction reflects a commercial assessment which should be in the hand of those most involved. The actual support of creditors but also of shareholders and possible other value contributors[1106] must, therefore, be the main factor in a decision-making design. Second, the probability of making a right decision under uncertainty is held to be higher if the independent opinions of individuals with different levels of knowledge and private information are collected as it can be done by a voting procedure. The aggregated information of many has proven to be more accurate even to the opinion of a single expert (e.g. a judge or an expert witness). [1107] From this perspective, plan proceedings are more than just a way to facilitate the indispensable cooperation of stakeholders in the debtor's business.[1108] It is an aggregation mechanism for private information from the group of

[1106] For the value of 'soft variables', see Michelle Harner, 'The Value of Soft Variables in Corporate Reorganizations', University of Illinois Law Review 2015, p. 509.

[1107] The process of preparing and negotiating a plan and, in particular, the process of having a vote from a large and diverse group of people with different expertise and private information actually improves the likelihood of making the right decision about the business under the given uncertainty, see Stephan Madaus, 'On Decision-making in Rescue Cases: Why Creditors and Shareholders should decide about a Rescue Plan', in Bernard Santen and Dick van Offeren (eds), *Perspectives on International Insolvency Law: A Tribute to Bob Wessels* (Kluwer 2014), at 215 for further details.

[1108] It is commonly held that plan proceedings address a coordination problem that is best described by the 'prisoner's dilemma' in game theory, see e.g. Thomas H. Jackson, *The Logic and Limits of Bankruptcy Law* (Harvard University Press 1986) 10; Horst Eidenmüller, *Unternehmenssanierung zwischen Markt und Gesetz* (Köln 1999), 19; Claire Finkelstein, 'Financial Distress as a Noncoorporative Game: A Proposal for Overcoming Obstacles to Private Workouts', 102 Yale L.J. 1992-1993, 2205. However, it may not only be an issue of information asymmetry but also other factors in human behaviour and decision making (see the indications of the 'public goods game' in particular, explained by e.g. James Andreoni, 'Why Free Ride?', Journal of Public people who are most probably in possession of it. At the end of this process, their vote forms a sort of wisdom of crowds that determines whether to try and rescue the business according to the plan.

660. The involvement of a court is essential for safeguarding the procedural as well as substantial rights of all parties. A court could fulfil this task either upon the request of a party claiming a violation of said rights, or ex officio while holding the voting and confirmation hearings. While in a pre-insolvency cases, a more limited role of a court seems preferable (see 1.2.2.), courtrooms are usually the venue of formal proceedings. Here, the need for judicial oversight seems evident. At the same time, a mandatory plan confirmation increases the degree of reliance on a plan because the plan has already passed the test of complying with all legal requirements.

8.7.1 The right to present a plan

661. The right to draft and present a plan should be left with the debtor for an exclusive period of time. Exclusivity allows the debtor to maintain in control of plan proceedings and, thus, provides incentives for troubled debtors to enter rescue proceedings at an early stage of a crisis. Every threat of losing control of the process, especially in the form of a competing plan that could provide for a replacement of the debtor's management or a sale of the business, leads to a situation in which debtors would try to avoid plan proceedings as long as possible.

662. On the other hand, an exclusive right for the debtor to present a plan is, of course, susceptible for abuse. A debtor could initiate plan proceedings for the purpose of stalling claim enforcing creditors as well as delaying any solution to a failing business by making use of an automatic stay.

663. The balance of both aspects could be a combination of an exclusive right for the debtor to present a plan with an efficient test to terminate plan proceedings that are being abused (for termination or conversion of plan proceedings see 1.3). Another option is to allow a debtor to exclusively present a plan only for a stipulated period of time.[1109] The latter option allows experts like an administrator or secured creditors to draw competing plans instead of just waiting for the debtor to come up with a plan, or to being limited to a later negotiation about modifications to the debtors plan. Especially in a procedure that does not exclusively aim at a reorganisation (see Germany, England & Wales or the US), the resulting plan competition could be seen as a valuable tool to publicly offer bids for the business in the form of competing plan. Still, at least an exclusivity period is necessary to protect the restructuring strategy of the debtor and, thus, incentivise debtors to make use of plan proceedings at an early stage.

Economics 1988/37, p. 291; also U. Ones and L. Putterman, 'The ecology of collective action: A public goods and sanctions experiment with controlled group formation', 62 J. of Economic Behavior & Org. 2007, p. 495) that plays a significant role when stakeholder vote on a plan.

[1109] In U.S. Chapter 11, the debtor has the exclusive right to file a plan for (at least) 120 days; see 11 U.S.C. s 1121.

664. In the case of competing plans, the debtor's plan should, therefore, enjoy a priority treatment and, if accepted, be confirmed.

665. Another way to possibly abuse the right to propose a plan could be a debtor filing a subsequent number of plan proposals and, thereby, delaying the process. A response to this threat could be the right of the court to reject any subsequent proposal that cannot prove stakeholder support.

8.7.2 Plan content

666. Any plan content must ensure two things. First, the plan must provide all the information required to allow any voting stakeholder an informed decision about whether they actually want to reinvest their expected insolvency payoff in the debtor's new business plan under the specific conditions and ranking of the plan. In this respect, a plan is a sort of a 'selling prospectus'. Second, the plan must contain all the legal steps that are required to implement the rescue strategy. Here, a plan provides in detail for the new claims or rights of the stakeholders with regard to the debtor and to plan guarantors.

667. In fulfilling these requirements, a plan may become a rather voluminous document in case of the restructuring of larger companies. Here, a mandatory summary would reflect best practice. In addition, the full text of a plan should be available electronically in order to facilitate access for stakeholders. In small business cases, the amount of required information should be rather limited accordingly (for further details on SME cases, see chapter 9).

8.7.3 Scope of a plan and protection of parties

668. The purpose of a plan also suggests that all relevant contributions of any participant in a business rescue should be allowed to be collected in a single document – the plan. If a promising business model of the debtor's business requires modifications on all levels of the debtor's debt and capital structure, a plan could not provide the desired degree of reliance if it was only allowed to comprise the treatment of unsecured claims while any required changes to security rights and secured claims, to preferential claims or the capital structure would instead depend on the success of additional agreements with secured or preferential creditors, or resolutions of a shareholder meeting. The timing of such additional measures in relation to plan proceedings has proven to be rather complex and, in case of a vetoing position, no cram down would be available, even in a case of bad faith. Thus, a plan conditioned on the contribution of a secured creditor would simply collapse (by not being confirmed) if the plan condition proves to be impossible to meet.

669. A statutory authorisation to include all the rights of stakeholders in a (restructuring) plan does, of course, not mean that each plan must include them. It should be decided in each individual case whether the rescue strategy actually requires an involvement of secured creditors' or preferential claims or shareholders' rights. Sometimes, a plan may only contain a single class of all unsecured creditors while not impairing the rights of any other stakeholder.

670. An extended scope of a plan would, of course, require a differential treatment of classes of affected stakeholders in relation to their non-bankruptcy entitlement and their position in an alternative liquidation of the estate.

8.7.4 Secured creditors

671. Today's restructurings must not include secured creditors but they often do, especially in larger cases. As the 'ABI Commission to Study the Reform of Chapter 11' pointed out in its 2014 report, there is not only anecdotal evidence that the percentage of secured debt of insolvent companies has increase significantly in the past decades resulting in the fact that the vast majority of assets is encumbered by security rights.[1110] Efforts by lawmakers, led not the least by UNCITRAL Working Group VI (secured transactions)[1111], support this trend by ensuring that any asset of the debtor, including intangibles, is available for collateralisation. Beyond this background, any restructuring plan without the capacity to address the (by far) largest class of creditors appears outdated.

672. If a proposed plan intends to impair security rights, their classification must reflect sufficiently any substantial difference in the legal rights. Such differences may result from the type of security right and collateral (e.g. mortgages, liens on movables, pledges on shares etc.), but also from their value in an alternative liquidation (e.g. first ranking mortgage and lower ranking mortgages).

673. The adequate protection of security rights holders follows mainly from a probable veto position in their class under the application of the 'no creditor worse off' principle in cases of a cramdown. Under this principle, the liquidation value[1112] of a security *right* is protected and must be distributed under the plan in the form of an adequate (possibly deferred) payment on the secured *claim*. Thus, a fully secured claim is only represented in the plan by the security right while a not fully secured claim would lead to a deficiency claim participating in a class of unsecured claims.

8.7.5 Preferential Creditors

674. The preferential treatment of creditors in ordinary insolvency proceedings is an insolvency policy decision which must, in principle, be respected in plan proceedings (see above chapter 4). The preference of post-commencement creditors for claims resulting from a transaction with the insolvent estate is a particular example. Any threat to their full payment guarantee by a restructuring plan would lower the availability of post-petition credit and supplies which would result in the inability of the debtor or the administrator to continue the business.

[1110] ABI Report (2014), at 12 citing Mark Jenkins & David C. Smith, 'Creditor Conflict and the Efficiency of Corporate Reorganization', available at https://ssrn.com/abstract=2444700, according to which by 2012, secured debt accounted for more than 70 percent of the debt of Moody's rated bankruptcy filers.

[1111] See the new UNCITRAL Model Law on Secured Transactions (2016), available at www.uncitral.org/uncitral/uncitral_texts/security.html.

[1112] The hypothetical position of the secured creditor in a liquidation must be determined in a valuation of the collateral. The standards of valuation must reflect the likely scenario without the plan including a liquidation of collateral in connection with a going-concern sale; see M. Crystal and R.J. Mokal, 'The Valuation of Distressed Companies: A Conceptual Framework', ICR 2006, p. 123, 126.

675. However, the principle of non-infringement should be handled less strictly in jurisdictions with a wide range of preferences for pre-petition creditors. Here, the exclusion of preferential claims from the scope of a plan may result in rendering plans useless. Instead, legislators should consider carefully whether the policy objective that supports a preferential treatment of specific creditors in the distribution of the proceeds of a liquidation actually also requires this claim to be immune from any plan provision. The protection of preferential creditors who reject the plan by voting against it may sufficiently result from the application of the 'no creditor worse off' principle that would guarantee plan payments equal to the likely payment in an alternative liquidation.

676. In addition, lawmakers should consider whether preferences that may have a solid justification in case of a liquidation are also useful in a reorganisation scenario. Here, for instance, the protection of tax revenues may be served better by focusing on the rescue of viable businesses and future tax incomes instead of protecting unpaid tax claims (see chapter 4 for a discussion of preferential claims). Employees may also expect to continue working with the business in a reorganisation and extended mandatory guarantee scheme (see chapter 5, recommendation 5.07) could sufficiently provide for social protection.

8.7.6 Other creditors

677. The satisfaction or write-off of unsecured and non-preferential claims or ordinary claims forms the traditional scope of a plan. Here, a classification of creditors that reflects the differences in their legal position (e.g. bondholders – possibly holding bonds with different maturity, suppliers, subcontractors, and customers) ensures that a single sub-group (like e.g. bondholders) may not dominate the voting process by marginalising creditors with smaller claims or in smaller numbers.

678. Creditors with subordinated claims (e.g. mezzanine lenders or shareholder loans; see above chapter 4) also fall into the traditional scope of a plan. They would form their own class(es) and be entitled to vote. As these creditors often cannot expect to receive anything in a liquidation, cramdown rules ensure that these classes are not able to veto a plan that found sufficient support in other classes. The common test ('no creditor worse off') sufficiently reflects their subordination without fully disenfranchising these creditor classes.

8.7.7 Shareholders

679. In case of a company debtor, the rescue of a business may require changes in the capital structure of the company. New shares may be issued to attract new equity investors. Usually, giving shares to old creditors is a useful way of "paying" them without the need to pay them in cash. In order to create new shares or transfer existing shares, the debtor not only needs to convince creditors to re-invest their possible pay-off in exchange for shares. Company law requires all existing shareholders to (exclusively) decide whether and how to write off old and issue new shares.

680. Insolvency law has been of little help in this area for a long time. As the shares of the debtor company are not owned by the debtor, they do not form a part of the estate. Just like

when enforcing their claim outside of insolvency proceedings, creditors have had no access to the shares of the company in insolvency proceedings as they are not part of the insolvent's estate. Instead, the involvement and cooperation of shareholders is required to implement a redistribution of shares or to issue new shares according to a debtor's rescue plan.

681. As we have shown, most jurisdictions have yet neither followed the US nor English approach of shareholder involvement in (pre-)insolvency proceedings. Leaving the realm of company law untouched by insolvency law provisions, these jurisdictions rely on the good will cooperation of shareholders in the event of a business failure to negotiate and later implement a plan solution that includes a modification of the firm's capital structure. Thus, any such plan would depend on its implementation by the shareholders under company law rules (and majorities).

682. However, the resulting dependency of a plan is disadvantageous for all parties. It seems preferable to follow the Anglo-American and German approach as far as their law involves all shareholders in plan proceedings as soon as a plan proposal includes a modification of shareholder rights. Negotiations towards or following such a proposal as well as the voting process itself would include shareholders who would form a separate class entitled to vote.[1113] And if a shareholder class accepts the plan with a stipulated majority[1114], all shareholders are not only bound to implement a new capital structure according to the plan, but the plan itself may even serve as the decision required under company law to change the capital structure by, for instance, issuing new shares or transferring shares. As a result, a confirmed plan would provide all-round solution with legal certainty about the implementation of the plan for all stakeholders.

683. If a class of shareholders, however, does not accept the plan, a cross-class cramdown should be available in principle if the plan finds sufficient actual creditor support. Such a coercive element facilitates restructuring negotiations as it decreases the leverage of shareholders at the table. At the same time, the specific design of such an element is subject to longstanding controversy.

684. The main or even sole argument in favour of a cross-class cramdown bears on an economic perspective. As was shown above for US and English law, shareholders of an insolvent company who cannot expect to receive any value in a liquidation of the company's assets are held to have no "real economic interest in the company". As a consequence, they

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[1113] Such a direct involvement of shareholders also reflects the fact that the duties of directors of failing or insolvent companies commonly expand to also include the interests of creditors (and possibly other stakeholders) affected by a failure. With directors not bound to shareholder interests anymore, shareholders require a different, more direct way to be heard. The value of hearing the voice of a minority group which shareholders certainly are compared to the classes of creditors, comes from aggregating their private information and, possibly, strengthening the decision-making process, see also Dov Solomon, 'The Voice. The Minority Shareholder's Perspective', 17 Nevada Law Journal 739 (2017), available at https://ssrn.com/abstract=2868725 (for the decision-making process in a public company).

[1114] The majority could basically follow company law rules. However, if company law would require the support of all shareholders, e.g. of a partnership, insolvency law should allow for a majority vote to prevent unjustified hold-outs.

should not be able to veto a plan solution for an insolvent company, even if the plan provides for a reorganisation.

685. There is, however, some rationale to question this simple deduction:

- 'Comparative argument': If the presumption is good that shareholder rights or interest in a restructuring should not be different or even better than in an alternative liquidation, why should it only apply to shareholders, but not creditors? In any liquidation inside or outside insolvency proceedings, creditors would only have access the value of the company's assets by auctioning them off. They could neither access the debtor's entity itself nor the shares. As a result, any assignment of rights in a reorganisation according to a distribution in a hypothetical liquidation creates a dilemma because the extra value, that is solely connected to the entity (e.g. in form of favourable rental agreements or licenses) and available only in a restructuring of the debtor, could neither be claimed by the debtor nor the creditors in such a liquidation. It simply would not be generated there.[1115]

- 'Purpose argument': Commonly, insolvency law is held to be a form of (collective) enforcement law because it portraits well the aspect of insolvency proceedings that allows of an equal enforcement of creditor claims by orderly liquidating the debtor's assets. It seems natural to also view the reorganisation of an insolvent debtor from a general enforcement law perspective.[1116] If we, however, include all current forms of debt restructurings in troubled companies to our analysis, the contractual nature of such arrangements appear to be a more dominant factor than the enforcement of claims, because it is not only inherent to workout agreements, but also to schemes or reorganisation plans in (pre-)insolvency proceedings. Under such a perspective, the assignment of rights and interests in a reorganisation would better be governed by contract law principles (including an obligation to enter into a contract in cases of abusive or discriminating refusals). It leaves little room to apply enforcement law distribution rules.

- 'Extra value ownership argument': It seems also questionable to simply suggest that all extra value extracted in a restructuring must be allocated to creditors as long as they have not yet been paid in full. This assumption is governing US, English and German restructuring law, best highlighted in their "absolute priority rule", but the assumption itself seems to beg the question. If a specific value can only be created in cooperation with the entity and its legal owners (shareholders), it might not belong to creditors *alone* in the first place. The argument that shareholders with no real economic interest cannot claim any value (including the extra value from cooperation) as long as creditors have not yet been paid in full has no legal basis. First, it is not consistent with property law, because, during reorganisation

[1115] See Stephen J. Lubben, 'The Overstated Absolute Priority Rule', 21 Fordham J. Corp. & Fin. L. 2016, 581, 603 pointing at the trouble that begins by duplicating a rule for the distribution of liquidation proceeds in the reorganisation context. See also Douglas G. Baird, 'Priority Matters: Absolute Priority, Relative Priority and the Costs of Bankruptcy', 165 U. Penn L. Rev. 785, 788 (2016): 'much of the complexity and virtually all of the stress points of modern Chapter 11 arise from the uneasy fit between its priority regime (absolute instead of relative) and its procedure (negotiation in the shadow of a judicial valuation instead of a market sale).'

[1116] See Valeria Confortini, 'Privatautonomie and Corporate Reorganisations: Legal Treatment of Shareholders under Insolvenzordnung and Italian Insolvency Law', IILR 2016, 6 10.

proceedings, the legal ownership of the entity still rests with the shareholders. Second, creditors cannot claim the extra value based on their pre-insolvency rights because they are not entitled to this value under any enforcement law. Stating such a right in insolvency turns out to be a petitio principii.

- 'Creditor's privilege argument': A strict APR improves one-sidedly the position of creditors. Outside of reorganisation proceedings, a creditor may decide to maintain the investment in the debtor's business in case of a default which means to waive the right to declare a default (and to accordingly repossess collateral in case of secured creditors). In reorganisation proceedings, a creditor may decide to do just the very same, e.g. by accepting a plan that offers him the adapted value of his rights. Outside of reorganisation proceedings, however, creditors may not keep their stake in the firms and, at the same time, also eliminate junior creditors and shareholder in the capital structure while under insolvency law, a strict APR compels reorganisation plans that eliminate junior stakeholders. A more flexible (relative) priority rule would better reflect pre-insolvency entitlements as it allows to create a new capital structure that also keeps everyone in the picture. As *Douglas G Baird* puts it: "Such a new capital structure can be consistent with the firm's current financial condition (doing away with such things as the obligation to pay dividends and interest as well as stripping junior investors of voting or other control rights), yet still recognize the junior investors' right to any excess that remains when, at some time in the future, all the accounts are ultimately squared. This is the essence of relative priority."[1117]

- 'Shareholder protection argument': Any rule that disregards a shareholder vote for the simple reason of not having a "real economic interest in the company" may also conflict with the protection that a shareholder enjoys under the fundamental rights guarantees of constitutional law. Here, the right of property usually includes protection of shares and may not only provide for a due process guarantee and sufficient compensation if the owner of a share was to be expropriated. An infringement of ownership may also meet further requirements under the restriction of commensurability, like e.g. the size of the debtor or systemic risks resulting from not confirming the plan.[1118] Beyond the right of property, shareholders may also have the protection of other, more specific constitutional rights. In Germany, for instance, Article 9 of the constitution provides for the right to establish (and manage) a company. It is discussed whether the resulting protection conflicts with the existing rules of a cross-class cramdown because shareholders are rendered defenceless in insolvency proceedings.[1119] This issue has already been discussed in the light of shareholder protection under the Second Company Law Directive[1120] by the CJEU stating that in the case of a failing bank of systemic relevance the "provisions of the Second Directive do not preclude an exceptional measure affecting the share capital of a public limited liability company, such as the Direction Order, taken by the

[1117] Douglas G. Baird, 'Priority Matters: Absolute Priority, Relative Priority and the Costs of Bankruptcy', 165 U. Penn L. Rev. 785, 791 (2016).
[1118] See also the decision of the French Constitutional Council about the very cautious new French rules in the Law Macron of 2014 in Decision No. 2015-715 DC, 5 August 2015, §145.
[1119] See Stephan Madaus, ‚Keine Reorganisation ohne die Gesellschafter', ZGR 2011,p. 749, 761.
[1120] Directive 2012/30/EU of 25.10.2012, OJ L315, 74; replacing Directive 77/91/EEC of 13.12.1976, OJ L 26, 1.

national authorities where there is a serious disturbance of the economy and financial system of a Member State, without the approval of the general meeting of that company, with the objective of preventing a systemic risk and ensuring the financial stability of the European Union."[1121] A common business failure without such a risk to the financial stability of the EU would probably not suffice to ignore the protection under the Second Directive.[1122]

In addition, any cross-class cramdown rule that renders shareholders defenceless may also conflict with existing Bilateral Trade Agreements protecting foreign shareholders under their investment protection rules. These rules require a "fair and equitable" treatment of investor rights by local law including insolvency law. Recent arbitral awards indicated that arbitral tribunals are inclined to sceptically reassess the application of insolvency law by local courts.[1123] A strict rule that abnegates any effective shareholder standing in restructuring proceedings when losing their rights may not stand this test even if such rules have been common to some jurisdictions for quite some time.

