THE

Restructuring Review

Tenth Edition

Editor
Christopher Mallon
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PREFACE

I am very pleased to present this tenth edition of The Restructuring Review. As with the previous editions, our intention is to help general counsel, private practice lawyers and the public sector understand the conditions prevailing in the global restructuring market in 2017, with a view to the coming year, and to highlight some of the more significant legal and commercial developments and trends that have been evident in recent years and that are expected to be significant in the future.

The global economic situation continues to be uncertain, presenting an interesting market for restructuring and insolvency practitioners. While, as in previous years, politics continues to throw up surprising and disruptive events as populations grapple with the competing forces of globalisation and culture, some of the more pessimistic predictions of recent times have not, in fact, come to pass.

Nevertheless, as the political implications of, among other factors, Brexit and mass immigration continue to be worked out in Europe and beyond, at a more fundamental level the realisation is dawning on many that a turn in the economic cycle may be approaching and that the severe economic crisis of 2008–9 may not be an isolated event. For example, the Bank for International Settlements has recently warned that the global economy is trapped in a perpetual boom–bust cycle and that, as debt levels continue to swell, a severe reckoning may be imminent.

Beyond finance, the perennial tensions surrounding the Middle East, Russia and South East Asia show no indication of being resolved. In a rapidly changing global environment, the tentative peace between the great powers that has prevailed since the mid-twentieth century seems ever more fragile.

While, of course, no credible predictions as to the consequences of the above factors for insolvency and restructuring activity are possible, past experience has taught us that where there is uncertainty and stress there is a healthy restructuring market. As such, the tenth edition of this work continues to be relevant and important, in particular, as a result of the cross-border nature of many corporate restructurings.

I would like to extend my gratitude to the contributors from some of the world’s leading law firms who have given such valuable support and cooperation in the preparation of this work, and to our publishers, without whom this work would not have been possible.

Christopher Mallon
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London
July 2017
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

It is well documented that Australia emerged from the turbulent times that followed the collapse of Lehman Brothers in comparatively good shape. The market has in recent times, however, become increasingly susceptible to financial stresses caused by factors at both domestic and international levels. At the international level, such factors include decreased demand and consumption emanating from China and the changes to capital requirements resulting from the Basel Accords. On the domestic front, businesses and individuals have focused on reducing their debt burden; however, at the consumer level, due to record low interest rates and appetite in the housing market, individuals are taking on more debt.

Within this landscape, the secondary debt trading market has steadily grown, and this has seen a growth in consensual restructurings, particularly where borrowers have found it difficult to refinance. The relative stability of the Australian banking sector, the robust prudential regulations imposed on Australian banks and a willingness of par lenders to exit their positions – often at considerable discounts – has promoted increased activity in the secondary debt trading market since 2009, which reached peak levels in 2012.

This increased willingness to trade has seen a number of international players enter the market, commonly in the form of credit funds and private equity funds. These funds can have very different goals, time frames and strategies from the former dominant local financial institutions. In combination, these circumstances have also given rise to an increase in the pursuit of ‘debt-for-equity’ restructurings. Given that the ultimate goal of this strategy is often ownership of the business, credit fund participants are more conscious of enterprise value destruction, and there has been a reluctance to proceed to formal insolvency in these circumstances (particularly at the higher end of the market). As a result, schemes of arrangement are becoming an increasingly common mechanism through which to effect these strategies, although the threat of a formal insolvency process, such as receivership or voluntary administration, is often used as a bargaining tool in restructuring negotiations. Having said that, administration and deeds of company arrangement are being used more frequently to effect debt-for-equity swaps.

The increase in debt trading over recent times has led to the debt in restructured entities being held by credit funds and other institutions, and not necessarily by traditional lenders. The restructurings of Centro, Alinta, Redcape, I-Med, Colorado and, more recently, the Nine Entertainment Group, Atlas Iron, Billabong, Mirabela Nickel, Nexus Energy, Emeco, Boart Longyear, BIS Industries and Slater and Gordon, have all had a large number of credit

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1 Dominic Emmett is a partner and Jessica Arscott is a senior associate at Gilbert + Tobin.
and private equity fund participants. This has seen a consequential change in dynamics within lender groups, as credit funds are more willing than traditional banks to take equity positions. This has begun to evolve in recent times, however, and certain banks are now more willing to consider quasi-equity positions in the Australian market. Traditional lenders are also increasingly requiring the issue of warrants in return for their agreement to restructure debt facilities.