686. With regards to all arguments presented, a balanced cross-class cramdown rule based on contract law principles seems preferable. Such a rule would find a "fair and equitable" treatment of shareholders in a plan depending on the conditions that the shareholders *agreed to* when they invested in the firm.

(1) Shareholders who took an interest in the firm in terms of a *financial investment* are treated adequately in a restructuring or in insolvency if the law only respects their economic interest. If financial investors accept an equity position in a firm instead of a bondholder or a creditor position, they should not be allowed to veto a restructuring plan that simply reflects this decision. The justification to apply the common ranking of a liquidation, where shareholders are the residual claimants, to a restructuring, and to the allocation of any extra value, can be found in the prior investment decision of each shareholder. Still, shareholder protection under applicable constitutional law or bilateral trade agreements may require to give affected shareholders access to court and a claim for adequate compensation in case of any residual value. Depending on local jurisprudence, some additional preconditions might be required, like e.g. the "no alternatives" test or the test of the economic relevance of the debtor company as found in French law. Shareholders could, of course, also raise objections against a plan confirmation relying on the general grounds to deny confirmation, like e.g. the unequal treatment of shareholders of the same class or any creditor getting paid more the 100 percent. Such a confirmation rule would respect the pre-insolvency priority regime. It should, however, not dictate that junior creditors or shareholders may not receive any value before all senior creditors have been paid. Instead, it should be possible (not

[1121] ECJ, 8.11.2016, C-41/2015 *Dowling* EU:C:2016:836 at p. 51.

[1122] The European Commission addresses this issue in its Proposal Restructuring Directive (2016) by adding a safe harbour from the shareholder protection under the Second Directive in a proposed Article 32.

[1123] See in particular *Dan Cake (Portugal) S.A. v. Hungary* ICSID Case No. ARB/12/9; see also *Yukos Universal Limited (Isle of Man) v. The Russian Federation* PCA Case No. 2005-04/AA227. In each cases the application of national insolvency law was held to be unfair and damages were awarded to foreign equity investors. See also Axel Flessner, ‚Insolvenzrecht und Investitionsschutz nach TTIP und CETA - ein noch unbemerkter Konflikt', ZIP 2016, p. 1046.

necessary) to keep such stakeholders in the capital structure as long as the plan provides that they only receive distributions on their rights after senior claims have been paid according to the plan (relative priority).

With regards to the constitutional requirement of proportionality, the rights of disenfranchised shareholders could be respected even further in a debt to equity swap plan scenario by introducing a mandatory option to buy back shares after the swap for cash from creditors. Such a rule would not only allow shareholders to reinvest in "their" restructured firm for a market price. It would also offer creditors a quick way to exit the company for cash, in particular if their shares are not traded stock.

(2) Shareholders who not only invested in the company but also manage or otherwise work for the company (*soft variables contributors*,[1124] like e.g. an owner-manager craftsman, artist, doctor or lawyer) deserve more protection in a restructuring because they did not set up or enter the company with a sole view on a financial investment. The simple reduction of their involvement to an economic interest and the determination of their rights solely under aspects of the capital structure of a firm is not adequate here because such shareholders are not just financial (money) investors. In addition, a restructuring would quite often depend on the continuation of their daily contribution (as a doctor, lawyer, craftsman or cook) anyway. At the same time, protection from losing the business to creditors in a restructuring (in contrast to a liquidation) would form an incentive family businesses as well as single shareholder-managers to positively approach restructuring instruments. Against such shareholders, a cross-class cramdown would not be available. Any plan restructuring of such companies would either have to leave shareholder rights unimpaired (which would still allow for a debt to mezzanine swap to get access to future revenue[1125]), or it would have to seek the support of (a majority of) shareholders.

(3) Another type of treatment seems adequate in a *corporate group restructuring* cases where shares are fully owned by parent companies. Here, the rules of corporate insolvency law provide for mechanisms of coordination and cooperation, in some jurisdictions also options for a procedural consolidation which prevail and govern the restructuring of a corporate group. A cross-class cramdown should not interfere.

687. The suggested differentiated treatment of specific types of shareholders avoids the downsides of a strict absolute priority rule (APR) that emerge whenever a plan would distribute value to shareholders without fully paying all creditors including junior creditor. Under a strict APR, any class of junior creditors could veto such a plan unless the receiving shareholders provide for new value under the plan under a 'new value exception' rule.[1126] In

[1124] For the specific term of 'soft variables', see Michelle Harner, 'The Value of Soft Variables in Corporate Reorganizations', University of Illinois Law Review 2015, p. 509, 519.

[1125] See Stephan Madaus, 'Reconsidering the Shareholder's Role in Corporate Reorganisations under Insolvency Law', 22 Int. Insolv. Rev. 106, 115-116 (2013).

[1126] As already explained earlier, the U.S. Supreme Court introduced the idea of a 'new value exception' to the APR in the 1930s arguing that distributions to shareholders were valid as long as shareholder provide new value to the company of (at least) the same amount, see *Case v. Los Angeles Lumber Co.*, 308 U.S. 106, 121 f. (1939). However, the court has not yet applied this exception to current law, see *Norwest Bank Washington v.*

contrast to that, a differentiated application of the APR would protect junior creditors who oppose a preferential treatment of shareholders who made financial investments just like they did. Here, a mandatory purchase option for shareholders would render a "new value exception" dispensable. At the same time, soft variables contributing shareholders would not fall into the scope of the APR which means that leaving value (shares) with these shareholders would not create a veto opportunity for creditors.

8.7.8 'No creditor worse off' principle, APR and valuation

688. The common test of the fairness of a plan focusses from a strict legal angle on what each individual creditor would have received in the scenario without the plan, usually a liquidation, according to their ranking. In the abstract, this is a wonderful concept. It refers to the economic, instead of the nominal, value of a claim or right by assessing how much payoff a creditor had received if his claim were to be enforced in a regular insolvency liquidation of the assets of the insolvent debtor. In theory, this value is all what they can expect facing an insolvent debtor. Any plan alternative must, therefore, offer at least just as much to dissenting creditors or otherwise the plan harms their (constitutionally protected) property rights.

689. In practice, however, it is usually not a simple task to determine the payoff of a creditor in a hypothetical liquidation because the payoff depends on the value of the assets of the debtor, in case of a business rescue, on the value of the debtor's business in a liquidation scenario. There are several factors which complicate valuation. First, the liquidation scenario is not simply the scenario of a piecemeal liquidation. Regular insolvency proceedings allow for a going concern sale of (a viable part of) the debtor's business which means that such a sale also needs to be reflected when applying the 'no creditor worse off' test.[1127] In practice, however, it can be difficult to determine whether there is a potential buyer in a purely hypothetical liquidation scenario and which price could be negotiated in a hypothetical going concern sale. Second, setting the price for a business in a hypothetical sale is usually done by way of expert testimony referring to generally accepted methods of valuating a business.[1128] The assumptions in such expert opinions as well as the resulting numbers are, however, open for debate which often prompts parties to present contradicting expert opinions in support of their opinion. As a result, disputes about valuation are easy to start, expensive and time consuming.[1129] To avoid such disputes, several models have been suggested which all aim at providing a real market price for a business.[1130] Unfortunately, none of these ideas

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Ahlers, 485 U.S. 197 (1988), and *Bank of America Nat'l Trust & Say. Ass'n v. 203 LaSalle St. Partnership*, 526 U.S. 434 (1996); see also Edward S. Adams, 'Toward a New Conceptualization of the Absolute Priority Rule and its New Value Exception', 1993 Det. C.L. Rev. 1445 (1993).

[1127] See e.g. M. Crystal and R.J. Mokal, 'The Valuation of Distressed Companies: A Conceptual Framework', ICR 2006, p. 123, 126.

[1128] For an overview of current valuation techniques, see G. Smith and D. King, 'How lnsolvency Practitioners Value a Business', 28 Insolvency Intelligence 2015, 20. For a look at their evolution, see Michael Simkovic, 'The Evolution of Valuation in Bankruptcy', Seton Hall Public Law Research Paper, available at https://ssrn.com/abstract=2810622, Am. Bankr. L. J. (Forthcoming).

[1129] See Douglas G. Baird, 'Priority Matters: Absolute Priority, Relative Priority and the Costs of Bankruptcy', 165 U. Penn L. Rev. 785, 788 (2016): A "nonmarket valuation procedure […] is costly and prone to error."

[1130] See e.g. P. Aghion, O. Hart and J. Moore, 'The Economics of Bankruptcy Reform', 8 J.L. Econ. & Org. 1992, 523; Lucian Arye Bebchuk, 'A New Approach to Corporate Reorganizations', 101 Harv. L. R. 1987-1988, p. 775, 785; David Hahn, 'When Bankruptcy Meets Antitrust: The Case for Non-cash Auctions in Concentrated Banking could solve the valuation challenge so far. Moreover, these models were only developed for publicly held companies.

690. As things stand, the issue of valuation and valuation disputes may only be resolved by using procedural means. The law on plan proceedings should provide that any plan proponent must evaluate the business in a probable liquidation scenario and attach a calculation or expert opinion explaining the value to the plan. That gives each affected creditor (and shareholder) the chance to see whether they agree with the valuation and whether they would receive less under the plan than in an alternative liquidation. If a creditor (or shareholder) does not agree with the valuation and, therefore, holds that they receive less under the plan, they may vote against the plan. Being a minority creditor (or shareholder) in a class or facing a cross-class cramdown, the dissenting party may file an objection in the confirmation hearing. Here, the fact that a majority of creditors (and shareholders) accepted the plan allows for the assumption that the plan provides a better solution than a liquidation for the creditors (and shareholders) as a whole. An objecting dissenting party must, therefore, prove that they individually are worse off under the plan. Giving the uncertainties of a valuation, any such objection should be required to present expert testimony showing that the objecting party would *evidently* do better in an alternative liquidation.

8.7.9 Confirmation standards

691. A plan may only be confirmed by a court if it complies with all legal requirements. These requirements should be designed in a way that the judges asked to confirm a plan makes legal, but not business decisions. The decision to invest in the business based on the plan is a stakeholder, usually a creditor decision. This decision includes the assumption of a feasible plan. It should not be part of a judge's task, therefore, to assess a plan's feasibility. It should also be left with the stakeholders, and not with the judge, to decide whether they want to invest in the business of a debtor who has a criminal record or tried to withhold information if these circumstances were disclosed in the plan. Investors should decide whether the debtor still deserves a second chance.

692. The list of legal requirements should include:

- the disclosure of all relevant information by the debtor;
- the proper classification;
- the acceptance of the plan by all classes (by actual majority support in all classes or application of a cross-class cramdown rule);
- the actual consent of essential third parties (e.g. plan guarantors, regulatory bodies, etc.); and
- the presentation of the plan in good faith and in compliance with public policy (e.g. no tax avoidance scheme).

Upon the request of a creditor or shareholder who actually voted against the plan, confirmation should be denied if the plan does offer less value to this individual creditor that what he would have received in an alternative liquidation. To tackle creditor/shareholder

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Markets', 11 Stan. J.L. Bus. & Fin. 2015, 28; O. Hart, R. La Porta Drago, F. Lopez-de-Silanes and J. Moore, 'A New Bankruptcy Procedure that Uses Multiple Auctions', 41 Eur. Econ. Rev. 1997, p. 461 et seq.; Mark J. Roe, 'Bankruptcy and Debt: A New Model for Corporate Reorganization', 83 Colum. L. Rev. 1983, p. 527, 559.

passivity, every creditor and shareholder who does not participate by voting or by filing an appeal should be deemed to accept the treatment of their claim or right under the plan.

8.7.10 Implementation, supervision and termination

693. The implementation of a confirmed plan should only be stayed pending appeal upon the request of the appellant and if the appellate court deems a stay to be appropriate. Otherwise, the delay cause by filing appeals may effectively destroy a plan's feasibility.

694. The implementation and execution of a plan should be supervised in the interest of all parties if the plan provides for supervision, but not ex officio. Supervising all confirmed plans by a court has proven to be quite burdensome to the judicial system because judges are not allowed to close files even if there is no indication for a problem. In the same way, reporting duties regardless of specific cause bind the capacity of insolvency practitioners and result in additional costs without justification. Instead, proceedings (including all office holders' involvement) should end after the final confirmation of the plan. Sufficient protection for creditors against defaulting or even fraudulent debtors is available under general contract, company and insolvency law rules which are fully applicable again. In addition, creditors should be able to include supervision provisions to the plan which can either be contractual in nature (e.g. reporting duties under covenants) or make use of a specific statutory right to mandate the insolvency practitioner (or an independent auditor), supervise the debtor and alarm the creditors in case of wrongful actions or a negative development in order to allow them to initiate a plan modification or new (insolvency) proceedings.

695. A negative business development or a default should not immediately result in invalidating the original plan. Instead, debtors should be allowed to turn to the original court where they could either argue that the default is not significant and will be cured immediately, or present a modified plan, which reacts to the changed circumstances that caused an incurable default, with the request to initiate a vote on the modified plan by affected creditors only. Only if the modified plan is not accepted or not confirmed, the debtor should be forced to initiate a new round of proceedings, probably liquidation proceedings, in which the creditors of the debtor will participate with their original claims.

8.7.11 Tax exemption

696. Finally, although not mentioned in the Inventory Reports, the restart of a troubled firm under a reorganisation plan must not be burdened by a tax regime that considers a debt relief under the plan taxable income and creates an immediate income tax claim. A restructuring framework should comprise a reliable income tax exemption.

8.8. Recommendations

Recommendation 8.01: Member States should ensure that in cases where the rescue of a business requires more than just a sale of the business, a restructuring plan is available that is binding on all parties of a restructuring if it receives sufficient actual support of affected stakeholders, and if a court confirms (ex officio or upon request) that the plan complies with all legal requirements.

Recommendation 8.02: Member States should grant the right to present a plan exclusively to the debtor, at least for an initial period of time long enough to negotiate and modify the proposed plan, and have a vote. An accepted debtor plan should be confirmed notwithstanding a competing plan.

Recommendation 8.03: Member States should require the plan proponent to disclose all information relevant for an informed decision about the proposed plan. Such a full disclosure should be easily accessible (electronically) and be accompanied by an executive summary.

Recommendation 8.04: Member States should allow a plan to contain all measures required to rescue the business. They should also require a plan to describe and explain these measures. The range of tools should include the impairment of security rights and shareholder rights. With respect to preferential claims, Member States should recognize that only a preferential treatment of stakeholders that are essential to keep the business alive should not be affected by a plan.

Recommendation 8.05: Member States should reflect the diversity of creditors and shareholders which can be affected by a plan by mandating a classification. They should prompt the court to scrutinise the non-discriminatory classification in a proposed plan.

Recommendation 8.06: All creditors and shareholders whose rights are impaired by the plan should be allowed to vote. The weight of their vote should reflect the value of their claim or right in a class. Disputes with regard to their claim, right or voting right should be solved immediately and finally by the disputing parties and, eventually, by the court without prejudice for a later proof of claims for distribution rights.

Recommendation 8.07: Pending further requirements under local constitutional law on fundamental rights, Member States should allow a cross-class cramdown against a class of creditors and shareholders. In case of a shareholder class, such a cramdown should only be available if affected shareholders took an interest in the firm in terms of a financial investment.

Recommendation 8.08: Member States should bind the court to confirm a plan unless it does not comply with specific legal requirements regarding content, acceptance and fairness of the plan.

Recommendation 8.09: The court should not be asked to make business decisions. It should only hear objections of creditors or shareholders who actually voted against the plan. Objections based on the valuation of the business should only be heard if the objecting party presents expert testimony showing that it would evidently do better in an alternative liquidation.

Recommendation 8.10: Member States should provide that a confirmed plan is binding on all parties. Any appeal against the confirmation order should, in principle, not stay the implementation of the confirmed plan.

Recommendation 8.11: Member States should allow any plan to provide for a supervision of the implementation of all plan provisions.

Recommendation 8.12: Member States should ensure that only a significant failure of the debtor to perform invalidates the plan and its effects. Here, the debtor may prevent such a harmful event by filing a modified plan which then must be accepted by affected creditors and confirmed by the court again.

Recommendation 8.13: Member States should ensure that a debt relief under the restructuring plan is not considered taxable income.

CHAPTER 9:
Corporate group issues

9.1. Introduction

697. Since the last decade of the last century, the need to treat an enterprise group in insolvency proceedings as one unit is looking for an adequate legislative answer.[1131] An efficient administration of insolvency proceedings related to companies belonging to the same group would minimize costs and loss of time, should minimize losses for creditors, employers and shareholders of the companies, assembled in the group and would maximise the groups' value. However, national insolvency laws applicable in the EU as well as international proposals are based on the central principle of insolvency law, generally being the principle of the 5 one's: one insolvent debtor, one estate, one insolvency proceeding, one court and one insolvency office holder.[1132] It is rather complex to apply this strict legal foundation to the economic phenomenon of a group of companies. Remarkably, however, as of 26 June 2017 the EIR (2015) applies a novelty in that groups of companies are addressed in some twenty legislative provisions, in an aim to '… ensure the efficient administration of insolvency proceedings relating to different companies forming part of a group of companies'.[1133]

698. Groups of companies, common in today's corporate world, differ greatly as to structure, organization, financing, ways of management and control and ownership. The kind of structures may involve subsidiaries, sub-subsidiaries, service companies, joint ventures, and equity ownership.[1134] According to UNCITRAL, a company group, for a working definition, may be described as '… two or more legal entities (group members) that are linked together by some form of control (whether direct or indirect) or ownership'.[1135] The EIR (2015) – while respecting the separate legal personality of each group member – tries to overcome basic legal notions regarding cross-border insolvencies of groups of companies, using as a definition of a group of companies '... a parent undertaking and all its subsidiary undertakings'.[1136] A parent company is an undertaking which controls either directly or indirectly, one or more subsidiary undertakings. An undertaking which prepares consolidated financial statements in accordance with Directive 2013/34/EU on annual financial statements shall be deemed to be a parent undertaking. According to Directive 2013/34/EU different types of subsidiaries exist: (i) an undertaking in which another

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[1131] The contribution to this chapter by Dr Samantha Renssen, assistant professor of Corporate and Insolvency Law, Maastricht University, is gratefully acknowledged.

[1132] See Jessica Schmidt, 'Das Prinzip "eine Person, ein Vermögen, eine Insolvenz" und seine Durchbrechungen vor dem Hintergrund der aktuellen Reformen im europäischen und deutschen Recht', KTS 2015, p. 19-53.

[1133] See Recital 51 and Chapter V of the EIR (2015) ('Insolvency proceedings of members of a group of companies'), Articles 56 to 78 EIR (2015), further discussed at para. 9.4.

[1134] I. Chaika, 'Insolvency of Group of Companies through the prism of the Recast Insolvency Regulation (EU) 2015/848', Institute of International and European Insolvency Law, University of Cologne, Germany.

[1135] UNCITRAL Legislative Guide (2010), p. 5. Part Three was available in 2010, and published as an e-book in 2012, to be downloaded from http://www.uncitral.org. For a detailed overview, see Bob Wessels, *International Insolvency Law Part I. Global Perspectives on Cross-Border Insolvency Law*, (4th ed., Deventer: Kluwer, 2015), para. 10425b et seq or Bob Wessels and Gert-Jan Boon, *Cross-Border Insolvency Law, International Instruments and Commentary* (2nd Ed., Alphen aan den Rijn: Kluwer Law International 2015), para. 12.

[1136] Article 2(13) EIR (2015).

undertaking (parent company) has a majority of the shareholders' or members' voting rights, (ii) an undertaking in which the parent company has the right to appoint or remove a majority of the members of the administrative, management or supervisory board and is at the same time a shareholder in or member of that undertaking, and (iii) an undertaking in which the parent company has the right to exercise a dominant influence over it of which it is a shareholder or member, pursuant to a contract entered into with that undertaking or to a provision in its memorandum or articles of association, where the law governing that subsidiary undertaking permits being subject to such contracts or provisions.[1137]

9.2. The phenomenon of groups of companies

699. In 2010 UNCITRAL acknowledges that although the number of cross-border insolvency cases has increased significantly since the 1990s, but that the adoption of legal regimes, either domestic or international, equipped to address cases of a cross-border nature has not kept pace. The result has often been inadequate and uncoordinated approaches, unpredictable solutions, whilst there is a lack of recognition of the rights and priorities of existing creditors, the treatment of foreign creditors and the law that will be applicable to cross-border issues.[1138]

700. Several factors shape the formation of group of companies, ranging from legal and economic (operational, managerial, financial) factors to societal, cultural, and institutional factors. Advantages of conducting business through a group of companies are reduction of commercial risk and maximization of financial (including tax) returns.[1139]

701. A company group may have a vertical structure, with succeeding layers of parent and subsidiaries, or a horizontal structure, with many sibling group members.[1140] As to organization and ownership, an overall distinction can be made between groups in the US and in continental Europe. In the US, groups with 100 percent owned subsidiaries are common, while in continental Europe the parent companies usually own less of the subsidiaries, just enough to maintain control.[1141] Groups are also run in different ways. Some are tightly controlled by the parent company, while others are loosely combined with a high level of independency of the several companies.[1142] Moreover, groups have different legal forms. This depends on the corporate forms available in the national jurisdictions (such as private limited liability companies, public limited liability companies, either stock listed or non-listed, and (commercial) partnerships), but also on an international level, such as the

[1137] Article 22 (1) Directive 2013/34 on annual financial statements.

[1138] 'There is often a clear tension between the traditional separate legal entity approach to corporate regulation and its implications for insolvency and the facilitation of insolvency proceedings concerning a group or part of a group in a cross-border situation in a manner that would enable the goal of maximizing value for the benefit of all creditors to be achieved.' See UNCITRAL Legislative Guide (2010), p. 85.

[1139] UNCITRAL Legislative Guide (2010), p. 11.

[1140] UNCITRAL Legislative Guide (2010), p. 11.

[1141] K.J. Hopt, 'Groups of Companies. A Comparative Study on the Economics, Law and Regulation of Corporate Groups', Law Working Paper N. 286/2015, Max Planck Institute for Comparative and International Private Law and ECGI.

[1142] J.H. Dunning, 'Multinational Enterprises in the 1970's, An Economist's Overview of Trends, Theories and Policies' in K.J. Hopt (ed.), European Merger Control (Berlin, New York 1982), p. 3-23.

Societas Europaea (SE). The choice of the type of undertaking is most often tax-driven.[1143] In our report we limit ourselves to matters of insolvency.[1144]

9.3. Significant elements from national regimes

702. With regard to company group issues in insolvency law, studied from a national perspective, several questions arise. Firstly, does national insolvency law make special provisions for insolvent groups of companies in a domestic context? And if not, how are such cases handled? Secondly, does national insolvency law allow for procedural consolidation of domestic insolvency proceedings concerning companies in a company group? Lastly, does national insolvency law allow for substantive consolidation of domestic insolvency proceedings across a company group into a single procedure, and if so how and subject to what limitations? To illustrate the difference between procedural consolidation and substantive consolidation, one could think of the following questions: does insolvency law allow for any kind of joint administration of insolvency proceedings of group members? Respectively: if consolidation takes place to the detriment of individual creditors, are such creditors entitled to compensation out the consolidated estates?

9.3.1. Special provisions for insolvent groups of companies in a domestic context

703. Nowadays, most Member States do not provide for special provisions for insolvent groups of companies. Evidently, this is because the phenomenon contradicts the fundamental principle that each individual company is deemed to be a single legal entity, in control over its own assets. For the purposes of restructuring and insolvency a single company is a debtor, unrelated to for instance a sister company, a parent-company (who is a shareholder) and even – for that matter – unrelated to a lender or a principal customer. As a consequence, according to the insolvency laws of most Member States, a separate insolvency proceeding must be opened with respect to each insolvent company of a group.

[1143] W. Schön, 'Perspektiven der Konzernbesteuerung', Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht 171 (2007), p. 409-445. See on the widely spread lack of solutions of an integrated concept of group insolvency: Stephan Deyda, Der Konzern im europäischen internationalen Insolvenzrecht (Baden-Baden: Nomos, Schriften zum Insolvenzrecht no. 20, 2007); Irit Mevorach, Insolvency Within Multinational Enterprise Groups, (Oxford University Press 2009); Robert van Galen, 'International groups of insolvent companies in the European Community', International Insolvency Law Review 3/2012, 376 et seq; idem, 'Groups of Companies in Cross Border Cases and Rescue Plans', Report to the Netherlands Association for Comparative and International Insolvency Law 2012, available at www.naciil.org; S.A.P. Franssen, 'Corporate Group Insolvencies: One Company, One Insolvency, One Proceeding … or Consolidation?', in J.J.A. Hamers, S. Rensen, C.A. Schwarz & R.A. de Wolf (eds.), Young Corporate Lawyers 2014 (Zutphen: Uitgeverij Paris 2014), p. 53 et seq.; Reinhard Bork and Renato Mangano, European Cross-border Insolvency Law (Oxford University Press 2016), 8.01 et seq.

[1144] For European corporate law developments, see Peter Hommelhoff, 'Die Unternehmensgruppe im Europäischen Binnenmarkt', in Mathias Habersack, Karl Huber & Gerald Spindler, *Festschrift für Eberhard Stilz zum 65. Geburtstag* (München : C.H. Beck 2014), 287 et seq.; Marc-Philippe Weller, Johanna Bauer, 'Europäisches Konzernrecht: vom Gläubigerschutz zur Konzernleitungsbefugnis via Societas Unius Personae', ZEuP 2015, 6 et seq.; Christoph Teichman, 'Corporate Groups within the Legal Framework of the European Union: The Group-Related Aspects of the SUP Proposal and the EU Freedom of Establishment', ECFR 2/2015, p. 202 et seq. It is noted that 'insolvency' is hardly touched upon by these authors.

704. In some countries, however, sparsely in legislation or practice there is some room for economic reality. In Belgium cases involving two or more related companies are handled on an ad hoc basis by the courts, by appointing the same supervisory judge and bankruptcy trustee or court representative. Also the Swedish Enforcement Authority has stated that if it is appropriate, one administrator shall be appointed for all companies of an insolvent group. In some Member States there are some provisions for or jurisprudence about the reorganisation of groups of companies. In the United Kingdom for example, it is possible to devise schemes of arrangement or company voluntary arrangements for a group of companies.[1145] Hungarian law provides for the submission of contracts concerning recognized or de facto groups of companies as an annex to the request for the commencement of a reorganization procedure by the debtor, and the separate registration of claims against the debtor by companies belonging to the same group.[1146] During the preparation of a reorganisation settlement, the debtor may request the assistance of other members of the company group.[1147] In Italy, it is possible for the *commissario* to submit to the creditors a sole settlement proposal for all companies pertaining of a large group (having together with the subsidiaries, more than 500 employees and debts amounting to more than Euro 300,000,000). The assets and liabilities of each company, however, will remain separate.

705. The only Member States currently providing for special provisions for insolvent groups of companies are France, Spain and Romania[1148], while in Germany, in 2013, a legislative proposal has been issued.

706. In France, judicial liquidation proceedings are governed by the French Code de commerce (Commercial Code).[1149] With regard to the court having jurisdiction to open such proceedings, Article L. 641-1 of that Code refers to Article L. 621-2 of the same Code which, in the version resulting from Law No 2005-845 of 26 July 2005 on the protection of undertakings provides: 'The competent court will be the *Tribunal de commerce* (Commercial Court) if the debtor is a trader or he is registered with the craftsmen's register. The *Tribunal de grande instance* (High Court) shall be competent in other cases. One or more other persons may be joined to opened proceedings where their property is intermixed with that of the debtor or where the legal entity is a sham. The court that has opened the initial proceedings shall remain competent for this purpose.'[1150]

[1145] [2009] EWHC 2114 (Ch.); *Re Olympia & York Canary Wharf Holdings Ltd & Ors.* [1993] BCC 866.
[1146] Cstv. 8(2)(e), Cstv. 12(2)(bc).
[1147] Cstv. 17(3).
[1148] It has been communicated that a few countries have adopted legislation regarding the treatment of enterprise groups in insolvency based on the UNCITRAL Legislative Guide on Insolvency Law (discussed in para. 1.1) or have applied certain of its recommendations, one of them being Romania (eurofenix Spring 2015, 44), the others Argentina (INSOL World, Fourth Quarter 2011, 18 et seq) and Colombia (INSOL World, Second Quarter 2014, p. 32 et seq),
[1149] Articles L. p. 640-1 et seq.
[1150] The provision has been scrutinised for its international effect prominently by the Court of Justice of the EU, see CJEU 15 December 2011, C-191/10 (*Rastelli Davide e C. Snc v Jean-Charles Hidoux, liquidator of Médiasucre International*); ECLI:EU:C:2011:838. The core question in this case is whether main insolvency proceedings opened in France, based the cited national (French) rule of 'consolidation', can include a debtor/company with has its registered office in another Member State (in the case at hand Italy), when both companies' assets are intermingled. The CJEU observes that although the single procedure is justified by the finding that the two debtors form a de facto unit because their property is intermixed, this finding has no bearing on the legal

707. In Spain, debtors belonging to the same company group can request the joint commencement of insolvency proceedings. Also a creditor holding claims against companies belonging to the same company group may request the joint commencement of insolvency proceedings of those companies. The court that has jurisdiction to open the insolvency proceedings of the parent company or (in case the parent company's insolvency proceedings are not requested) the company with the highest amount of liabilities, will have jurisdiction to commence insolvency proceedings on all the remaining companies of the group.[1151]

708. In 2013, the German legislator proposed the Act to Facilitate Group Insolvencies (*Gesetz zur Erleichterung der Bewältigung von Konzerninsolvenzen*).[1152] This Act aims to amend the existing Insolvency Code to be better tailored for the specific needs of group insolvencies and to introduce a new procedure to coordinate separate insolvencies within the same group. In this new Act, the *Rechtsträgerprinzip* is still leading, meaning that each separate legal entity is subject to its own insolvency proceeding. A substantive consolidation within a group of companies is thus rejected by the German legislator. The Act does provide for the coordination and the cooperation between the individual insolvency proceedings within a company group. It is based on the following four pillars:

1 *Special jurisdiction for group insolvencies* (par. 3a to 3d InsO)

This provision allows for a concentration of all insolvency proceedings within the same group at one court. The priority rule is applied: the court at which the first insolvency proceeding of a member of the group is filed, has special jurisdiction. However, there are two prerequisites for this special jurisdiction. Firstly, it must be in the common interest of all creditors. Secondly, the first filing group member must

personality of the two debtors. The CJEU has consistently held that in the system established by the EIR (2000) for determining the competence of the Member States, which is based on the debtor's COMI, '… each debtor constituting a distinct legal entity is subject to its own court jurisdiction and draws the logical consequence that a decision producing, '… with regard to a legal entity, the same effects as the decision to open main insolvency proceedings can only be taken by the courts of the Member State that would have jurisdiction to open such proceedings'. The CJEU limits the meaning of the French provision: '… the possibility that a court designated under that provision as having jurisdiction, with regard to a debtor, to join another legal entity to insolvency proceedings on the sole ground that their property has been intermixed, without considering where the centre of that entity's main interests is situated, would constitute a circumvention of the system established by the Regulation. This would result, inter alia, in a risk of conflicting claims to jurisdiction between courts of different Member States, which the Regulation specifically intended to prevent in order to ensure uniform treatment of insolvency proceedings within the European Union.' The mere finding that the property of those companies has been intermixed is not sufficient to establish that the centre of the main interests of the Italian company concerned by the action is also situated in that other Member State. In order to reverse the presumption that this centre is the place of the registered office, it is necessary that an overall assessment of all the relevant factors allows it to be established, in a manner ascertainable by third parties, that the actual centre of management and supervision of the company concerned by the joinder action is situated in the Member State where the initial insolvency proceedings were opened, thus the CJEU.

[1151] Article 25 LC.

[1152] See Entwurf eines Gesetzes zur Erleichterung der Bewältigung von Konzerninsolvenzen, Deutscher Bundestag Drucksache 18/407 of 30 January 2014. It is commenly known that the German proposal forms the conceptual approach underlying Chapter V of the EIR (2015). See Volker Böhm, Christoph von Wilcken, *Einführung eines Konzerninsolvenzrechts,* in (Insolvenzrecht und Unternehmenssanierung, Schultze & Braun Jahrbuch 2016), 16 et seq. The German Bundestag voted the bill to facilitate the handling of domestic group insolvencies (*Gesetzes zur Erleichterung der Bewältigung vor Konzerninsolvenzen*) in march 2017. It will enter into force 21 April 2018.

not have a mere marginal importance within the group with regard to its balance sheet, revenue numbers and its number of employees.

2 *Appointment of a single administrator* (par. 56b InsO)
This provision lays down an examination and consultation obligation on the involved courts. It is the task of the involved courts in a group insolvency to decide whether it would be in the common interest of the creditors to appoint a single administrator for some or all separate insolvency proceedings within the same group.

3 *Duty of cooperation* (par. 269a et seq. InsO)
The appointed administrators are obliged to inform each other and to work together. In particular, the administrator of a company group member must give all information relevant to the insolvency proceedings of the other group members to the administrator of such a different proceeding. Besides, administrators have to participate actively in the coordination of liquidation or restructuring strategies and have to solve disputes within the group. These obligations of cooperation are also applicable to courts.

4 *Coordination procedure* (par. 296d et seq. InsO)
A coordination procedure can be ordered by the court that has special jurisdiction for all group-related insolvency proceedings. It can be lodged by the insolvency debtor, an administrator and a creditors committee. The foundation of the coordination procedure is the appointment of a coordination administrator. He can suggest a coordination plan. This plan must be approved by the court and by the group creditors committee (if formed). The coordination plan can provide for all measures which are relevant to and necessary for a conflict-free coordination of the individual insolvency proceedings within the company group.

9.3.2. Procedural consolidation of domestic insolvency proceedings concerning companies in a company group

709. In most Member States, e.g. Austria, Belgium, the United Kingdom, Germany, Greece, Hungary, Italy, Latvia, the Netherlands, Poland and Sweden, insolvency law does not allow for procedural consolidation of domestic insolvency proceedings concerning companies in a company group. In some of these Member States however, this lack of basis in legislation is solved by legal practice. In Belgium, courts tend to streamline insolvency proceedings opened in respect of company groups. Also in Germany, it is not prohibited to appoint a single administrator for members of a company group. The same goes for the Netherlands, where some courts appoint the same liquidator for different companies within a company group when they have been declared bankrupt. In Greece, if both a parent company and a subsidiary file bankruptcy before the same court, they could request to appoint a single liquidator. However, to the knowledge of the Greek reporters, that has never actually happened. According to Italian case law, it is possible to file an application in relation to a group of companies. Although assets and liabilities of each company shall remain separate, the plan filed with the application should be aimed at ensuring the continuity of the business of the group as a whole.[1153] The competent courts tend to appoint the same deputy judge

[1153] Tribunale di Palermo, Sez. IV Civile e Fallimentare, 4 giugno 2014.

and *commissaria giudiziale,* in order to ensure that the procedures are consistently carried out. In the United Kingdom, it is possible and common for the company or holder of a qualifying floating charge to appoint the same administrator in all separate administrations of a company group. Moreover, the proceedings are concentrated in the High Court, which has comprehensive jurisdiction.