While foreign banks with exposures in Australia (predominantly from the United States, the United Kingdom and continental Europe) took active steps after the global financial crisis to reduce their exposure in Australia, this has largely stabilised and foreign banks are now starting to show interest in returning to Australia.

The past couple of years saw a number of loan portfolio sales whereby both Australian and foreign banks sought to exit their potential exposures completely. Some key examples have included the sale of Lloyd’s businesses, GE Capital’s book, Barclays’ book and the ANZ/Esanda book. These sales processes were very competitive, and involved both credit funds and Australian institutional banks.

Economic indicators continue to paint a patchy outlook for Australia’s economy in the near term. There are areas of increased vulnerability in the marketplace, particularly as the resources boom continues to slow, commodity prices continue their decline and mining investment steadily contracts. Corporate collapses are occurring throughout Australia due in large part to slackening demand, cash-flow concerns and an inability to refinance at the same leverage levels. Some of the most notable collapses of the past year have included Arrium, Dick Smith, BBY Ltd and Queensland Nickel.

Sectors that have been hit particularly hard in recent times include mining and commodities, and service-based businesses associated with the mining sector, retail (which is a reflection of broader factors playing out on a global scale, such as an increased focus on savings and shoppers turning to online purchasing) and the construction sector, which has been a victim of cash-flow problems, particularly as government spending has slowed. There is also increased evidence of consolidation in the mining sector, and this is expected to continue as commodity prices remain volatile and companies continue to take cost-cutting steps to raise efficiency. Mining companies are increasingly conscious of improving efficiency of production as margins continue to drop. Increased restructuring activity is expected in each of these categories and, in particular, in mid-market mining projects and mining services companies in Western Australia and Queensland.

A significant proportion of external administration appointments have resulted from borrowers breaching financial covenants, failing to meet an amortisation payment or an inability to refinance debt facilities at the end of their term. In these circumstances, where a mutually acceptable deal has not been reached between equity, management and the lenders, directors will invariably opt to appoint a voluntary administrator or invite the secured lenders to appoint a receiver over the company’s assets. It would, however, be rare for the board of a company with secured lenders to appoint a voluntary administrator without first inviting the secured lenders to appoint a receiver, or to make a dual appointment of both a voluntary administrator and receiver in a coordinated fashion.

Curiously, during this period secured lenders have granted far more leniency to borrowers, and have been more willing to work through restructurings to ensure businesses remain viable as a going concern. Put another way, formal appointments are often seen as
the least attractive option, and, therefore, the rate of appointments could have been higher if lenders had been quicker to commence external administration, as they were in the recession of the early 1990s.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Formal procedures

The formal procedures available under Australian law are:

- **a** receivership (both private and court-appointed);
- **b** voluntary administration;
- **c** a deed of company arrangement (DOCA);
- **d** provisional liquidation;
- **e** liquidation; and
- **f** a court-sanctioned scheme of arrangement between creditors and the company.

For receivership, voluntary administration, DOCA and liquidation, the individual appointed must be an independent registered liquidator, except in the case of a members’ voluntary liquidation.

Receivership

The main role of a receiver is to take control of the relevant assets, and realise those assets for the benefit of the secured creditors. One or more individuals may be appointed as a receiver or a receiver and manager of the relevant assets. Despite some historical differences, in practice it is difficult to distinguish between the two roles and most security interests will allow for the appointment of either. Receivers are not under an active obligation to unsecured creditors on appointment, although they do have a range of duties under statute and common law. Despite being appointed by the secured creditors, a receiver is not obliged to act on the instructions of the secured creditors. A receiver must, however, act in their best interests, and this will invariably lead a receiver to seek the views of secured creditors on issues that are material to the receivership.