710. However, French and Spanish laws do provide for procedural consolidation of domestic insolvency proceedings concerning companies in a company group. In France, the court that opened an insolvency proceeding on the most significant company of a company group may appoint an administrator and a creditors' representative common to all proceedings in addition to the insolvency practitioners appointed in each single proceeding.[1154] As already mentioned in the previous paragraph, in Spain procedural consolidation can be ordered at the commencement of the insolvency proceedings of members of a company group. The insolvency officer of each group member may request the court to procedurally consolidate all the insolvency proceedings.[1155] This request can also be lodged by any creditor.[1156] The court dealing with the insolvency proceedings of the company with the highest amount of liabilities, or of the parent company, or of the company that has been first declared insolvent, will have jurisdiction to consolidate the insolvency proceedings of the remaining companies of the group.[1157]

9.3.3. Substantive consolidation of domestic insolvency proceedings across a company group into a single procedure

711. Again, in most Member States, e.g. Austria, Belgium, the United Kingdom, Germany, Greece, Hungary, Italy, Latvia, the Netherlands, Poland and Sweden, insolvency law does not allow for substantive consolidation of domestic insolvency proceedings across a company group into a single procedure with one unified estate. In some of these Member States, this lack of specific provisions is solved by legal practice. In the United Kingdom a group of companies may, under certain circumstances, be treated as one single company.[1158] Substantive consolidation of assets and liabilities of different members of a group of companies may only be considered where their affairs '… are so hopelessly intertwined that a pooling of their assets, with a distribution enabling the like dividend to be paid to both companies' creditors, is the only sensible way to proceed' and where it 'would make no sense to spend vast sums of money and much time trying to disentangle and unravel'.[1159] Similarly, in the Netherlands substantive consolidation is permitted in very specific cases whereby all assets and liabilities of the various legal entities have been commingled in a sense that they cannot easily be untangled without severe effort and costs. Spanish law does provide for a corresponding provision: substantive consolidation of assets and liabilities is permitted when the assets and liabilities are so intermingled that it is not possible to determine the ownership of the assets and liabilities without incurring in unjustified costs or

[1154] Article L.622-8 Commercial Code.
[1155] Article 25 bis. 1 LC.
[1156] Article 25 bis. 2 LC.
[1157] Article 25 bis. 3 LC.
[1158] [1976] 1 WLR 852 *DHN Food Distributors Ltd. v. Tower Hamlets London Borough Council.*
[1159] *Re Bank of Credit and Commerce International SA (No. 3)* [1993] WL 96496, per Dilllon LJ, quoting and affirming the decision of Sir Donald Nicholls V-C at first instance.

delay in the preparation of the report of the insolvency officer.[1160] In France, a substantive consolidation of insolvency proceedings may be ordered by the court in case of commingling of estates and in case of a fictitious corporate entity. Commingling of estates means that it is impossible to distinguish the assets and liabilities of a group member from another and/or the existence of abnormal financial flows between two or more group members. Fictitious corporate entity entails that the company is found to be fiction, without an independent management running the business.[1161]

9.4. European Insolvency Regulation (2015)

712. As indicated, the EIR (2015), entering into legal force on 26 June 2017[1162], introduces a specific chapter to group insolvencies. In general, it has been found that the EIR (2000) has functioned well overall but that it would be desirable to improve the application of certain of its provisions in order to enhance the effective administration of cross-border insolvency proceedings.[1163] One of the EIR (2000)'s shortcomings is that it does not deal with the insolvency of groups of companies.[1164]

713. The absence of appropriate rules on a European level about insolvency of groups of companies led this issue to be dealt with by case law on both national and supranational level and market practice.[1165] One main issue was how to ascertain the COMI in case of insolvency of a group of companies, when the different members of the group are located in different jurisdictions. The EIR (2000) treated – as a matter of course – each company individually and separately focussing on the COMI of each of those companies instead of addressing issues of group insolvency as a whole.[1166]

714. The EIR (2015) defines a group of companies as 'a parent undertaking and all its subsidiary undertakings'.[1167] The EIR (2015) tries to create a system of efficient administration of insolvency proceedings relating to different companies which form a part of a group of companies by, most importantly, leaving untouched the central principle of respect for separate legal personality of each group member. The solution is: '… cooperation, cooperation, cooperation'. Recital 52 provides: 'Where insolvency proceedings

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[1160] Article 25 ter. 2 LC.
[1161] Article L. 621-2 Commercial Code.
[1162] Article 92 EIR (2015).
[1163] Burckhart Hess, Paul Oberhammer and Thomas Pfeiffer, European Insolvency Law, Heidelberg-Luxembourg-Vienna Report (C.H. Beck – Hart – Nomos 2014), available at: http://ec.europa.eu/justice/civil/files/evaluation_insolvency_en.pdf.
[1164] See also: Bob Wessels, 'EU Insolvency Regulation v. Recast: Recitals compared', 2015, http://bobwessels.nl/2015/08/2015-08-doc1-eu-insolvency-regulation-v-recast-recitals-compared/.
[1165] I. Chaika, 'Insolvency of Group of Companies through the prism of the Recast Insolvency Regulation (EU) 2015/848', Institute of International and European Insolvency Law, University of Cologne, Germany. It goes beyond the scope of this report to further elaborate on ten (!) solutions presented or applied by courts and scholars to arrange for insolvency proceedings of groups of companies, see extensively Bob Wessels, *International Insolvency Law Part I. Global Perspectives on Cross-Border Insolvency Law* (4th ed., Deventer: Kluwer 2015), para. 10425f et seq.
[1166] Recital 13 and article 3 EIR (2015).
[1167] Article 2(13) EIR (2015). As explained in the opening paragraph, the EIR (2015) aligns with definitions from the Directive 2013/34/EU on annual financial statements.

have been opened for several companies of the same group, there should be proper cooperation between the actors involved in those proceedings. The various insolvency practitioners and the courts involved should therefore be under a similar obligation to cooperate and communicate with each other as those involved in main and secondary insolvency proceedings relating to the same debtor. Cooperation between the insolvency practitioners should not run counter to the interests of the creditors in each of the proceedings, and such cooperation should be aimed at finding a solution that would leverage synergies across the group.'[1168] EIR (2015) introduces procedural rules on the administration of the insolvency proceedings of members of a group of companies. First of all, it provides for the obligation for the actors involved in insolvency proceedings (insolvency practitioners and courts) to communicate and cooperate. Secondly, the EIR (2015) provides for rules on the coordination of insolvency proceedings. These rules on cooperation, communication and coordination in the framework of the insolvency of members of a group of companies only apply to the extent that proceedings relating to different members of the same group of companies have been opened in more than one Member State.[1169]

9.4.1. Cooperation and communication (Articles 56-60 EIR (2015))

715. According to Article 56(1) EIR (2015) insolvency practitioners appointed in insolvency proceedings relating to two or more members of a group of companies have to cooperate with each other to the extent that such cooperation is appropriate to facilitate the effective administration of those proceedings, is not incompatible with the rules applicable to such proceedings and does not entail any conflict of interest. That cooperation may take any form, including the conclusion of agreements or protocols. The insolvency practitioners shall (i) as soon as possible communicate to each other any information which may be relevant to other proceedings (provided that appropriate arrangements are made to protect confidential information), (ii) consider whether possibilities exist for coordinating the administration and supervision of the affairs of the group members which are subject to insolvency proceedings, and if so, coordinate such administration and supervision, and (iii) consider whether possibilities exist for restructuring group members which are subject to insolvency proceedings and, if so, coordinate with regard to the proposal and negotiation of a coordinated restructuring plan.

716. Article 57 EIR (2015) introduces a similar obligation of cooperation and communication for courts that have opened insolvency proceedings relating to two or more members of a group of companies. The courts may, where appropriate, appoint an independent person or body to act on its instructions, provided that this is not incompatible with the rules applicable to them. The cooperation between the courts may, in particular, concern: (i) coordination in the appointment of insolvency practitioners, (ii) communication of information by any means considered appropriate by the court, (iii) coordination of the administration and supervision of the assets and affairs of the members of the group, (iv)

[1168] The 'similar' obligation to cooperate and communicate is laid down in Article 41 EIR (2015).
[1169] Recital 62 EIR (2015). For a detailed commentary on the related articles, see for single debtor cases Jessica Schmidt, in Reinhard Bork and Kristin van Zwieten (eds.), *Commentary on the European Insolvency Regulation* (Oxford University Press 2016).

coordination of the conduct of hearings, and (v) coordination in the approval of protocols where necessary.
According to Article 58 EIR (2015) lays down a similar obligation of cooperation and communication exists between insolvency practitioners and courts.

717. Article 60 EIR (2015) illustrates the powers of the insolvency practitioner in proceedings concerning members of a group of companies. He may be heard in any of the proceedings opened in respect of any other member of the same group. Furthermore, he may request a stay of any measure related to the realization of assets in the proceedings opened with respect to any other members of the same group, provided that: (i) a restructuring plan for all or some group members has been proposed and presents a reasonable chance of success, (ii) such a stay is necessary in order to ensure the proper implementation of the restructuring plan, (iii) the restructuring plan would be to the benefit of the creditors in the proceedings for which the stay is requested, and (iv) neither the insolvency proceedings in which the insolvency practitioner has been appointed nor the proceedings in respect of which the stay is requested are subject to coordination. Lastly, the insolvency practitioner may apply for the opening of group coordination proceedings.

9.4.2. Coordination (Articles 61-77 EIR (2015))

718. According to Article 61 EIR (2015), group coordination proceedings may be requested over insolvency proceedings of members of the group by an insolvency practitioner appointed in insolvency proceedings in relation to a member of a group. Those group coordination proceedings can be requested before any court having jurisdiction over the insolvency proceedings of a member of the group. With regard to court jurisdiction, the priority rule is applied by Article 62 EIR (2015): where the opening of group coordination proceedings is requested before courts of different Member States, any court other than the court first seized shall decline jurisdiction in favour of that court. Article 66 EIR (2015) formulates an exception to the priority rule. Where at least two-thirds of all insolvency practitioners appointed in insolvency proceedings of the members of the group have agreed that a court of another Member State having jurisdiction is the most appropriate court for the opening of group coordination proceedings, that court shall have exclusive jurisdiction.

719. The court seized of a request to open group coordination proceedings shall give notice as soon as possible of the request and of the proposed coordinator to the insolvency practitioners appointed in relation to the group members, if it is satisfied that the following requirements are met: (i) the opening of such proceedings is appropriate to facilitate the effective administration of the insolvency proceedings relating to the different group members, (ii) no creditor of any group member expected to participate in the proceedings is likely to be financially disadvantaged by the inclusion of that member in such proceedings, and (iii) the proposed coordinator fulfils the requirements laid down in Article 71 EIR (2015).

720. Insolvency practitioners have the right to object to the inclusion within group coordination proceedings of the insolvency proceedings in respect of which he/she has been appointed, or to the person proposed as a coordinator.[1170] Where an insolvency practitioner has objected on the first ground, the insolvency proceedings shall not be included in the

[1170] Article 64 EIR (2015).

group coordination proceedings.[1171] Where an insolvency practitioner has objected on the second ground, the court may refrain from appointing the proposed coordinator and invite the objecting insolvency practitioner to submit a new request.[1172]

721. After the period in which insolvency practitioners are able to lodge objections (30 days), the court may open group coordination proceedings if the conditions set out in Article 63 (1) 2015 are met. In such a case the court shall appoint a coordinator, decide on the outline of the coordination, and decide on the estimation of costs and the share to be paid by the group members. The opening of the group coordination proceedings shall be brought to notice of the participating insolvency practitioner and of the coordinator.[1173] According to Article 69 EIR (2015) any insolvency practitioner may request the inclusion of the proceedings in respect of which it has been appointed, where there has been an objection to the inclusion of the insolvency proceedings within the group coordination proceeding, and where insolvency proceedings with respect to a member of the group have been opened after the court has opened group coordination proceedings.

722. According to Article 71 EIR (2015), the coordinator of group coordination proceedings shall be a person eligible under national law to act as an insolvency practitioner, but not one of the insolvency practitioners appointed to act in respect of any of the group members, and shall have no conflicts of interest. Article 72 EIR (2015) lays down the tasks and rights of the coordinator. He shall identify and outline recommendations for the coordinated conduct of the insolvency proceedings and propose a group coordination plan. According to Article 70 EIR (2015), an insolvency practitioner is not obliged to follow in whole or part the coordinator's recommendations or the group coordination plan. In case the insolvency practitioner decides to not follow, he shall give reasons for not doing so to the persons or bodies that it is to report to under national law, and to the coordinator (comply-or-explain rule). Article 72 (4) EIR (2015) stresses that the coordinator shall perform his/her duties impartially and with due care. Article 74 EIR (2015) introduces an obligation of cooperation and communication between insolvency practitioners and the coordinator.

723. According to Article 75 EIR (2015), the court shall revoke the appointment of the coordinator of its own motion or at the request of the insolvency practitioner where the coordinator acts to the detriment of the creditors of a participating group member, or the coordinator fails to comply with his/her obligations.

724. After having briefly described the system under the EIR (2015), it should be mentioned that until now in the academic literature these provisions have had a mixed reception.[1174]

[1171] Article 65 EIR (2015).
[1172] Article 67 EIR (2015).
[1173] Article 68 EIR (2015).
[1174] See I. Mevorach, 'The new proposed regime for EU corporate groups in insolvency: a critical note', 6 Corporate Rescue and Insolvency 2013, p. 89 et seq.; S. Madaus, 'Insolvency proceedings for corporate groups under the new Insolvency Regulation', 6 International Insolvency Law Review 2015, p. 235 et seq.; Maximilian J. Eble, 'Auf dem Weg zu einem europäischen Konzerninsolvenzrecht – Die 'Unternehmensgruppe' in der EuInsVo 2017', NZI 4/2016, 115 et seq; Alessandro Merlini, 'Reorganisation and Liquidation of Groups of Companies: Creditors' Protection vs. Going Concern Maximisation, the European Dilemma, or simply a Misunderstanding in the light of the new EU Insolvency Regulation No. 2015/848', 7 International Insolvency Law Review 2016, p.

9.5. Significant international tendencies

725. Over the last years, several international initiatives are taken in the field of the phenomenon corporate group issues in insolvency.

9.5.1. The UNCITRAL Legislative Guide on Insolvency Law

726. The UNCITRAL Legislative Guide on Insolvency Law provides key objectives and principles that should be reflected in national insolvency laws. The Legislative Guide is divided into four parts. In 2010 UNCITRAL added the Third Part about the treatment of groups of companies in insolvency (UNCITRAL Legislative Guide (2010)). In this part of the UNCITRAL Legislative Guide it is suggested to facilitate the global treatment of enterprise groups in insolvency by ensuring that existing principles for cross-border cooperation (Articles 25 – 27 Model Law) apply to enterprise group insolvencies. The aim is to '… facilitate commercial predictability and increase certainty for trade and commerce, as well as fair and efficient administration of proceedings that protects the interests of the parties, maximizes the value of the assets of group members to preserve employment and minimizes costs.'[1175] It is furthermore recognized that there will be enterprise groups where separate insolvency proceedings may be a feasible option because there is a low degree of integration in the group and group members are relatively independent of each other, but '… for many groups cooperation may be the only way to reduce the risk of piecemeal insolvency proceedings that have the potential to destroy going concern value and lead to asset ring-fencing, as well as asset shifting or forum shopping by debtors'.[1176]

727. The overall goal of this Part is to permit, in both domestic and cross-border contexts, treatment of the insolvency proceedings of one or more company group members within the context of the company group to address the issues particular to insolvency proceedings involving those groups and to achieve a better, more effective result for the company group as a whole and its creditors.[1177] Part Three consists of 55 recommendations. We list them as follows:

1. Joint application for commencement of insolvency proceedings (recommendations 199-201);
2. Procedural coordination (recommendations 202-210);
3. Post-commencement finance (recommendations 211-216);
4. Avoidable actions (recommendations 217-218);
5. Substantive consolidation (recommendations 219-231);
6. Appointment of a single or the same insolvency representative (recommendations 232-236 and 251-252);
7. Coordinated reorganization plans (recommendations 237-238);
8. Access to courts and recognition of foreign proceedings (recommendation 239);
9. Cooperation between courts (recommendations 240-245);

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119 et seq.; Reinhard Bork and Renato Mangano, *European Cross-border Insolvency Law* (Oxford University Press 2016),p. 8.30 et seq.

1175 UNCITRAL Legislative Guide (2010), 'B. Promoting cross-border cooperation in enterprise group insolvencies', at p. 7.

1176 Ibid.

1177 UNCITRAL Legislative Guide (2010), to be downloaded from http://www.uncitral.org.

10. Cooperation between the insolvency representatives and the foreign courts (recommendations 246-250); and

11 Cross-border insolvency agreements (recommendations 253-254).

9.5.2. UNCITRAL Key principles of regime to address insolvency in the context of enterprise groups

728. Since 2015 UNCITRAL is drafting a legislative proposal with regard to group insolvencies. It particularly builds on the recommendations and has taken into account the rules adopted for group insolvencies in the EIR (2015).

729. In December 2015 UNITRAL published a set of 'Key principles of regime to address insolvency in the context of enterprise groups'.[1178] Below follows the text:

Principle 1

If required or requested to address the insolvency of an enterprise group member, insolvency proceedings may be commenced. When proceedings are not required or requested, there is no obligation to commence such proceedings.

Principle 2

When it is proposed that an enterprise group solution be developed for some or all of the members of an enterprise group, that solution will require coordination as between group members and may be developed through a coordinating proceeding.

Principle 3

Adopting the approach of recommendation 250, enterprise group members might designate one of the insolvency proceedings commenced (or to be commenced) with respect to group members participating in the group solution to function as the coordinating proceeding, the role of which would be procedural, rather than substantive. A proviso might be that the coordinating proceeding should be a proceeding taking place in a State that is the COMI of at least one of the group members that is a necessary and integral part of the enterprise group solution.

Principle 4

1. The court located in the COMI (the COMI court) of an enterprise group member participating in a group solution can authorize the insolvency representative appointed in insolvency proceedings taking place in the COMI to seek: (i) to participate and be heard in a coordinating proceeding taking place in another jurisdiction, and (ii) recognition by the coordinating court of the proceeding in the COMI jurisdiction; and
2. The coordinating court can receive such a request for recognition.

Principle 5

Participation in the coordination process would be voluntary for those group members whose COMI is located in a jurisdiction different to that of the coordinating proceeding. For those group members whose COMI is located in the same jurisdiction as the coordinating proceeding, the recommendations of part three of the Legislative Guide on Insolvency Law with respect to joint application and procedural coordination could apply. Solvent members of the enterprise group may participate in a coordination process without such participation implying a submission to the

[1178] See UNCITRAL Working Groep V (Insolvency Law), 48th session, 14-18 December 2015, A/CN.9/WG.V/WP.133

jurisdiction of a domestic or foreign insolvency court or to the applicability of domestic or foreign insolvency laws.

Principle 6

Creditors and stakeholders of each enterprise group member participating in the group solution would vote in their own jurisdiction on the treatment they are to receive under the group reorganization plan according to the applicable domestic law.

Principle 7

Following approval of the group reorganization plan by relevant creditors and stakeholders, each COMI court would have jurisdiction to deal with the group reorganization plan in accordance with domestic law.

Principle 8

The insolvency representative appointed in the proceeding designated as the coordinating proceeding should have a right of access to the proceedings in each COMI court to be heard on issues related to implementation of the group reorganization plan.

9.5.3. International Insolvency Institute - Guidelines for Coordination of Multinational Enterprise Groups (2013)

729. The International Insolvency Institute ('III') aims to promote and advance international insolvency law, and in particular to support better cooperation in cross-border insolvency cases. III undertakes and supports research projects. Cooperation with multiple enterprise groups has drawn the specific interest of III and was studied by its Committee on International Jurisdiction and Cooperation. The Committee, chaired by Hon. Ralph Maybe, has drafted 'Guidelines for Coordination of Multinational Enterprise Groups' ('Guidelines'). They were concluded in 2013. In general emphasis has been on liquidating rather than restructuring financially overcommitted businesses, however, these Guidelines try to address this issue and incorporate both.[1179] Although the Guidelines aim to coordinate insolvency of situations where a multiple enterprise group covers multiple countries, it is interesting to note that 'cooperation' is at the very heart of the Guidelines. More specifically, the Guidelines relate to enterprise groups with '… operations, assets and employees located in more than one country, which has unified corporate governance, either through common or interlocking shareholding or by contract.'

730. The Guidelines consider seven topics, whereof – according to the drafting Committee – Guidelines 1-6 should be well applicable in most jurisdictions and Guidelines 7-11 should suit many jurisdictions. Finally, Guidelines 12-22 may need statutory amendments in various jurisdictions.

Guidelines 1 and 2 provide how an insolvency representative should act with a debtor that is an affiliate of a multinational upon the opening of insolvency proceedings. The other affiliates should be allowed to be heard on their interest in the insolvent affiliate (Guideline 3). Guideline 4 provides that the centre of main interests ('COMI') should be determined, in particular for countries that have adopted the UNCITRAL Model Law on Cross-Border

[1179] For a short description, see Bob Wessels and Gert-Jan Boon, *Cross-Border Insolvency Law, International Instruments and Commentary* (2nd Ed., Alphen aan den Rijn: Kluwer Law International 2015), p. 63 et seq. The Guidelines discussed appear as Annex 22 in this book.

Insolvency, should be determined only after verifying the group's structure and the affiliate's COMI. Court-to-Court Communication Guidelines should be applied, also insolvency representatives and creditors should support communications (Guidelines 5 and 6).

731. Guidelines 7 and 8 promote the use of protocols (or insolvency agreements) by debtors and/or insolvency representatives. Guideline 9 provides that the court may stay its decision on COMI of an affiliate when the COMI of an enterprise remains undecided. With regard to governance of proceedings, preferably one insolvency representative should be appointed in all insolvency cases related to the enterprise group (Guidelines 10). Furthermore, one officeholder should be appointed per category, where officeholder in this situation relates to legal counsel, accountants, and various (bodies of) representatives (Guideline 11).
Finally, a set of 'aspirational' Guidelines concern the localisation of the Group Center and the consequence thereof. The COMI of an enterprise be the '… coordination center for the enterprise …' (Guideline 12). Proceedings relating to affiliates should as much as possible be opened in the COMI of the enterprise (even though their respective COMI might be elsewhere). Protocols can be used for coordination purposes (Guidelines 13-15). There should preferably be administrative coordination of all proceedings (Guideline 16). A stay in the Group Center should have effect on all affiliates (Guideline 17). Secondary proceedings may only be filed for affiliates outside the Group Center (Guideline 18). Courts should hear insolvency representatives and all other interested parties (in accordance with Guideline 2) where requests have been made to open Enterprise Group Proceedings with respect to multiple affiliates of an enterprise group (Guideline 19). Court-to-court cooperation should take place to, whenever necessary, provide for localising of assets or in the reorganisation or liquidation of the enterprise group.