There are two ways in which a receiver or receiver and manager may be appointed to a debtor company. The most common manner is pursuant to the relevant security document granted in favour of the secured creditor when a company has defaulted and the security has become enforceable. Far less common in practice is the appointment of a receiver pursuant to an application made to the court. Court appointments normally take place to preserve the assets of the company in circumstances where it may not be possible to otherwise trigger a formal insolvency process. Given the infrequency of court-appointed receivers, however, this chapter focuses on privately appointed receivers.

For a privately appointed receiver, the security document itself will entitle a secured party to appoint a receiver, and will also outline the powers available (supplemented by the statutory powers set out in Section 420 of the Corporations Act 2001 (Cth) (the Act)). Generally, a receiver has wide-ranging powers, including the ability to operate, sell or borrow against the secured assets. The appointment is normally effected contractually through a deed of appointment and indemnity, and the receiver will be the agent of the debtor company, not the appointing secured party.
On appointment, a receiver will immediately take possession of the assets subject to the security. Once in control of the assets, the receiver may elect to run the business if he or she is appointed to oversee all or substantially all of the assets of a company. Alternatively, and depending on financial circumstances, a receiver may engage in a sale process immediately. While engaging in a sale process, a receiver is under a statutory obligation to obtain market value or, in the absence of a market, the best price obtainable in the circumstances. This obligation is enshrined in Section 420A of the Act. It is this duty that has posed the most significant stumbling block to the adoption of pre-packaged restructuring processes through external administration that have been seen in, for example, the UK market. This is because of the inherent concern that a pre-packaged restructure that involves a sale of any asset without testing against the market could be seen as a breach of the duty under Section 420A. Once a receiver has realised the secured assets and distributed any net proceeds to the secured creditors (returning any surplus to the company or later ranking security holders), he or she will retire in the ordinary course.

**Voluntary administration**

The concept of voluntary administration was introduced in 1993. Voluntary administration, unlike receivership, is entirely a creature of statute, and its purpose and practice is outlined in Part 5.3A of the Act. Voluntary administration has been compared with the Chapter 11 process in the United States, but unlike the Chapter 11 process, voluntary administration is not a debtor-friendly process. In a voluntary administration, the creditors control the final outcome to the exclusion of management and members. The creditors ultimately decide on the outcome of the company, and it rarely involves returning management responsibilities to the former directors.

The purpose of Part 5.3A is to either:

- **a** maximise the chances of the company, or as much as possible of its business, to continue in existence; or
- **b** if the first option is not possible, achieve a better return for the company’s creditors and members than would result from an immediate winding up of the company.

There are three possible ways an administrator may be appointed under the Act:

- **a** by resolution of the board of directors that, in their opinion, the company is, or is likely to become, insolvent;
- **b** a liquidator or provisional liquidator of a company may, in writing, appoint an administrator of the company if he or she is of the opinion the company is, or is likely to become, insolvent; and
- **c** a secured creditor who is entitled to enforce security over the whole or substantially whole of a company’s property may, in writing, appoint an administrator if the security interest is over the property and is enforceable.

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2 Often referred to as a ‘pre-pack’, this is where a restructure is developed by the secured lenders prior to the appointment of a receiver, and is implemented immediately or very shortly after the appointment is made.
3 Section 435A of the Act.
4 Section 436A of the Act.
5 Section 436B of the Act.
6 Section 436C of the Act.
An administrator has wide powers and will manage the company to the exclusion of the existing board of directors. Once an administrator is appointed, a statutory moratorium is activated, which restricts the exercise of rights by third parties under leases and security interests\(^7\) and in respect of litigation claims, which is designed to give the administrator the opportunity to investigate the affairs of the company, and either implement change or be in a position to realise value, with protection from certain claims against the company.