732. The Guidelines foresee that difficulties may arise in achieving full coverage of the entire group with main and secondary proceedings. In that cases parties (including courts, insolvency representatives and creditors) should aim to achieve results that are approximating as much as possible these Guidelines (Guideline 21). Finally, insolvency representatives are obliged to inform the Group Center Court of relevant changes on an affiliate's status or proceedings. This Guideline provides also for modification and termination of the Group Center designation.

9.5.4. The World Bank Principles (2016)

733. Next to the UNCITRAL Legislative Guide, the World Bank Principles (2016) contain multiple principles on dealing with company group issues. These Principles are in line with the Recommendations of UNCITRAL. According to the World Bank, the national systems should specify that the administration of insolvency proceedings with respect to two or more company group members may be coordinated for procedural purposes. The scope and extent of the procedural coordination should be specified by the court.[1180] Furthermore, the national systems should permit:

- a company group member subject to insolvency proceedings to provide or facilitate post-commencement finance or other kind of financial assistance to other members in the group which are also subject to insolvency proceedings;[1181]

[1180] World Bank Principle (2016), Principle C16.1.
[1181] World Bank Principle (2016), Principle C16.2.

- the court to consider whether to set aside a transaction that took place among company group members, or between any of them and a related person, to take into account the specific circumstances of the transaction;[1182]
- a single or the same insolvency representative to be appointed with respect to two or more company group members, including provisions addressing situations involving conflicts of interest;[1183]
- where there are different insolvency representatives for different company group members, the insolvency representatives to communicate directly and to cooperate to the maximum extent possible;[1184]
- coordinated reorganization plans to be proposed in insolvency proceedings with respect to two or more company group members;[1185] and
- company group members not subject to insolvency proceedings to voluntarily participate in a reorganization plan of other group members subject to insolvency proceedings.[1186]

734. With regard to substantive consolidation, the World Bank starts with stating that the insolvency system should respect the separate legal identity of each of the company group members. In case substantive consolidation is contemplated, it should be restricted to circumstances where:
- assets or liabilities of the company group members are intermingled to such an extent that the ownership of assets and responsibility for liabilities cannot be identified without disproportionate expense or delay; or
- the company group members are engaged in a fraudulent scheme or activity with no legitimate business purpose.

735. The court should be able to exclude specific claims and assets form an order of consolidation. In case of substantive consolidation, the system should contemplate an adequate treatment of secured transactions, priorities, creditor meetings, and avoidance actions. A substantive consolidation order would cause the assets and liabilities of the consolidated companies to be treated as if they were part of a single estate, extinguish debts and claims as amongst the relevant enterprises, and cause claims against the relevant companies to be treated if they were against a single insolvency estate.[1187]

736. In the context of the insolvency of company group members, the system should provide foreign representatives and creditors with access to the court, and for the recognition of foreign insolvency proceedings, if necessary.[1188] The system should allow the national court to cooperate to the maximum possible extent with foreign courts or foreign representatives, either directly or through the local insolvency representative. The system should permit the national court to communicate directly with, or to request information or assistance directly from, foreign courts or representatives.[1189] The system should also allow insolvency

[1182] World Bank Principle (2016), Principle C16.4.
[1183] World Bank Principle (2016), Principle C16.5.
[1184] World Bank Principle (2016), Principle C16.5.
[1185] World Bank Principle (2016), Principle C16.6.
[1186] World Bank Principle (2016), Principle C16.6.
[1187] World Bank Principle (2016), Principle C16.3.
[1188] World Bank Principle (2016), Principle C17.1.
[1189] World Bank Principle (2016), Principle C17.2.

representatives appointed to administer proceedings with respect to a company group member to communicate directly and to cooperate to the maximum extent possible with foreign courts and with foreign insolvency representatives in order to facilitate coordination of the proceedings.[1190] In specific circumstances, it should be allowed to appoint a single or the same insolvency representative for company group members in different States. In such cases, the system should include measures addressing situations involving conflicts of interest.[1191] Insolvency representatives and other parties of interest should be permitted to enter into cross-border insolvency agreements involving two or more company group members in different States in order to facilitate coordination of the proceedings. The system should allow the courts to approve or implement such agreements.[1192]

737. The EIR (2015) only introduces procedural rules on the administration of the insolvency proceedings of members of a group of companies, such as rules on communication and cooperation between the insolvency practitioners and courts, and rules on coordination of insolvency proceedings. UNCITRAL and the World Bank, however, do recommend some level of substantive consolidation with respect to group insolvency.

9.6. Impetus to reporters' recommendations

738. The Reporters limit themselves – in the light of the chosen methodology, see para. 3.1 in the Introduction – to recommendations closely related to 'insolvency'.

739. The national legislators of the Member States have not been very active in enacting provisions regarding group insolvency. According to the Inventory Reports, only French and Spanish laws do provide for rules on procedural and substantive consolidation of domestic insolvency proceedings concerning companies in a company group. German law provides for coordination and procedural consolidation options. In some Member States, this lack of provisions is solved by legal practice. In other Member States, it does not seem possible at all to consolidate (procedural nor substantial) domestic insolvency proceedings concerning companies in a company group.

740. At European level, the EIR (2015) provides for some procedural rules on the administration of the insolvency proceedings of members of a group of companies. The EIR (2015) does not, however, cover substantive consolidation matters. Moreover, coordination of insolvency proceedings is voluntary according to the wording of Recital 56: the insolvency practitioners involved should be able to object to their participation in the proceedings within a specified time period. Furthermore, during a group coordination procedure, insolvency practitioners are not obliged to follow in whole or part the coordinator's recommendations or the group coordination plan. It is questionable whether these new provisions do actually offer an effective solution to group insolvencies.

741. The EIR (2015), however, seems to include some leeway for courts in the Member States. Recital 53 provides: 'The introduction of rules on the insolvency proceedings of

[1190] World Bank Principle (2016), Principle C17.3.
[1191] World Bank Principle (2016), Principle C17.4.
[1192] World Bank Principle (2016), Principle C17.5.

groups of companies should not limit the possibility for a court to open insolvency proceedings for several companies belonging to the same group in a single jurisdiction if the court finds that the centre of main interests of those companies is located in a single Member State.' This reminder (suggestion?) of the European Commission could be seen as a response to the desirability of introducing a 'One Group – One COMI' principle. The Recital can, however, also be traced back to CJEU's case law.[1193] Recital 53 continues: '… In such cases, the court should also be able to appoint, if appropriate, the same insolvency practitioner in all proceedings concerned, provided that this is not incompatible with the rules applicable to them.' This would mean that the courts of the Member State within the territory of which the debtor's COMI is situated shall have jurisdiction to open main insolvency proceedings. COMI '… shall be the place where the debtor conducts the administration of its interests on a regular basis and which is ascertainable by third parties', see Article 3(1) EIR (2015). It would mean, too, that Article 5 EIR (2015) ('Judicial review of the decision to open main insolvency proceedings') applies. The debtor (including every company of the same group) or any creditor may challenge before a court the decision to open main insolvency proceedings on grounds of international jurisdiction, see Article 5(1) EIR (2015). Furthermore, the decision to open main insolvency proceedings may be challenged '… by parties other than those referred to in paragraph 1 or on grounds other than a lack of international jurisdiction where national law so provides.' This line should be understood as an invitation to Member States to further detail its rules. Overall, legislation at the national and European level should aspire to implement the 'One Group – One COMI' principle.

742. Conscious that a European COMI rule is hard to implement in the nearer future, the Reporters hold that on a European level, group coordination proceedings should be strengthened. This type of additional tool should include more efficient tools for European corporate group restructuring and insolvency cases. First and following the UNCITRAL Recommendations, insolvency practitioners of a group company should not be allowed to object to their participation in such proceedings unless it would result in a significant detriment to the interest of their creditors. Under the same conditions, insolvency practitioners should be obliged to comply with the coordinator's recommendations. Furthermore (following the example of the US bankruptcy practice), the adoption of a group restructuring or insolvency (sale) plan should be allowed in group coordination proceedings where a specific majority of creditors across all proceedings vote in favor of such a plan. Here, conflicts of interest that are inherent to creditors of separate members of a group should be reflected by putting creditors of different entities into different classes and restricting any cross-class cramdown to classes belonging to the same entity (no cross-entity cramdown). The only exception to this main rule should be in case of the detriment of the creditors.

743. Finally, intermingling of assets should not lead to deceive creditors. In accordance with the recommendations of UNCITRAL, we feel that the law of the Member States should specify that the court may order substantive consolidation with respect to two or more company group members: (i) where the court is satisfied that the assets or liabilities of the company group members are intermingled to such an extent that the ownership of the

[1193] See CJEU 15 December 2011, C-191/10 (*Rastelli Davide e C. Snc v Jean-Charles Hidoux, liquidator of Médiasucre International*); EU:C:2011:838, referred to in para. 1152.

assets and responsibility for the liabilities cannot be identified without disproportionate expense or delay; or (ii) where the court is satisfied that the company group members are engaged in a fraudulent scheme or activity with no legitimate business purpose and that substantive consolidation is essential to rectify that scheme or activity.

9.7. Recommendations regarding corporate group issues

Recommendation 9.01: Members States individually and the European legislators, when reviewing the Insolvency Regulation (Recast), should provide for a specific framework to address insolvency in the context of group of companies, meaning a parent undertaking and all its subsidiary undertaking in the meaning of the definitions in the Insolvency Regulation (Recast), that contains the following elements.

Recommendation 9.02: Members States should ensure that a court, having to decide on a request for opening of insolvency proceedings with regard to a member of a corporate group, should verify whether a coordinated strategy is being considered for some or all of the members of the group.

Recommendation 9.03: The European and national legislators ensure that insolvency practitioners and courts are guided by the principles and guidelines set out in the Communication and Cooperation Guidelines for Cross-Border Insolvency Guidelines of 2007 ('CoCo Guidelines'), the EU Cross-Border Insolvency Court-to-Court Cooperation Principles of 2015 ('EU JudgeCo Principles'), which include EU Cross-Border Insolvency Court-to-Court Communications Guidelines ('EU JudgeCo Guidelines'). Communication and cooperation may take any form, including the conclusion of protocols. Such a protocol should include clauses regarding notices, the right of insolvency practitioners, creditors or other stakeholders to appear, access to data and information among insolvency practitioners, communication among committees, asset preservation, claim including specific rules for intercompany claims, submission of a restructuring plan of a liquidation plan, amendment of the protocol and the incorporation of the CoCo Guidelines, the EU JudgeCo Principles and EU JudgeCo Guidelines by reference and form part of this protocol in whatever form they are formally adopted by each court, in whole or in part and with or without modifications, if any, with the addition of a clause providing that where there is any discrepancy between the protocol and these principles and guidelines the protocol shall prevail.

Recommendation 9.04: The European and national legislators should mandate courts and insolvency practitioners to communicate and cooperate in international cases that do not fall under the application of the Insolvency Regulation (Recast) providing rules analogous to the CoCo Guidelines, the EU JudgeCo Principles and EU JudgeCo Guidelines. The fact the Insolvency Regulation (Recast) does not apply should not preclude insolvency practitioners and courts in relevant third country jurisdiction from communicating and cooperating with their respective counterparts to the extent that such communication or cooperation is compatible with the national laws of any such third country jurisdiction.

Recommendation 9.05: Member States should enable their courts to jointly open insolvency proceedings for several companies belonging to the same group if the court finds that the center of main interests (COMI) of those companies is located in their Member State.

Recommendation 9.06: The European and national legislators should ensure that group coordination proceedings under the Insolvency Regulation (2015) become more efficient.

Recommendation 9.07: The European and national legislators should provide that the court located in the COMI ('COMI court') of a member participating in group coordination proceedings may authorise the insolvency practitioner appointed to seek: (i) to participate and be heard in a coordinating proceeding taking place in another jurisdiction, (ii) recognition by the coordinating court of the proceeding in the COMI jurisdiction, whilst (iii) the coordinating court can receive such a request for recognition.

Recommendation 9.08: The European and national legislators should ensure that, while participation in group coordination proceedings is voluntary in principle, the decision not to participate is required to exclude a member from the effects of such proceedings (opt-out). In addition, the COMI court should be allowed to opt-out of its group member whenever the decision to opt out is not adopted in good faith. Where a high percentage (minimum of 80%) of equally affected members participate in group coordination proceedings, the COMI court should assume that an opt-out was decided in bad faith unless good faith is proven to the court.

Recommendation 9.09: Solvent members of a group should be allowed to formally participate in group coordination proceedings without such participation implying a submission to the jurisdiction of a court or to the applicability of its insolvency laws.

Recommendation 9.10: The European and national legislators should ensure that group coordination proceedings can result in a group restructuring or insolvency plan that is binding for all participating members. Creditors and stakeholders of participating group members would be placed in separate classes and vote under the rules according to the applicable national law in their own jurisdiction. Following the vote of the group restructuring or insolvency plan by relevant creditors and stakeholders, each COMI court would confirm the plan if it holds that the plan was accepted according to national law including all its cramdown options. A cross jurisdictional (cross entity) cramdown would not be possible.

Recommendation 9.11: The European and national legislators should ensure that the insolvency practitioner appointed in the group coordination proceedings (coordinator) should have the right of access to proceedings in each COMI court to be heard on issues related to implementation of the group restructuring plan.

Recommendation 9.12: The European and national legislators should ensure that a court may approve the substantive consolidation of the estates of jointly administered members of the group (see Recommendation 9.05), of parts of these estate, where (i) the assets and liabilities of all of the respective members have been commingled in a sense that they cannot easily be untangled without severe effort, delays and costs, or (ii) the group structure has been used to deceive creditors. They should also allow a group restructuring or insolvency plan to provide for such a form of consolidation in cross-border cases.

CHAPTER 10:
Special arrangements for small and medium-sized enterprises (SMEs) including natural persons (but not consumers)

744. The efficient application of an insolvency and, maybe even more, a restructuring framework rests on the assumption of some basic preconditions. The previous chapters should have made it obvious that a successful business rescue depends on institutions (courts, insolvency office holders, public agencies) that work with sufficient efficiency and transparency, a market that offers rescue finance as well as a purchase option for the business (a market price), and sufficient assets in the debtor's estate to incentivise all participants to actively engage in the process based on the idea that they have something to gain from it (be it the continuation or take-over of the business, a payoff on their debt or a remuneration).

745. While establishing and maintaining the legal and economic preconditions of an insolvency and restructuring framework is a task of public policy in the first place, a certain class of debtors has raised the question whether it can meet the preconditions in principle: smaller businesses. It's the lack of (unencumbered) assets in particular that has prompted some, but not all legislators (see table below) in the jurisdictions that this report covers to provide for a special legal treatment for smaller businesses in their framework. Beyond such a response by legislators, legal practice has responded to the special challenges of small business insolvencies in all jurisdictions, usually by not even considering a rescue when foreclosing the business. The connected task of reintegrating the entrepreneur behind a failed business is addressed in most jurisdictions.

10.1 Defining the special class of MSE businesses

746. Traditionally, a special treatment (often a simplified application of restructuring or insolvency procedure) is connected with the term "SME": small and medium-sized enterprises. A closer look at our Normative Reports reveals that existing regulations actually limit such privileges to businesses that do not exceed certain thresholds. While these thresholds are different across jurisdictions, the overall picture reveals that a special treatment is commonly only available for small, but not for medium-sized businesses. The latter ones may even be seen as a prototype for regular insolvency proceedings as, in a number of jurisdictions, specific provisions for large businesses exist as well. It might, therefore, be more appropriate to refer to the class of businesses at the lower end of the scale as "micro and small-sized enterprises" or "MSE". For medium-sized businesses, common insolvency and restructuring rules and procedures appear designed and applicable.

Member State	MSE privilege	MSE definition	Type of privilege
AT	--	--	--
BE	--	--	--
DE	--[1194]	Business satisfies two out of three	No mandatory

[1194] German insolvency law does not distinguish business debtors by their size; the only minor exception being Insolvency Code s 22a addressing the court's discretion to appoint a preliminary creditors' committee.

		requirements:[1195] 1. Balance sheet total of €600.000 max.; 2. Annual revenue of 12 million max.; 3. Max. of 50 employees on average	preliminary creditors' committee
EL	Not really[1196]	Assets below €100.000	Simplified insolvency procedure Simplified claims verification
ES	Yes	• Less than 50 creditors; • debt of max. €5 million; and • assets of max. €5 million	Simplified insolvency procedure[1197] (accelerated deadlines for liquidation)
FR	Yes	• Debtor does not own real estate, • does not have more than one employee, and • has an ex-VAT revenue of €300,000 max. [1198]	Simplified liquidation procedure (Régime simplifié obligatoire) with fixed deadline for liquidation of 6 month
		• Debtor does not own real estate, • does not have more than 5 employees, and • has an ex-VAT revenue of €750,000 max. [1199]	Simplified liquidation procedure (Régime simplifié facultatif) with fixed deadline for liquidation of one year
		• Entrepreneur (no company) does not own real estate, • has not employed anyone in prior 6 months (and no labour law suit pending), and • assets less than €5.000	Personal reinstatement proceedings (Rétablissement personnel) for a quick discharge
HU	--	--	--
IT	--[1200]	• Less than €300,000 p.a. assets • Less than €200,000 gross revenue; and • debt of max. €500,000	Consumer insolvency rules apply
LV	--	--	--
NL	--	--	--
PL	--[1201]	--	--

[1195] Insolvency Code s 22a (1) (copying the definition of a small corporation in the German Commercial Code s 267 (1)).
[1196] In such cases, the bankruptcy court may decide that different rules than those of the Greek Bankruptcy Code are applicable (Article 162 and 163 GBC).
[1197] Spanish Insolvency Code Article 190.
[1198] French Commercial Code Article D.641-10 para.1.
[1199] French Commercial Code Article D.641-10 para.2.
[1200] Companies that stay below certain thresholds are not subject to insolvency (fallimento) or restructuring (concordato preventivo) proceedings (Article 1.2 of Italian Insolvency Law). They are handled as consumer cases.

SE	--	--	--
UK	Yes	Business satisfies two out of three requirements: [1202] 1. annual turnover of max. £6.5 million; 2. assets on the balance sheet of max. £3.26 million; 3. max. of 50 employees	a) Moratorium to propose a CVA outside of administration[1203]
		Sole entrepreneur	b) Individual Voluntary Arrangement (IVA) procedure[1204]

747. Our reports also show that it is close to impossible to provide for a definition of classes of businesses that can be labelled micro or small-sized that would fit all European jurisdictions.[1205] Latest research on a global scale has shown that such a "one size fits all" definition of MSE does not exist.[1206]
Instead of focusing on numbers (revenue, employees, debt level, etc.), the scope of a privilege for small businesses should be adapted to the characteristics which justify a special treatment in insolvency and restructuring.[1207] There are actually two specific characteristics which could be utilised.

10.1.1 Limited resources, limited outsider expectations

748. The main obstacle to pursuing regular restructuring or insolvency proceedings in a small business case is the lack of resources.[1208] Typically, such businesses enter proceedings with little or no unencumbered assets. At the same time, there business idea is usually a very

[1201] Polish bankruptcy law only contains a small deviation from the general deadline for concluding a restructuring plan (3 month for small and medium-sized businesses instead of 4).
[1202] Insolvency Act 1986 s 1A, Schedule A1 para.3.
[1203] Insolvency Act 1986 s 1A with Schedule A1.
[1204] Insolvency Act 1986 s 252-263G.
[1205] Any definition of SME that includes medium-sized businesses would even define thresholds well above those found in our Inventory Reports; see e.g. the European Commission: either less than 250 employees and less than 50 million Euros of sales proceeds, or less than 250 employees and less than 43 million Euros of total assets; see the Commission's Recommendation concerning the definition of micro, small and medium-sized enterprises [2003] OJ L124/36, Annex I Article 2. See also the U.S. definition in 11 U.S.C. s 101 (51D)(A): "aggregate noncontingent liquidated secured and unsecured debts […] in an amount not more than $2,000,000".
[1206] See Ronald Davis, Stephan Madaus, Alberto Mazzoni, Irit Mevorach, Riz Mokal, Barbara Romaine, Janis Sarra, and Ignacio Tirado, 'The Modular Approach to MSME Insolvency' (working paper, 2016), 14-15; see also Oya Pinar Ardic, Nataliya Mylenko, Valentina Saltane, 'Small and Medium Enterprises a Cross Country Analysis with a New Data Set', The World Bank Financial and Private Sector Development Consultative Group to Assist the Poor, Policy Research Working Paper 5538, January 2011, p. 6-8.
[1207] André Boraine and Jani van Wyk, 'Various Aspects to Consider with Regard to Special Insolvency Rules for Small and Medium-Sized Enterprises in South Africa', 24 Int. Insolv. Rev. 2015, 228, 240-241; see also Brian A. Blum, 'The Goals and Process of Reorganizing Small Businesses in Bankruptcy', 4 J. Small & Emerging Bus. L., 2000 p. 181, 193.
[1208] *Idid*, 195; see also Donald R. Korobkin, 'Vulnerability, Survival, and the Problem of Small Business Bankruptcy', 23 Cap. U. L. Rev. 1994, p. 413, 428: 'resource poverty'.

common and interchangeable one (shop, restaurant, garage etc.).[1209] As a result, there is little to gain and, thus, no appetite to spill energy and resources to find out, for unsecured creditors in a liquidation or restructuring, even in a quick one.[1210] There is also little investor interest that could initiate a bidding process on the firm's assets or business ideas. Finally, there is little to no money in the firm to pay for expert advice,[1211] an insolvency office holder or a court. Overall, limited resources lead to limited expectations.

10.1.2 The entrepreneur

749. The second peculiar characteristic of small businesses is its interdependency with the entrepreneur.[1212] A small business usually thrives on the ideas and enthusiasm of its entrepreneur and provides for the livelihood of the entrepreneur and, often, the entrepreneur's family. The failure of such a small business is at the same time a failure of an entrepreneur. This fact not only involves a psychological aspect that commonly leads to very late filings and, thus, even fewer resources in proceedings. It also contributes a social aspect because the failure does not primarily hit financial stakeholders in the business (as there are often only a few employees or financial creditors with a significant volume of claims) but mostly the entrepreneurs and their families. Finally, the entrepreneur itself does also represent a limited resource when we look at their limited skills and personality.

750. The fact that an (individual) entrepreneur is running the small business is also an important characteristic to exclude cases of failing corporate groups from the scope of MSE procedures. Members of corporate groups can be small business in terms of revenue and number of employees, but they do not feature the characteristic of a sole entrepreneur. Instead, they are owned by other companies (being their shareholders) and run by a professional management.

10.1.3 Irrelevant factors

751. A system of special arrangements for small businesses rests on the assumption that the general rules for restructuring or liquidating a business cannot be applied sufficiently due to a lack of resources, outsider expectations and, sometimes, insider skills. Lawmakers should frame the scope of MSE procedures accordingly. Common references to thresholds in revenue or employees do not seem to reflect this background appropriately as they are too high (in particular when including medium-sized enterprises).

752. The same can be said about rules that exclude corporate debtors from MSE frameworks. The relevant lack of resources as well as the described interdependencies with the entrepreneur may be present regardless of the fact that the entrepreneur had decided

[1209] In this point, the situation might be different in cases of new economy start-ups where investors might be willing to invest in a new idea or an original design.

[1210] Brian A. Blum, 'The Goals and Process of Reorganizing Small Businesses in Bankruptcy', 4 J. Small & Emerging Bus. L. 2000, p. 181, 200.

[1211] *Idid*, 194; Donald R. Korobkin, 'Vulnerability, Survival, and the Problem of Small Business Bankruptcy', 23 Cap. U. L. Rev. 1994, 413, 427.

[1212] André Boraine and Jani van Wyk, 'Various Aspects to Consider with Regard to Special Insolvency Rules for Small and Medium-Sized Enterprises in South Africa', 24 Int. Insolv. Rev. 2015, 228, 242; Donald R. Korobkin, 'Vulnerability, Survival, and the Problem of Small Business Bankruptcy', 23 Cap. U. L. Rev. 413, 425 (1994).

earlier to or not to incorporate.[1213] Given the fact that the corporate veil may be pierced by personal guarantees of the entrepreneur in small businesses cases anyway, an exclusion of incorporated small businesses does not seem justified.

10.2 The specific challenges of MSE procedures

753. The application of the common restructuring and insolvency frameworks faces challenges in MSE cases on two levels.

10.2.1 Microeconomic challenges

754. In a microeconomic perspective, failing small businesses produce cases with very few or no assets. This scarcity brings a variety of implications. The most obvious one is the question of how to finance proceedings. Leaving aside indirect costs of every insolvency proceeding, the involvement of a court and an insolvency office holder does come with cost in terms of fees and remuneration which are already hard to cover (if at all) for a small failing business.[1214]

755. In addition, the limited amount of assets to be sold in a liquidation provides little incentive for unsecured creditors to even participate actively in proceedings because such activity is usually connected with additional costs (for traveling, legal advice, postage). Limited expectations result in rational creditor passivity. The only exception to this phenomenon is the secured creditor, often a sole local bank, who is the driving force behind such proceedings in order to secure a maximum return on their loan. The secured creditor, and the debtor/entrepreneur (and possibly their family and employees), are the main beneficiaries of orderly restructuring and insolvency proceedings for typical small businesses.

756. Overall, the microeconomic perspective reveals a situation which is dominated by insider incentives to have orderly proceedings while other stakeholders have good reasons to stay passive.[1215]

10.2.2 Macroeconomic challenges

757. While there is little to gain for everyone except the entrepreneurs and their dominating secured creditor in a single case, the importance of a sophisticated framework for MSE results from a macroeconomic perspective. It is the sheer number of small businesses in our economies that call for a legal framework that does not ignore their specific needs. Today,

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[1213] André Boraine and Jani van Wyk, 'Various Aspects to Consider with Regard to Special Insolvency Rules for Small and Medium-Sized Enterprises in South Africa', 24 Int. Insolv. Rev. 2015, p. 228, 242-244.

[1214] See, e.g., the Polish Inventory Report on Q10.2 expressing the bankruptcy procedures are often too expensive for small businesses in Poland.

[1215] See also the empirical study by Andrea Polo, Secured Creditor Control in Bankruptcy: Costs and Conflict, Andrea Polo, 'Secured Creditor Control in Bankruptcy. Costs and Conflict', 2012, available at https://ssrn.com/abstract=2084881, suggesting in cases of a business with intangible assets (human capital), the value of which might be lost in a public marketing process, there could be efficiencies to be gained from pre-packaged sales to a connected party.

MSE businesses dominate the economy in all Member States by number. The represent 99 per cent of all businesses in the EU. [1216] The Inventory Report for England and Wales refers to government statistics which are also showing that 99 per cent of all businesses in the UK are small and medium-sized (with less than 250 employees), and 95 per cent of all businesses (more than a million) are micro-businesses (with less than 10 employees).[1217] On a global scale, recent studies by the International Finance Corporation revealed that there are 125 million "formal" MSMEs in 132 countries for which data is are collected, including 89 million in emerging markets; 83 per cent are micro enterprises.[1218]

758. A well-functioning restructuring and insolvency framework for MSE must, therefore, be equipped to handle a large number of cases with little to no assets or creditor activity. Otherwise the sheer number of cases can become a burden to the judicial system and its surrounding institutions. At the same time, the system should be efficient in scrutinizing cases for fraud in order to quickly disqualify or, if honest, discharge an entrepreneur who failed with a business idea. A recent macroeconomic study has highlighted the desirable effects to economic growth and employment numbers that can be generated by reintegrating such entrepreneurs into the market.[1219]

10.3 The specific instruments of MSE procedures

759. A modern MSE restructuring and insolvency framework should address the specific challenges of this type of businesses on both the micro- and macroeconomic level.

10.3.1 Responding to the microeconomic challenges

760. The limited resources present in a MSE insolvency cause a financing problem that should not be solved by denying such businesses access to proceedings. Currently, a larger number of Member States do not even open[1220] or immediately terminate[1221] proceedings if the debtor does not have sufficient resources to cover at least the expenses of the court and the insolvency office holder; some even require the debtor to cover all expenses of insolvency proceedings.[1222] Denying orderly collective proceedings for a larger group of businesses provides the incentive to either restructure early (with sufficient time and assets to be successful) or close down very late – with insufficient assets to pay for orderly proceedings that would scrutinise the debtor's (and creditors') behaviour in the crisis. Without an investigation, fraudulent transfers or other misconduct of directors and creditors remain unnoticed and unsanctioned. Instead, lawmakers should ensure that all businesses

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[1216] European Commission, 'What is an SME', see http://ec.europa.eu/growth/smes/business-friendly-environment/sme-definition_de.

[1217] House of Commons Library, Business Statistics, 23 November 2016, available at http://www.parliament.uk/business/publications/research/briefing-papers/SN06152/business-statistics.

[1218] Khrystyna Kushnir, Melina Laura Mirmulstein and Rita Ramalho, 'Counting MSMEs Across the World', IFC, available at http://www.ifc.org/msmecountryindicators.

[1219] Jean-Charles Bricongne, Maria Demertzis, Peter Pontuch and Alessandro Turrini, *Macroeconomic Relevance of Insolvency Frameworks in a High-debt Context: An EU Perspective*, Discussion Paper 032 (June 2016).

[1220] See, e.g., Austria, Germany, Greece, also UK (for liquidation proceedings).

[1221] See, e.g., Belgium, and Spain.

[1222] See, e.g. Poland.

that are not wound up voluntarily are subject to their insolvency (or a similar investigative) framework.

Financing

761. Financing for small business proceedings can be generated by ensuring that the estate can efficiently enforce claims from fraudulent transfers and avoidance actions as well as director liability claims. In Germany, for example, it was reported that a relevant number of insolvency proceedings are only commenced based on the assumption of sufficient liquidity from the successful enforcement of such claims. Additional financing, for micro-sized businesses in particular, could also be provided by government support, in particular by deferring the payment of procedural costs (court fees, IP remuneration) to the moment when proceedings end.[1223] Third party funding, e.g. from family members or business supporters in the local community, but also from professional litigation funding organisations, should not only be allowed, but also incentivised (possibly by introducing a tax deductibility, or a priority for repayment from generated assets after costs are paid).

762. At the same time, lawmakers must ensure that MSE proceedings are conducted in a cost-sensitive manner.[1224] There are a (few) Member States (see e.g. Hungary, the Netherlands, Sweden, also Latvia) that have already provided for a simplified (liquidation) procedure. Here, the costs of proceedings are reduced by a statutory limit of their duration. Costs can also be minimised by not establishing costly stakeholder representatives like creditors' committees[1225] or by appointing an insolvency office holder only on a case by case basis if necessary and cost-efficient.

Complexity

763. Proceedings for small businesses should be easily accessible. The entrepreneur should be, and feel, able to initiate such proceedings if it seems useful or necessary. Despite their usually limited knowledge in matters of business restructuring proceedings and little resources for hiring advice, entrepreneurs must be offered a restructuring option as soon as they realise that their business is in trouble that they can easily access on their own. Legal requirements for filing, in particular for restructuring proceedings, should reflect these circumstances. Our reports show that an overly complex or sophisticated procedure, in particular with regards to filing requirements,[1226] is hardly ever used in practice.[1227] Interviews with NC's also indicated that the liquidation of a small business, which may of course also include a going concern sale (or a sale back to the owner), is the dominant

[1223] In Germany, for instance, most consumer insolvencies are only commenced thanks to a provision introduced only in 2001 (Insolvency Code s 4a) that allows the court to defer payments on costs to the very end of the discharge proceedings. In many cases, costs are covered by the estate at that moment. If not, cost remain with the government.

[1224] See e.g. the UK Inventory Report on Q10.1 stressing that the nominee in a CVA with moratorium must always assess whether the company is likely to have sufficient funds to carry on trading during the period of the moratorium.

[1225] See e.g. Germany: no mandatory preliminary creditors' committee in smaller cases (Insolvency Code s 22a).

[1226] Latest reforms in the UK addressed the complexity issue by relaxing procedural requirements, for instance the requirement to have in person meetings.

[1227] See the UK Inventory Report's assessment of the CVA with moratorium (responding to Q10.1).

strategy in all jurisdictions. However, our reporters suggest that tentatively insolvent small businesses are very likely to be liquidated on a piecemeal basis.[1228] Such business file too late (if at all; often creditors file) with too little left to restructure or sell as a going concern. A well drafted, simple option to initiate a court restructuring would provide an alternative to struggling entrepreneur at an earlier moment in a business crisis.

Passivity

764. Limited expectations for unsecured creditors regarding any distributions on their claims in small insolvency cases often result in the rational decision to not participate in such proceedings. Creditor passivity is rational. Such behaviour causes a problem, however, if the design of a restructuring and insolvency framework is geared towards creditor autonomy and creditor decision making. Lawmakers can respond to this peculiarity of small business cases in various ways.

765. One option would see decision making shifted from creditors to the court. Thus, creditor passivity would not affect the legitimacy of the proceedings. The disadvantage of this shift is the burden that would be put on judges who may not be best equipped to make a business decision when asked to decide on a restructuring plan.[1229]

766. A preferred solution could be a distinctive treatment of passivity in the decision making process which would remain with the creditors. Here, their active involvement could be triggered by asking all affected creditors to vote on a plan (or sale proposal) within a strict timeframe and counting each non responding creditor's vote as if they vote as a 'yes' ('deemed consent'). Passivity would be seen as approving what is proposed and done in proceedings. With such a deemed approval, passive creditors would also lose the right to appeal the decision. Such a framework should be able to activate dissenting creditors while lowering overall participation cost as creditors would only need to actually participate (with all costs involved) if they feel that they could do better by following a different strategy or plan. Rational passivity would no longer damage proceedings, but instead facilitate them.

Abuse

767. Every effort to facilitate the access to a restructuring and insolvency framework as well as the success of such proceedings allows for abusive strategies. A quickly initiated procedure based on a simplified motion that results in an outcome that was mostly approved by passive creditors seems to literally invite dishonest entrepreneurs who look for a way to escape their creditors. The best way to counter such strategies should still not comprise extensive filing requirements or high hurdles to have a plan confirmed by creditors. Instead, legislators should turn to stakeholders who also have a real interest in the outcome of small insolvency or restructuring cases. Stakeholders like the main financial

[1228] See the Inventory Reports on Q10.2 from Greece, Italy, Latvia, the Netherlands, Poland, Spain, or England and Wales.

[1229] Douglas G. Baird and Edward R. Morrison, 'Bankruptcy Decision Making', J. L. Econ. & Org. 356, 366-367 (2001): "the bankruptcy judge is ill equipped to make the shutdown decision." See also Barry E. Adler and Ian Ayres, 'A Dilution Mechanism for Valuing Corporations in Bankruptcy', 111 Yale L. J. 2001-2002, p. 83, 90; Yaad Rotem 'Better Positioned Agents: Introducing a New Redeployment Model for Corporate Bankruptcy Law', 10 U. Pa. J. Bus. & Emp. L. 2007-2008, p. 509, 525.

creditor (usually a secured creditor), main trade creditor, or a public authority (like the tax or social security agency) have resources as well as incentives to initiate and closely watch even small cases and raise flags if they suspect abusive debtor behaviour.

768. It seems preferable not to establish a strict check for abuse at the stage where proceedings are initiated (which usually entails strict duties of the debtor to provide a lot of information). Instead, the course of proceedings should be used to gather information and decide about a possible abusive strategy of the debtor. In addition, such a strategy can be frustrated by limiting the guaranteed effects of commenced proceedings, in particular by granting only a short moratorium on the outset (e.g. 14 days in UK IVA [1230]), or a short deadline for restructuring attempts (see e.g. Poland). Lawmakers could also consider balancing negative effects of a 'no vote is a yes vote' rule by giving no or less voting rights to associates of the debtor in cases where they are eligible to vote because they are creditors.

10.3.2 Macroeconomic challenges

769. Another important aspect of any framework addressing small business cases comes from the fact that there are so many. Based on the structure of the economy in all Member States which is dominated by small businesses, an efficient restructuring and insolvency framework for such businesses would prompt a high number of cases. The sheer quantity of cases presents a burden to the legal and institutional framework of small business insolvencies. This challenge can be mastered by decentralising and automating the case management on the one hand, and by shortening such proceedings on the other.

Decentralising and automating

770. Traditional insolvency and restructuring proceedings are court proceedings. As the number of courts and judges in all Member States is limited and commonly charged to capacity, the additional case load caused by efficient proceedings for small businesses could cause additional delay and extensive durations for any court based procedure. Any framework for small business cases must, therefore, try to save the scarce resource of the judiciary from overload.

771. One option would be to require a workout attempt by the debtor before they are allowed to go to court. Such a requirement would prompt debtors to initiate negotiations with their creditors before turning to the court. It would, however, also mean that debtors cannot simply and quickly initiate restructuring or insolvency proceedings in a crisis. A mandatory workout attempt requirement would, thus, conflict with the objective of a low entrance barrier, and it's the latter objective which should prevail. Experience from Germany, where a mandatory workout attempt requirement has existed for consumer insolvencies for more than 15 years, indicates that such a hurdle does not result in a significant number of successful workouts and, therefore, has little impact on limiting the number of cases going to court.[1231] In addition, the later the restructuring starts, the higher

[1230] Insolvency Act 1986 s 255(5).

[1231] For the German experience with such a rule see Werner Sternal, *Uhlenbruck, Insolvenzordnung*, § 305 at para.11.

the costs of financial distress will be (in particular from distracting the entrepreneur from the task of actually running the business).

772. The preferred way to relieve judges from the burden of small business cases is to assign such cases to a different institution for case management, and to involve courts only when it is imperative to do so with respect to the constitutional rights of stakeholders. Commonly, the constitutional right to be heard by a judge is relevant if a stakeholder is affected by a procedure and is actively objecting the decision that affects their rights.[1232] Depending on the constitutional requirement in a Member State, lawmakers should allow for the administration of small business cases by local authorities (possibly authorities that are designed to cover this task).[1233] The case management could also be assigned to private entities, in particular to the dominating financial creditor that would also cover most assets of the debtor in a private enforcement outside of insolvency law.[1234]

773. In addition, the workload of any entity assigned with the task of handling small business cases should be minimised by using modern IT tools to collect and distribute information. Lawmakers should provide for simple filing forms[1235] or, if possible, interactive only templates which would not only allow a debtor to easily initiate proceedings, but also enable the administrating entity to easily process and distribute all relevant information.

Speeding up proceedings

774. Finally, the burden caused by the number of cases can be reduced by limiting the time they stay with a court. Any (voluntary and involuntary) liquidation procedure should be conducted swiftly. Inventory Reports from Spain and France indicate the use of accelerated liquidation deadlines. In addition, the liquidation in total could be left for the secured creditor outside of proceedings if there are no unencumbered assets to be found in the estate of a small business.

775. In case of a restructuring procedure for small cases, short deadlines (e.g. 14 days) should limit the availability of a stay as well as the time to present a plan and to cast votes. If creditors come to the conclusion that the debtor is only wasting time in a restructuring procedure, they should be able to file a motion for the termination of the restructuring and the initiation of a liquidation. Such a motion must be successful if it is filed by a creditor or a number of creditors with the voting power to veto any plan.

[1232] See in particular the CVA under English law where no court decision is required as long as no objection is filed by an affected creditor.

[1233] See, for instance, the 'crisis settlement panel' for debt payment and cancelation plans of individuals in Italy.