There are two meetings over the course of an administration critical to the outcome of the administration. Once appointed, an administrator must convene the first meeting of creditors within eight business days (at such meeting, the identity of the voluntary administrator is confirmed, the remuneration of the administrator is approved and a committee of creditors may be established). The second creditors’ meeting is normally convened 20 business days after the commencement of the administration (this may be extended by application to the court). At the second creditors’ meeting, the administrator provides a report on the affairs of the company to the creditors and outlines the administrator’s views as to the best option available to maximise returns. There are three possible outcomes that can be put to the meeting: entry into a DOCA with creditors (discussed further below); winding up the company; or terminating the administration.\(^8\)

The administration will terminate according to the outcome of the second meeting (i.e., either by progressing to liquidation, entry into a DOCA or returning the business to operate as a going concern (although this is rare)). When the voluntary administration terminates, a secured creditor that was estopped from enforcing a security interest due to the statutory moratorium becomes entitled to commence steps to enforce that security interest unless the termination is due to the implementation of a DOCA approved by that secured creditor.

**Deed of company arrangement**

A DOCA is effectively a contract or compromise between the company and its creditors. Although closely related to voluntary administration, it should, in fact, be viewed as a distinct regime where the rights and obligations of the creditors and company will differ from those under a voluntary administration.

The terms of a DOCA may provide for, *inter alia*, a moratorium of debt repayments, a reduction in outstanding debt, and the forgiveness of all or a portion of the outstanding debt. It may also involve the issuance of shares, and can be used as a way to achieve a debt-for-equity swap through the transfer of shares either by consent or with leave of the court.\(^9\) This was how the successful debt for equity restructure was achieved in *Mirabela*.

Entering into a DOCA requires the approval of a bare majority of creditors both by value and number voting at the second creditors’ meeting. A DOCA will bind the company, its shareholders, directors and unsecured creditors. Secured creditors can, but do not need to, vote at the second creditors’ meetings, and typically only those who voted in favour of

\(^7\) There is, however, an exception to the moratorium on the exercise of rights under security interests in the case of a secured creditor that has security over all or predominantly the whole of the assets of the company.

\(^8\) Section 439C of the Act.

\(^9\) Section 444GA of the Act.
the DOCA at the second creditors’ meeting are bound by its terms.\textsuperscript{10} Unlike a scheme of arrangement, court approval is not required for a DOCA to be implemented provided it is approved by the requisite majority of creditors.

Upon execution of a DOCA, the voluntary administration terminates. The outcome of a DOCA is generally dictated by the terms of the DOCA itself. Typically, however, once a DOCA has achieved its goal it will terminate. If a DOCA does not achieve its goals or is challenged by creditors it may be terminated by the court.

**Provisional liquidation**

A provisional liquidator may be appointed by the court in a number of circumstances. The most commonly used grounds include:

\begin{itemize}
  \item [a] insolvency;
  \item [b] where an irreconcilable dispute at a board or shareholder level has arisen that affects the management of the company;
  \item [c] where the shareholders of the company have, by special resolution, resolved that it be wound up; or
  \item [d] if the court is of the opinion that it is just and equitable to do so.
\end{itemize}

A creditor, a shareholder or the company itself has standing to apply for the appointment of a provisional liquidator, although in most cases a creditor will be the applicant. A provisional liquidator will normally only be appointed by the court when there is a risk to the assets of a company prior to a company formally entering into liquidation. As such, a provisional liquidator is normally only given very limited powers (i.e., the power to take possession of the assets), and the main role of the provisional liquidator is to preserve the status quo.

A court determines the outcome of a provisional liquidation. It may order either that the company move to a winding up, with the appointment of a liquidator, or that the appointment of the provisional liquidator is terminated.

**Liquidation**

Liquidation is the process whereby the affairs of the company are wound up and its business and assets are realised for value. A company may be wound up voluntarily by its members if solvent or, alternatively, if it is insolvent, by its creditors or compulsorily by order of the court.