[1234] In the Netherlands, the major financial creditor of a small business (usually a Dutch bank) is already heavily involved in 'an intensive coaching and supporting strategy to accompany the debtor in financial difficult times'; see the Dutch Inventory Report on Q 10.2. From here it is only a small step to also involve them in administering a formal restructuring or liquidation. See also Carsten Jungmann, *Grundpfandgläubiger und Unternehmensinsolvenz, Deutschland — England — Schottland* (Bonn, Köln, Berlin, München 2004) 422; Andrea Polo, 'Secured Creditor Control in Bankruptcy: Costs and Conflict, 2016, p. 4-7, available at http://ssrn.com/abstract=2084881.

[1235] See, e.g., the German law that requires the use of an official form for filing a consumer insolvency motion; see Insolvency Code s. 305 (5) 2. The template is available online at http://www.bmjv.de/DE/Service/Formulare/Formulare_node.html.

Quick discharge for entrepreneurs

776. Currently most MSE insolvency cases do not aim at a restructuring (which could be changed by making a restructuring option more viable by following our recommendations); they are initiated in order to close the business and achieve a discharge for the entrepreneur from business related debt. The primary purpose of insolvency proceedings shifts in such cases – from maximising payoff for creditors to ensuring that a discharge is equitable. Most of these (numerous) cases are conducted with no distribution to unsecured creditors. Yet, conducting such proceedings is mandatory in all Member States to arrive at a discharge.[1236]

777. The macroeconomic task of allowing entrepreneurs a fresh start is either completed by discharging their troubled but viable business in a restructuring, or by discharging the individual entrepreneur while or after selling or winding up their business. For the latter task, a number of jurisdictions relegate the entrepreneur to the procedure for debt adjustment available for all individuals[1237]; only a few Member States have reported specific provisions for discharging failed entrepreneurs[1238] or merchants.[1239]

778. It must be stated that under the current conditions the individual entrepreneur is often not discharged from business related debt concurrently with the conclusion of liquidation proceedings (with only a few jurisdictions being the exemption).[1240] Instead, failed entrepreneurs are often obliged to 'earn' their discharge with future income by assigning the bulk of their future income for years in order to be discharged eventually.[1241] It seems like the honesty of a debtor is not simply taken from the fact that they lose all their assets due to insolvency alone. Instead, they need to prove the worthiness of being discharged by (trying to) working off their remaining old debt. And even if they do so, some legal regimes limit the effect of a discharge in a way that it does not even include a significant part of the remaining debt. Such legal frameworks do not appear well fitted to achieve a quick and macro

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[1236] This is true even in jurisdictions like Germany that provide for separate procedures for insolvency and discharge proceedings: insolvency proceedings need to be finished first before the debtor is allowed to access discharge proceedings; see Insolvency Code s 286.

[1237] See the Inventory Reports on Q10.3 from Austria, Germany, the Netherlands, Poland, and Spain.

[1238] See Belgium or Latvia where honest entrepreneurs are immediately discharged upon request at the conclusion of those proceedings in which their business has been transferred or wound up. Honesty is assumed. In Italy, an entrepreneur who complies with the requirements provided by law and who has repaid even in part its debts is discharged when the insolvency proceeding is terminated. Under English law, discharge of the debtor occurs automatically at the end of the period of one year beginning with the date on which the bankruptcy order was made (Insolvency Act 1986 s 279(1)). The entrepreneur the bankrupt may be discharged even earlier if the official receiver files with the court a notice stating that investigation of the conduct and affairs of the bankrupt is unnecessary or concluded (Insolvency Act 1986 s 279(2)).

[1239] See Greece where the discharge of merchants may be granted two years after the declaration of bankruptcy. Debtor's good faith at the time of the bankruptcy declaration and during the insolvency proceedings as well as his good cooperation with the bodies of the bankruptcy procedure are required. In addition, the insolvency shall not be a result of the debtor's fraud (Greek Bankruptcy Code Article. 168 and 169). Non-merchants individuals may obtain a discharge only after three years.

[1240] Such an immediate discharge would reflect the standard set by the Principles of European Insolvency Law (2003), § 13.2.

[1241] See Austria (3-7 years), Germany (3-6 years). Under Spanish law, specific minimum payments are required for an immediate discharge.

economically desirable reintegration of entrepreneurs into the economy.[1242] Instead, lawmakers should ensure that entrepreneurs that make all their assets available for paying off old debt have a secured path to be discharged from all[1243] business related[1244] debt by the end of insolvency proceedings if there is no objection raised based on any fraudulent behaviour. If such behaviour is discovered only later, the discharge should be revocable. As a result, the 'price' of a discharge is requiring a debtor who has no acted fraudulently to make available all their remaining assets. If the debtor intends to keep some of their wealth while being discharged, a payment plan should be available which becomes effective if the creditors agree with a stipulated majority.

10.4 Recommendations

Recommendation 10.01: Member States should define the scope of special provisions for small business restructuring and insolvency cases with a focus on micro and small businesses. Member States should not include medium-sized businesses as they usually not require a special treatment.

Recommendation 10.02: Member States should ensure that (near) insolvent micro and small businesses have access to orderly proceedings regardless of available assets to cover the costs of proceedings.

Recommendation 10.03: Member States should allow for the payment of procedural costs (court, insolvency practitioner) to be deferred in order to allow for the thorough investigation and efficient enforcement of claims from fraudulent transfers and avoidance actions as well as of director liability claims.

Recommendation 10.04: Member States should consider financing procedural costs of restructuring and insolvency proceedings of no-asset cases by public funds, and further incentivising third party funding of restructuring and insolvency proceedings (e.g. by a first priority repayment of these funds and/or a tax deductibility).

Recommendation 10.5: Member States should lower the complexity and duration of small business cases in order to limit costs, but also to facilitate the access to procedures for average skilled sole entrepreneurs.

Recommendation 10.06: Member States should reflect the rational creditor passivity in the rules on the decision about the restructuring plan, a sale of the business, or a piecemeal liquidation by a deemed approval rule. To ensure speed and efficiency of proceedings, non-

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[1242] See DG Justice, Initiative on insolvency – Inception Impact Assessment, 03/03/2016, at p. 2-3. More general see Stephan Madaus (reporter), The Impact on SMEs of the Proposal of Preventive Restructuring, Second Chance and Improvement Measures, an In-Depth Analysis (PE 583.151, May 2017), at the request of the European Parliament's Policy Department for Citizens' Rights and Constitutional Affairs, available at www.europarl.europa.eu/RedData/etudes/IDAN/2017?583151/IPOL_IDA(2017)583151_EN.pdf.

[1243] This basic rule does not exclude narrow exemptions to a full discharge for penalties and fines.

[1244] As a distinction between business-related and private debt may be difficult for many small business entrepreneurs. Lawmakers should design any rule discharge-friendly and, possible, not differentiate between both types of debt for the purpose of an effective discharge.

participating creditors should also not be able to delay proceedings at a later stage by appealing to (higher) courts.

Recommendation 10.07: Member States should ensure that facilitated procedures for micro and small businesses are not abused to disenfranchise creditors. The honesty of a debtor should, however, not be tested on the first day of proceedings based on extensive filing requirements, but instead be scrutinised during the cause of proceedings by investigations of the court, an insolvency practitioner, informed public authorities (tax or social security agencies) and creditors (financing bank; trade creditor). In case of a proven dishonesty, the denial of a discharge for the entrepreneur should work as an efficient sanction.

Recommendation 10.08: Member States should consider having proceedings for micro and small businesses administered outside the court system (by public authorities or secured creditors or other private entities) and only involve courts in handling objections and appeals – as far as their respective constitutional law allows for it.

Recommendation 10.09: Member States should limit the administrative burden of micro and small business cases by using mandatory templates and modern IT tools like interactive templates.

Recommendation 10.10: Member States should only provide for very short periods of a stay or a plan proposal in order to limit the incentive for abuse as well as the overall duration of proceedings.

Recommendation 10.11: Member States should provide for a secured path for failed entrepreneurs to be discharged from all business related debt by the end of insolvency proceedings if there is no objection raised based on any fraudulent behaviour.

APPENDICES

1 Questionnaire for National Correspondents for national inventory reports

2 Questionnaire for National Correspondents for normative reports

APPENDICES

1 Questionnaire for National Correspondents for national inventory reports

ELI Business Rescue Project: Questionnaire for National Correspondents

Guidance for National Correspondents in responding to the Questionnaire:

1. The Questionnaire follows the order of the 10 topics identified in the ELI Proposal.
2. The two National Correspondents for each jurisdiction are requested to liaise with each other to formulate responses to the Questionnaire, and then to provide a single response by typing answers under each question posed, and returning the completed document to the Reporters by **[Submission date]**.
3. In answering the questions, please provide brief and pointed answers.
4. All questions relate to the national legal system of a National Correspondent, excluding rules of private international law.
5. Some questions are followed by related queries/suggestions which, where relevant, should also be addressed by National Correspondents.
6. National Correspondents are asked to note the following special terms and their meaning:

   "Business rescue": Except where the question otherwise indicates, references to "business rescue" should be understood as encompassing both the rescue of the debtor (such that the entity itself survives) and the rescue of the debtor's business on a going concern basis (whether or not the business continues to be carried on in the same entity). It should be contrasted with the sale of the debtor's assets on a piecemeal or break-up basis.

   "Pre-/insolvency procedure" or "Pre-/insolvency proceedings": Questions 1.1.2 and 1.1.4 ask respondents to identify formal pre-insolvency procedures and formal insolvency procedures that can be used to achieve a business rescue outcome. Except where the question otherwise indicates, any references in subsequent sections to "pre-/insolvency procedures" or "pre-/insolvency proceedings" should be interpreted as referring to the procedures identified in response to Questions 1.1.2 and 1.1.4: that is, they refer only to those formal procedures which can be used to achieve a business rescue outcome, thereby excluding all other forms of formal procedure.

   "Debtor": References to debtors should be interpreted to exclude references to banking and insurance debtors, and references to consumer bankruptcies. For the avoidance of doubt, debtors shall include sole traders and entrepreneurs as well as corporate entities.
7. In responding, National Correspondents are asked to specifically identify the source of any rule to which they refer (for example, by noting the relevant statute and section/article number; the case that has led to a rule being interpreted in a particular way; etc.).

8. When asked about whether a particular rule exists, National Correspondents are encouraged to consider whether – if they answer that no such rule exists – there is another kind of rule that performs an equivalent function, and to identify this.
9. Where they answer “Not applicable” to a question, National Correspondents are asked to explain why this is so unless it will be obvious.

10. The questions are primarily concerned with the current state of the law in each jurisdiction. National Correspondents will also be invited to express their views as to the deficiencies in the law, and their remedial recommendations, in a separate “Normative Report”. A list of 5-10 open-ended questions will be provided in a later stage to help structure this brief report.

Any questions about the Questionnaire should be directed to the Reporters using the email address businessrescue@europeanlawinstitute.eu.

The ELI and the Reporters thank National Correspondents for their time in responding to this Questionnaire.

1. Governance and supervision of a rescue in court and out-of-court

1.2. *Conditions for out-of-court workouts, conditions for opening of such 'proceedings', conditions for opening formal pre-insolvency and insolvency proceedings*

1.2.1. Out-of-court workouts:

(a) Are there any established practices for facilitating out-of-court workouts (i.e. workouts conducted without recourse to any formal restructuring or insolvency procedure)?

For instance: some jurisdictions have developed (e.g. through their Central Bank, or Banking Association) a framework for enabling restructuring negotiations to be conducted for debtors with exposure to multiple banks.

(b) Does the law include specific rules to enable or facilitate out-of-court workouts?

For instance: are there rules of taxation law that facilitate restructuring or the sale of the business on a going concern basis either by providing incentives or removing disincentives to restructure? Does the law provide for a state agency, judge, court or tribunal to offer assistance in the negotiation of an out-of-court workout?

1.2.2. Pre-insolvency procedures:

(a) Does the law provide any formal pre-insolvency procedure in addition to the main formal insolvency procedures that can be used to achieve a business rescue for a debtor in difficulties or anticipation of such difficulties?

(b) What are the general conditions for the opening/commencement of these pre-insolvency proceedings?

For instance: are they to be initiated by debtor only or also by creditors (and if the latter, is there a minimum number of creditors or a minimum value of claims required)? If initiated by the debtor, is notice required to be given to creditors? Are other parties allowed to initiate, such as a government agency or the public prosecutor? Can the debtor or (certain) creditors be banned from requesting such proceedings (e.g. on the basis of an abuse of right principle)?

(c) Where the debtor is a corporate entity: which organs are entitled to decide whether the entity should request the opening of these pre-insolvency proceedings?

For instance: is prior approval of the general meeting of shareholders required? Are minority shareholders protected from being squeezed out in the course of such proceedings initiated by major shareholders? Is prior consultation or approval of a Works Council, or any other form of employee consultation, required?

(d) What publicity rules apply to filing for, and the opening of, these insolvency proceedings (excluding any requirements imposed by securities law for listed entities)?

For instance: is a request for the opening of the proceedings published? Are creditors actively informed of such a filing? If so, are they alerted by an individual notice or by a message containing general information to all creditors? Form of *publicity: Official Gazette, newspapers, court register, trade register, online? Are there any special rules for foreign domiciled creditors?*

1.2.3. Formal insolvency procedures in general:

(a) What formal insolvency procedures are available for business debtors, and what (if anything) are their stated purposes?

(b) Does the law prescribe any hierarchy or order of priority regarding the purpose and/or outcome of insolvency proceedings?

For instance: does the law require a business rescue to be pursued before a piecemeal sale of the debtor's assets, and (if so) does it require a reorganisation to be pursued before a sale of the business on a going concern basis?

1.2.4. Formal insolvency procedures that can be used to achieve a business rescue outcome:

(a) Which of the insolvency procedures identified in 1.1.3 above can be used to achieve a business rescue?

(b) What are the general conditions for the making of the request to commence these insolvency proceedings?

For instance: are they to be initiated by debtor only or also by creditors (and if the latter, is there a minimum number of creditors or a minimum volume of claims?). Are other parties allowed to initiate, such as a government agency or the public prosecutor? Can the debtor or (certain) creditors be banned from requesting such proceedings (e.g. on the basis of an abuse of right principle)?

(c) Where the debtor is a corporate entity and is entitled to request the opening of these insolvency proceedings, which organs of the entity are entitled to decide whether the entity should make the request?

For instance: is prior approval of the general meeting of shareholders required? Are minority shareholders protected from being squeezed out in the course of such proceedings initiated by major shareholders? Is prior consultation or approval of a Works Council, or any other form of employee consultation, required?

(d) If there is a period of time between filing and the opening decision, does a court have the power to order protective interim measures regarding the estate?

For instance: may a court order a preliminary stay or designate a preliminary administrator in order to protect the estate while investigating the conditions for the opening?

(e) What are the general conditions for the opening/commencement of these insolvency proceedings?

For instance: what are the relevant conditions/triggers that must be satisfied to open the proceedings? Are they always relevant or can they be overturned in order to promote a business rescue (e.g. by court order or creditors' vote)? May the court investigate all relevant facts ex officio*? If not, what information and documents must the applicant submit with their request (e.g. financial ratios, plan proposal, expert testimony about the feasibility of a proposed business rescue, prior consent of creditors)? Does the law provide for adversarial procedure including a hearing and the full body of evidence? What is the evidentiary standard and who bears the burden of proof? Which stakeholders are to be heard? Is the decision to open made* *by an independent impartial court (compare Article 6 European Convention on Human Rights)? Does the law provide any stakeholder with a right to appeal? If so, does any appeal delay the commencement?*

(f) Does the law exclude the use of these insolvency proceedings by debtors whose business is unviable (i.e. economically - rather than merely financially - distressed debtors), and if so how?

(g) What publicity rules apply to filing for, and the opening of, these insolvency proceedings (excluding any requirements imposed by securities law for listed entities)?

For instance: is a request for the opening of the proceedings published? Are creditors actively informed of such a filing? If so, are they alerted by individual notice or by a message containing general information to all creditors? Are there specific publicity requirements for opening insolvency proceedings? If so, are they designed to make proceedings visible in another Member State? Form of publicity: Official Gazette, newspapers, court register, trade register, online? Notification of foreign domiciled creditors?

1.3. *Role of a court, a supervisory judge or other state agency*

1.3.1. Who supervises pre-/insolvency procedures?

For instance: if supervision is not within the primary control of a court, is there another form of supervision, and if yes, by whom (committee of creditors; an agency; an insolvency practitioner, and/or supervision of those practitioners by a body that licenses insolvency practitioners)? In such a case, is there any role for a court?

1.3.2. Where a court has a supervisory function in relation to pre-/insolvency procedures:

(a) What is the nature and scope of the court's role?

For instance: is a court involved in certain (substantial) decisions made by the debtor or the insolvency practitioner, and if so which ones? Can the court give binding instructions to the debtor or the insolvency practitioner, as applicable (for instance on request by particular parties or of its own motion)?

(b) Is this role carried out by a specialist insolvency court, or by a specialist insolvency division within a court, or by a specialist insolvency judge?

(c) Are the actions of the court reviewable, and if so by whom and on what basis?

1.3.3. Who is responsible for devising the rules of practice and procedure that apply to those pre-/insolvency procedures that involve a court?

1.3.4. Which (if any) government agencies are involved in a business rescue, and for what purpose?

For instance: are certain governmental regulators empowered to promulgate regulations or set (non-binding) guidelines in insolvency matters, such as Insolvency Councils, or an Insolvency Service? Which exact tasks are assigned to them? Are the *persons appointed to act independently? Are some agencies tasked with intervention on behalf of government in the rescue of strategically important companies?*

1.4. ***Status, powers and supervision of insolvency practitioners; duties and liabilities of directors***

1.4.1. Do pre-/insolvency procedures involve insolvency practitioners?

1.4.2. In any pre-/insolvency procedure where insolvency practitioners are involved:

(a) Who may be appointed to act as an insolvency practitioner?

For instance: Is the insolvency practitioner required to have a licence or to be registered in an official list or otherwise hold a formal authorisation? Do specific qualification requirements apply to insolvency practitioners (e.g. general experience in business and/or in insolvency law, mandatory (postgraduate) professional training and any continuing training requirements, mandatory membership of a professional association, evidence of a clean criminal record)?

(b) How are they appointed?

For instance: what is the appointment procedure? Is it court driven? Can it be influenced or determined by creditors? Can an appointment be challenged, and if so by whom and on what basis?

(c) What powers do they have in each relevant procedure?

For instance: does the insolvency practitioner have the power to manage the debtor's business, enter into new contracts on its behalf, and sell its assets? Does the insolvency practitioner have the power to compel the production of documents by the debtor or its management or other third parties? Does the insolvency practitioner need prior authorisation (e.g. court or creditor committee approval) for the exercise of his powers, and if so in what circumstances? What sanctions apply if the insolvency practitioner acts without authorisation or outside the remit of his/her powers? If the debtor's assets include shares in a company, can the insolvency practitioner invoke all the company law rights of a shareholder?

(d) What duties do they owe, and to whom? What sanctions apply for breach of duty, and do they include any risk of personal liability?

(e) What reporting obligations do they come under?

For instance: what information needs to be given to creditors or shareholders? What information must be made publicly available (e.g. inventories, public reports, etc.)? How is such information published (e.g. online, at a court) and how often?

(f) How are they remunerated?

For instance: is the remuneration based on an hourly rate, a fixed rate, a percentage of realisations from the debtor's estate or a combination of the foregoing? Is this a general rate or can it be adjusted based on, for example, the experience of the insolvency practitioner and the complexity of the case? Is remuneration affected by the outcome of the procedure (for example, through payment of a 'bonus' for maximisation of recoveries or rescue of the debtor's business)? Does a tariff system exist limiting the maximum amount of remuneration that can be charged by an insolvency practitioner?

1.3.3 Does the law impose any special obligations on the directors of distressed companies, and (if so) what are the consequences of breach?