**Voluntary liquidation (members and creditors)**

The members of a solvent company may resolve that a company be wound up if the board of directors is able to give a 12-month forecast of solvency (i.e., an ability to meet all its debts

\textsuperscript{10} There have been two cases challenging the validity of the widely held view that secured creditors are not ‘bound’ by a DOCA unless they vote in favour of it. In *Australian Gypsum Industries Pty Ltd v Dalesun Holdings Pty Ltd* [2015] WASCA 95 and *Re Bluenergy Group Limited* [2015] NSWSC 977, it was held that a DOCA can (if so expressed) have the effect of extinguishing the debt of a secured creditor that did not vote in favour of the DOCA pursuant to s.444D(1) of the Act. However, this extinguishment is subject to the preservation of the secured creditor’s ability (by virtue of s.444D(2) of the Act) to realise or deal with its security in respect of its proprietary interest in the secured property and to the extent that its debt was provable and secured assets were available at the date that debt would otherwise be released under the DOCA, without requiring that that debt be preserved into the future or for other purposes.
within the following 12 months). If not, or if the company is later found to be insolvent, the creditors take control of the process. Creditors may resolve at a meeting of creditors to wind up the company and appoint a liquidator (this may take place at the second meeting of creditors during an administration). If the requisite approvals are obtained in either a members’ voluntary winding up or a creditors’ voluntary winding up, a liquidator is appointed.

**Compulsory liquidation**

The most common ground for a winding-up application made to the court is insolvency, usually indicated by the company’s failure to comply with a statutory demand for payment of a debt or a judgment debt. Following a successful application by a creditor, a court will order the appointment of a liquidator.

In both a voluntary and compulsory winding up, the liquidator will have wide-ranging powers, including the ability to challenge voidable transactions and take control of assets. Generally, a liquidator will not run the business as a going concern, unless it will ultimately result in a greater return to stakeholders. During the course of the winding up, the liquidator will realise the assets of the company for the benefit of its creditors and, to the extent of any surplus, its members. At the end of a winding up, the company will be deregistered and cease to exist as a corporate identity.

**Scheme of arrangement**

A scheme of arrangement is a restructuring tool that sits outside formal insolvency; that is, the company may become subject to a scheme of arrangement whether it is solvent or insolvent.

A scheme of arrangement is a proposal put forward (with input from management, the company or its creditors) to restructure the company in a manner that includes a compromise of rights by any or all stakeholders. The process is overseen by the courts and requires approval by all classes of creditors. In recent times, schemes of arrangement have become more common, in particular for complex restructurings involving debt-for-equity swaps in circumstances where the number of creditors within creditor stakeholder groups may make a contractual and consensual restructure difficult.

A scheme of arrangement must be approved by at least 50 per cent in number and 75 per cent in value of creditors in each class of creditors. It must also be approved by the court in order to become effective.

The outcome of a scheme of arrangement is dependent on the terms of the arrangement or compromise agreed with the creditors but, most commonly, a company is returned to its normal state upon implementation as a going concern but with the relevant compromises having taken effect.

The scheme of arrangement process does, however, have a number of limiting factors associated with it, including cost, complexity of arrangements (i.e., class issues), uncertainty of implementation, timing issues (i.e., because it must be approved by the court it is subject to the court timetable and cannot be expedited) and the overriding issue of court approval (a court may exercise its discretion to not approve a scheme of arrangement, despite a successful vote, if it is of the view that the scheme of arrangement is not equitable). These factors explain why schemes of arrangement tend only to be undertaken in large corporate restructures and in scenarios where timing is not fatal to a restructure.
ii Rights of enforcement

Secured creditors may enforce their rights in every form of external administration. During a voluntary administration, a secured creditor with security over all or substantially the whole of the company’s property may enforce its security, provided it does so within 13 business days of receiving notice of appointment of the voluntary administration, or with leave of the court or consent of the administrator. In addition, if a secured creditor takes steps to enforce its security before the voluntary administration commences, it may continue to enforce its security.

Where a company pursues a DOCA, a secured creditor who did not vote in favour of such a proposal will have the ability to enforce its security interests once the DOCA becomes effective. If a voluntary administration otherwise terminates, a secured creditor may also commence steps to enforce its security interest upon termination.

iii Directors’ duties in distressed situations

Case law in Australia, particularly the *Westpac Banking Corporation v. Bell Group Ltd (in liq)* case (*Bell*), has reaffirmed the position that a director must be increasingly mindful of the interests of creditors as a company approaches insolvency. A director’s duty to creditors arises by operation of the well-established fiduciary duty owed by a director to the company more generally. When a company is solvent, the interests of the shareholders are paramount, and conversely, as recent case law has emphasised, when a company is near insolvency or of doubtful solvency, the interests of the creditors become increasingly relevant. It is important to emphasise that the duty to take into account creditors’ interests is owed to the company, not to the creditors *per se*.

The extent of this duty continues to be an evolving area of the law. It is, however, now well established under Australian law that directors must at the very least have regard to the interests of creditors when a company is in financial distress or insolvent. As noted by Lee AJA in *Bell*:

> At the point of insolvency, or the pending manifestation of insolvency, the duty to act in the best interests of each company was of central importance for the companies to comply with statutory obligations and the obligation of the companies not [to] prejudice the interests of creditors.

Further, it has been suggested that when the solvency of a company is doubtful or marginal, it would be a misfeasance to enter into a transaction that the directors ought to know is likely to lessen the company’s value if to do so will cause a loss to creditors. Directors should not, for instance, allow the company to enter into commitments that it clearly will not be in a position to meet or that may prejudice the interests of creditors generally.

It is also conceivable that directors could be held liable for loss suffered as a result of a transaction during a period of insolvency or near insolvency that is clearly value-dilutive. Transactions that are challenged, and that could put directors at risk, normally involve shareholders, directors and related parties receiving a benefit to the detriment of the company.

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11 See footnote 10
13 *Spies v. the Queen* [2000] HCA 43.
It has, however, been noted that there are limitations on this duty to creditors, and specifically that it is ‘a duty of imperfect obligation owed to creditors, one which the creditors cannot enforce save to the extent that the company acts on its own motion or through a liquidator’.  

Put another way, a breach of such a duty does not give rise to a direct right of action that may be brought by the creditors against the directors; rather, it gives rise to a right of action that must be undertaken either by the company itself or a liquidator, if and once appointed.

**Insolvent trading**

Directors may be held liable for new debts incurred by a company trading while cash-flow insolvent. This potential liability does not extend to debts incurred prior to the date a company became cash-flow insolvent, or recurring payments that become due after that date under the terms of preexisting arrangements such as rent or interest (i.e., when the liability to pay such amounts already existed at the time of insolvency).

In terms of a director’s personal liability, a court may make an order requiring the director to compensate the company for loss arising out of the insolvent trading, prevent a director from managing a corporation for a period of time and, in rare circumstances where the failure to prevent insolvent trading is ruled as a result of dishonesty, a fine of A$200,000 may be levelled against the offending director.

In certain circumstances, the insolvent trading provisions will also extend to holding companies.  

The appointment of a voluntary administrator or a liquidator by the directors protects a director from any claim that he or she allowed the company to trade while insolvent in respect of any debts incurred after the date of such appointment.

**iv Clawback**

Under Australian law, transactions will only be vulnerable to challenge when a company does in fact enter into liquidation. A liquidator only has the ability to bring an application to the court to declare certain transactions void. In the report to creditors at the second creditors’ meeting, a voluntary administrator may identify potentially voidable transactions, but he or she is not empowered to pursue a claim in respect of such transaction. Any such claim must be brought by a subsequently appointed liquidator.

There are several types of transactions that can be found to be voidable:

- unreasonable director-related transactions;
- unfair preferences;
- uncommercial transactions;
- transactions entered into to defeat, delay or interfere with the rights of any or all creditors on a winding up; and
- unfair loans.

Transactions in categories (b), (c) and (d) will only be voidable where they are also found to be ‘insolvent transactions’, that is, transactions that occurred while the company was cash-flow insolvent, or contributed to the company becoming cash-flow insolvent. Each type

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14 Gummow J in *Re New World Alliance Pty Ltd (Receiver and Manager Appoint); Sycotex Pty Ltd v. Baseler (No. 2)* [1994] 51 FCR 425 (and cited with approval in *Bell*).

15 Section 588V of the Act.
of voidable transaction has a different criterion and must have occurred during certain time periods in the lead up to administration or liquidation. The relevant time period is generally longer if the transaction involves a related party.

Upon the finding of a voidable transaction, a court may make a number of orders, including directions that the offending person pay an amount equal to some or all of the impugned transaction; directions that a person transfer the property back to the company; or directions that an individual pay an amount equal to the benefit received.