For instance: is there a legal obligation for directors to file a request for the opening of insolvency proceedings or pre-insolvency proceedings, or are there other important incentives for them to do so (e.g. the application of protective measures, or to prevent personal liability of directors for insolvent trading, etc.)? What are the consequences of delayed or premature filings by directors of distressed companies (civil and/or criminal liability)?

1.3.4 Where the debtor is a corporate entity, once pre-/insolvency proceedings are commenced:

(a) does the law permit debtors to remain in possession, and if so in what circumstances and under which pre-/insolvency procedures? Are there any limitations to their management powers?

(b) are there special sources of liability for directors who act for a debtor-in-possession?

(c) does the law allow individual directors of a debtor-in-possession to be replaced by creditors, special advisors and/or the insolvency practitioner, and if so in what circumstances?

(d) where debtors do not remain in possession, what (if any) residual powers are enjoyed by directors in each relevant pre-/insolvency procedure, and is their exercise subject to any special approval requirements?

For instance: do directors need the consent of an insolvency practitioner, creditors, shareholders or a court to exercise any residual powers?

1.4 How are unsuccessful rescue attempts in pre-/insolvency procedures terminated or converted into other procedures?

1.4.1 Does the law limit the time for which pre-/insolvency procedures can be used to effect a business rescue e.g. the time for the preparation and presentation of a rescue plan?

1.4.2 More generally, in what circumstances would these pre-/insolvency procedures:

(a) be terminated;

(b) converted into another form of procedure, such as (in the case of a corporate debtor) liquidation?

1.4.3 Where any form of insolvency procedure results in the liquidation and dissolution of a debtor (as in the case where the debtor's business is sold on a going concern basis, and the residual entity is wound up) what rules apply where additional assets of the debtor are subsequently discovered?

For instance: can an application be made to restore the company to the register, so that the asset can be recovered and distributed to creditors?

2. <u>Financing a rescue, including critical vendors and other pressures on liquidity; the stay</u>

2.1. ***Direct costs and their reimbursement***

3.1.1. What direct costs are incurred during pre-/insolvency proceedings?

For instance: fee for any IP, court; or legal/ financial advisor involved in proceedings

3.1.2. How are these direct costs met?

For instance: are direct costs discharged from the debtor's assets, and if so in what order of priority? How are direct costs discharged where the debtor's assets are insufficient to meet them?

3.2. ***Rescue finance***

3.2.1. Does the law make special provision for the extension of finance to a debtor after the commencement of pre-/insolvency proceedings?

For instance: can a petitioning party be ordered to make a down-payment on the costs of the proceedings (e.g. the insolvency practitioner's salary)? Which requirements apply to 'post-commencement' finance arrangements, e.g. approval of insolvency practitioner or court of such arrangements or limitation as to amount and/or scope of such finance? Does the law allow a priority or special security (e.g. super-priority) to the provider of post-commencement finance? Are lenders offering new finance in support of a rescue plan confirmed by a court exempted from any civil and criminal liability that may be associated with the continuation of the debtor's business or claw-back risk in any subsequent insolvency?

3.2.2. Where the debtor is a corporate entity:

(a) Does company law or insolvency law contain specific rules for shareholders and/or related companies to financially assist (directly or indirectly) a distressed debtor?

(b) Are shareholder loans subordinated in any subsequent liquidation and distribution of the debtor's assets in insolvency proceedings?

3.3. ***The stay/moratorium***

3.3.1. Where pre-insolvency or insolvency proceedings are used to effect a business rescue, what stay/ moratorium (if any) is provided by the law to protect the debtor's assets, and when and how does it arise?

For instance: does the law provide rules for sealing of the insolvent estate or guarding/security of certain assets. Does the stay arise automatically or only by court order? At what point does it arise? Is there any provisional or interim stay that arises on filing for pre-/insolvency proceedings, prior to the formal commencement?

3.3.2. What is the impact of any such stay/moratorium on:

(a) secured creditors (including the exercise of out-of-court enforcement rights, if any)?

For instance: *is the insolvency practitioner entitled to use, consume or dispose of secured assets during the stay/moratorium? If so: is the prejudiced creditor entitled to reimbursement for damages and/or can he demand substitute security? Can a secured creditor submit an application to the court for leave to enforce their rights as if the stay did not apply?*

(b) pending lawsuits, and unexecuted judgments?

(c) in the case of corporate debtors, petitions for their liquidation?

3.3.3. Are there any exclusions from the stay?

3.3.4. Is the stay subject to any time limit?

3.3.5. Does the law provide any form of stay protection for rescue plan negotiations that are conducted outside formal procedures?

For instance: is a stay available in a case where the debtor is in the course of negotiations leading to a restructuring plan? How does such a stay arise (e.g. court order) and subject to what conditions? e.g. demonstration of the potential benefits of the restructuring; demonstration of certain percentage of creditors interested in further negotiations? What is the maximum duration of such a stay?

4. Executory contracts, including leases, IP-licensing contracts; termination and modification of contracts; transfer of contracts

4.1. ***Executory contracts***

4.1.1. How are executory contracts affected in general by the commencement of pre-/insolvency proceedings?

For instance: who has the power to terminate or continue such contracts, and subject to what conditions?

4.1.2. Are there any specific rules regarding the treatment of hire-purchase and lease contracts (including any lease contracts related to business premises)?

4.1.3. Are there any specific rules regarding the treatment of utility contracts?

For example: does the law restrain utility suppliers from demanding ‘ransom’ payments from the debtor in exchange for the continuing supply of utilities?

4.1.4. Are there specific rules regarding IP, domain name and licensing contracts?

4.2. ***Termination and modification of contract rights***

4.2.1. Does the law address the validity of contractual clauses that purport to entitle the counterparty to terminate or modify contract rights in the event of the debtor’s insolvency or its entry into pre-/insolvency procedures, and if so how?

4.3. ***Transfer of contracts***

4.3.1. Can contracts to which the debtor is a party be transferred to a purchaser of the debtor’s business, and if so how and in what circumstances?

5. Ranking of creditor claims; governance role of creditors

5.1. ***Pre-commencement creditors*:**

5.1.1. How are pre-commencement creditors ranked for the purpose of a distribution of the debtor's assets? Please list in order of priority.

5.1.2. How are these creditor claims verified prior to a distribution?

5.1.3. Which (if any) of these creditor claims enjoy preferential status, and to what extent?

5.1.4. Which (if any) of these creditor claims are subordinated, and to what extent?

5.1.5. Can these creditor claims be traded during the course of pre-/insolvency proceedings?

5.2. ***Post-commencement creditors*:**

5.2.1. Does the law make any special provision for the treatment of debts incurred by a debtor in possession or insolvency practitioner after the commencement of pre-/insolvency proceedings, and if so what does the law provide?

5.2.2. If not, how are such claims treated?

5.3. ***Governance by creditors*:**

5.3.1. Creditors' committee:

(a) Does the law provide for a creditors' committee in pre-/insolvency procedures?

(b) How is such a committee constituted?

(c) What is the role and powers of such a committee?

(d) Are such committee members exposed to personal liability by virtue of acting as members, and if so on what basis?

(e) Are such committee members remunerated, and if so how and on what basis?

(f) To the extent that the law does not provide for a creditors' committee, is there any alternative form of creditor representation?

5.3.2. General meetings of creditors:

(a) Does the law require general meetings of creditors in pre-/insolvency proceedings, and if so when?

(b) What voting rules apply in such meetings?

6. Labour, benefit and pension issues

6.1. *Employment contracts*

6.1.1. Are there any special insolvency, contract, company or labour law provisions regarding the treatment of employment contracts or collective agreements where the employer is in distress or in pre-/insolvency proceedings?

For instance: are there specific rules on the termination of these contracts, e.g. requiring prior court approval, or some notice period? Under which circumstances can an employee sue the insolvent debtor or (where applicable) an insolvency practitioner for wrongful termination?

6.1.2. Does insolvency law provide any special or additional tools for restructuring employment contracts or collective agreements?

For instance: does the law make provision for the employment obligations of the debtor to be transferred to a third party if it buys the debtor's business on a going concern basis?

6.1.3. How are claims regarding unpaid salary entitlements (and any associated benefits e.g. holidays) of employees are treated/protected in pre-/insolvency proceedings?

For instance: do unpaid salary entitlements receive any preferential status in the distribution of the proceeds of the sale of the debtor's assets (see also Question 4.1.1 above)? Does the state provide for another mechanism by which such accrued sums are repaid?

6.2. *Pensions*

6.2.1. Does insolvency law, company law, labour law or social security law provide special protection for the pension entitlements of employees of distressed or insolvent debtors?

For instance: what rules apply to the recovery of pension entitlements accrued by employees of the debtor prior to the commencement of insolvency proceedings but unpaid (see also Question 4.1.1 above)? Does the debtor or insolvency practitioner have any obligation to continue payments that accrue after the commencement of pre-/insolvency proceedings (see also Question 4.2 above)? Do employees enjoy protection through recourse to a state fund where pension entitlements are unpaid?

6.2.2. Can pre-commencement pension entitlements be restructured in a business rescue, and if so how?

7. Avoidance powers, including safe harbour for failed rescue efforts in a later bankruptcy, and avoidance powers in pre-insolvency procedures and out-of-court workouts

7.1. ***Avoidance in insolvency procedures***

7.1.1. Does the law provide for the avoidance of transactions entered into by the debtor prior to the commencement of insolvency proceedings, and if so on what basis?

For instance: does law provide for the avoidance of preference payments to creditors in the lead-up to insolvency? Does law provide for the avoidance of asset transfers at undervalue or in fraud of creditors? Who is empowered to avoid such transactions, and in what circumstances? What is the effect of avoidance?

7.1.2. In which of the insolvency procedures identified in Question 1.1.3 are such avoidance actions available?

7.1.3. How is litigation to pursue an avoidance action financed?

For instance: are state funds or funds from the debtor's estate available to finance particular actions of the insolvency practitioner (e.g. to combat wrongful trading and fraudulent transactions)?

7.1.4. Who has standing to make an application for avoidance of transactions? Can creditors also apply directly to court for a transaction entered into by the debtor to be set aside?

7.2. ***Pre-insolvency procedures and out-of-court workouts***

7.2.1. Are any avoidance powers available in the pre-insolvency proceedings identified in Question 1.1.2 above or in the out-of-court workout procedures identified in Question 1.1.1 above?

For instance: are there avoidance powers that enable some transactions to be set side (for example, fraudulent conveyances) whether or not the debtor is in formal insolvency proceedings?

7.2.2. Does the law provide any special protection from avoidance for agreements achieved in an out-of-court workout or pre-insolvency proceedings?

For instance: if new finance is agreed (by individual arrangement or as part of a rescue plan) are these arrangements exempted from avoidance actions (see also Question 2.2.1 above)?

7. Sales of substantially all of the debtor’s assets on a going-concern basis

7.1. Is such a sale possible in pre-/insolvency proceedings?

7.2. Who prepares/negotiates such a sale and who needs to authorise it? What conditions need to be met?

For instance: if assets are realised by the insolvency practitioner, do they need to be sold by public auction or can they be realised via a private sale? Does a private sale need to be authorised by the court and/or a creditors’ committee? How are creditors protected (e.g. independent valuation of the business, information, authorisation)?

7.3. Is it possible for a ‘pre-packaged’ sale to be achieved? (One in which the contract for sale is negotiated confidentially prior to the commencement of an insolvency procedure, without consultation with all creditors, which takes effect immediately on the commencement of the formal proceedings).

8. Rescue plan issues: procedure and structure; distributional issues

8.1. ***Tools for achieving a plan***

8.1.1. What formal tools are provided by law for the negotiation and sanction of a rescue plan that is capable of binding dissenting stakeholders?

8.1.2. Are these formal tools available in all pre-/insolvency procedures?

8.1.3. Are these formal tools available outside pre-/insolvency procedures?

8.2. ***Scope of plan***:

8.2.1. Creditors:

(a) Which classes of creditor claim can be affected by such rescue plans?

For instance: can secured or preferential creditors be bound by a plan; can prospective or contingent creditors (such as potential tort creditors) be bound by a plan; can fiscal claims owed to the State (e.g. tax) be part of the plan?

(b) Does the law prescribe the number and types of classes of creditors?

For instance: does the number of classes of creditors depend on the individual case or are the classes fixed by law (e.g. secured and unsecured; financial and trade)?

(c) Where secured or preferential creditors can be affected by such rescue plans, does the law afford them any special protection in the negotiation and/or sanction of the plan?

(d) Are all creditors potentially affected by a proposed rescue plan entitled to notice of it, and to participate in negotiations over its content?

(e) May creditors propose a rescue plan, and if so may they do so in competition with a plan proposed by the debtor?

8.2.2. Shareholders:

(a) May shareholders' rights be affected by a rescue plan?

(b) If so, in what circumstances?

8.2.3. Content of plan:

(a) Are there any statutory limitations as to content and/or scope of the plan?

For instance: are there any restrictions on reducing the principal amount of debt owed to creditors in the plan or modifying any secured interest?

8.3. ***Negotiation of the plan***

8.3.1. Who is responsible for proposing a plan and negotiating its terms?

8.3.2. What rights do stakeholders have to notice of the proposed plan, and to participate in negotiations over its content?

8.4. ***Voting***:

8.4.1. Who is entitled to vote on a plan, and who determines this?

8.4.2. How are disputes over voting entitlements resolved?

8.4.3. What modes of voting are permissible?

For instance: are creditors allowed to vote on a restructuring plan via distance means of communication (e.g. on-line)?

8.4.4. Do trading claims ban new creditors from voting?

8.5. ***Confirmation and cram-down***:

8.5.1. What quorum rules apply to a meeting to vote on a plan?

8.5.2. By what majority (in value or number) does a plan have to be approved?

For instance: are stakeholders divided into classes, and is each class required to approve the plan by a particular majority?

8.5.3. Where the debtor is a corporate entity, do shareholders have to approve of the plan?

8.5.4. If the requisite majority of stakeholders or classes of stakeholder approve a plan, is there any further requirement for confirmation of the plan - and if so, what?

For instance: are there requirements for court confirmation, and if so what factors will influence the court to confirm the plan? (e.g. (i) procedural requirements for the notification of affected creditors and for the adoption of the plan are fulfilled, (ii) that the plan does not reduce the rights of dissenting and unknown creditors below what they would reasonably receive if the company went into liquidation, and/or (iii) that the plan does not change the order of priority which would be afforded to creditors in the event of liquidation?).

8.5.5. Does the court examine the overall fairness of the plan including the constitution of classes of creditors for voting purposes?

8.5.6. Can a confirmation order be appealed? Does an appeal delay the implementation of a confirmed plan?

8.5.7. Once confirmed, who does the rescue plan bind?

9. Multiple enterprise/corporate group issues

9.1. Does insolvency law make special provision for insolvent groups of companies in a domestic context? If not, how are such cases handled?

For instance: does the law make special provision for cooperation between insolvency practitioners or courts at domestic level in insolvent group cases?

9.2. Does insolvency law allow for procedural consolidation of domestic insolvency proceedings concerning companies in a corporate group?

For instance: does insolvency law allow for any kind of joint administration (i.e. the consistent procedural joint treatment of the insolvency proceedings), for example through a single court rather than through different courts within the jurisdiction? Can the insolvency practitioner consolidate his or her remuneration over the joint insolvent estates?

9.3. Does insolvency law allow for substantive consolidation of domestic insolvency proceedings across a corporate group into a single procedure, and if so how and subject to what limitations?

For instance: if consolidation takes place to the detriment of individual creditors, are such creditors entitled to compensation out the consolidated estates?

10. Special arrangements for small and medium-sized enterprises (SMEs) including natural persons (but not consumers)

10.1. Does the law make any special provision for resolving distress in SMEs, and if so what (if anything) is the stated purpose of such provisions?

For instance: does the law provide for a simple rescue plan for use by SMEs, or a simplified insolvency procedure?

10.2. In practice, what is the dominant strategy in an SME insolvency? (Winding up or selling the assets on a piecemeal basis? Reorganisation? Going concern sale?).

10.3. In cases where the SME debtor has no realisable assets, are any of the insolvency procedures identified in Question 1.1.3 available? Is a discharge available for the entrepreneur?

2 Questionnaire for National Correspondents for normative reports

Normative report by National Correspondents

Explanatory notes:

In their National Reports, National Correspondents (‘NCs’) identified and described the pre-/insolvency procedures (i.e. those supplied by law) that can be used to achieve a 'business rescue outcome' (broadly construed) in their jurisdiction, and described their key features. NCs also identified any legal rules that facilitate the achievement of a business rescue outcome out-of-court (e.g. through a work-out, not supplied by law). This memo relates to the Normative Report.

In their Normative Report, NCs are asked to critically evaluate these procedures and rules, and any other aspect of the legal framework that could be said to inhibit the achievement of a business rescue outcome. NCs are invited to structure their response using the questions below, but are warmly encouraged to flag any additional issues that are not caught by these questions but should be noted by the Reporters.

Please return the normative report by **[Submission date]** via email to: businessrescue@europeanlawinstitute.eu.

As in the Questionnaire:

- *business rescue* is to be construed broadly to encompass both the rescue of the debtor (such that the entity itself survives) and the rescue of the debtor’s business on a going concern basis (whether or not the business continues to be carried on in the same entity). It should be contrasted with the sale of the debtor’s assets on a piecemeal or break-up basis;
- *debtor* is to be construed to include sole traders and entrepreneurs as well as corporate entities, but to excludes references to banking and insurance debtors, and references to consumer bankruptcies.

Additionally:

pre-/insolvency procedures have the same meaning as in the Questionnaire (i.e. those pre-insolvency and insolvency procedures that can be used to achieve a business rescue outcome).

Questions:

1. *Would you, considering the state of insolvency law in your country, say that the law (both substantive and procedural) facilitates or impedes the resolution of financial distress of a business debtor? Please consider it both for:*
    a) *the restructuring of assets or liabilities of a financially distressed business?*
    b) *the sale of a distressed business on a going concern basis?*

    Please explain your answer.

2. *Does the existing domestic law impede or encourage in any way:*
    a) *the negotiation of informal solutions to financial distress, for example the negotiation of a non-binding standstill by some creditors;*
    b) *the negotiation of contractual solutions to distress, either* ex ante *(i.e. parties pre-committing themselves to a restructuring process in the event that distress arises*) *or* ex post *(i.e. once distress arose)*?

3. *In relation to the pre-/insolvency procedures you have identified:*
    a) what kind of debtors are most likely to have recourse to these procedures to achieve a business rescue outcome?
    b) *what would be their typical debt capital structure (e.g. would it be fragmented, or concentrated as is the case where there is a dominant lender holding a majority of the claims)?*
    c) *overall, would you say that these procedures are suitable or unsuitable for achieving a business rescue outcome for this kind of debtor?*

4. *Should the pre-/insolvency procedures you identified be reformed, and if so why and how?*

    In answering, please consider both substantive law and rules of practice and procedure (e.g. rules governing standing, costs, interim relief, appeals) as possible candidates for reform.

5. *Is there local demand for (or opposition to) the reform of the rules and procedures that govern business rescues in your jurisdiction, and if so by which constituencies?*

6. *To the extent that you have identified a need for reform to domestic rules or procedures in your answers above, do you believe that such reforms would best be achieved:*
    a) purely at the domestic level;
    b) through some form of harmonisation of these types of rules/procedures at EU level?
    c) through some form of soft law via an 'ELI Legislative Guide' (focusing at national legislation) as envisioned by the Reporters?

    Please explain your answer.

7. *More generally, do you regard proposals for harmonisation at EU level (such as the Commission's Recommendation of 12 March 2014, which encourages greater coherence between national insolvency frameworks [recital 11]) in the field of business rescue as:*
    a) *sensible in principle?*
    b) *feasible in practice?*

Please explain your answer.

8. *In your view, what kind of output from the Reporters would be most valuable, and why?* Outcomes envisioned by the Reporters in their project proposal are: a legislative guide, and (if justified) a legislative proposal (probably: Directive). Other suggestions are welcome. Such outputs are obviously additional to the publishing of the reports of the National Correspondents.