III AUSTRALIAN INSOLVENCY LAW REFORM

There have been two significant developments in Australian insolvency law reform in 2016 and 2017.

i Insolvency Law Reform Act 2016

The Insolvency Law Reform Act 2016 (Cth) (ILRA) was introduced with a split commencement, with some provisions starting on 1 March 2017 and the remainder starting on 1 September 2017. The ILRA makes a number of amendments to the Act, Bankruptcy Act 1966 (Cth) (Bankruptcy Act) and other pieces of legislation, including the insertion of:

a a new Schedule 2 into the Act, known as the Insolvency Practice Schedule (Corporations), which is designed to: (1) regulate persons registered as liquidators; and (2) regulate external administrations consistently and to give greater control to creditors; and

b Schedule 2 into the Bankruptcy Act, known as the Insolvency Practice Schedule (Bankruptcy), which is designed to: (1) regulate persons registered as bankruptcy trustees; and (2) regulate the administration of regulated debtors’ estates consistently and to give greater control to creditors.

A number of other legislative instruments have also been introduced to give full effect to the ILRA, namely the:

a Insolvency Practice Rules (Corporations) 2016, which provides a range of rules regarding the external administration of companies and the registration and discipline of external administrators;

b Insolvency Practice Rules (Bankruptcy) 2016, which provides a range of rules regarding the external administration of private individuals and the registration and discipline of bankruptcy trustees;

c Corporations and Other Legislation Amendment (Insolvency Law Reform) Regulation 2016, which amends the Bankruptcy Regulations 1996 (Cth), Corporations Regulations 2001 (Cth) and other relevant regulations consequential on the Insolvency Practice Rules. This instrument also provides for the partial delay of certain corporate law amendments under the ILRA;

d Insolvency Law Reform (Transitional Provisions) Regulation 2016, which provides for the partial delay of certain personal insolvency amendments under the ILRA; and

e Corporations (Fees) Amendment Regulation 2016, which allows for the change of fees required due to the Insolvency Practice Rules (Corporations) 2016.

Although the ILRA and Insolvency Practice Rules (Corporations) 2016 do not make wholesale changes to Australia’s corporate insolvency laws, they will complicate the day-to-day operation of external administrations and bolster creditor information rights.
On 3 May 2017, the federal government released further draft legislation of amendments to the Act and Bankruptcy Act to refine aspects of the ILRA. Public submissions regarding that draft legislation closed on 17 May 2017.

ii  Safe harbour and ipso facto reforms

On 1 June 2017, following an extensive public consultation on draft legislation, the government introduced the Treasury Laws Amendment (2017 Enterprise Incentives No. 2 Bill) 2017 (the Bill) into the Federal Parliament. The Bill contains two major reforms to Australia’s insolvency laws:

a  a new safe harbour from civil liability for insolvent trading for directors seeking to restructure financially distressed or insolvent companies (safe harbour provisions); and

b  restrictions on the enforcement of certain ipso facto rights (ipso facto provisions).

The Bill was passed by the House of Representatives (after a third reading) on 22 June 2017. The Senate referred the provisions of the Bill to the Senate Economics Legislation Committee, whose report, tabled on 8 August, recommended that the Bill be passed unamended.

Safe harbour provisions

The Bill introduces a new Section 588GA into the Act, which provides that Section 588G(2) of the Act (i.e., the provision that makes directors liable for debts incurred by a company whilst it is insolvent) will not apply if, after starting to suspect the company may become or be insolvent, the director starts developing one or more courses of action that are ‘reasonably likely to lead to a better outcome for the company’ than the immediate appointment of an administrator or liquidator to the company.

In determining whether a course of action is ‘reasonably likely to lead to a better outcome for the company’, the Bill provides that regard may be had as to whether the director:

a  has properly informed himself or herself of the company’s financial position;

b  is taking appropriate steps to prevent any misconduct by officers or employees of the company that could adversely affect the company’s ability to pay all its debts;

c  is taking appropriate steps to ensure that the company is keeping appropriate financial records consistent with the size and nature of the company;

d  is obtaining advice from an appropriately qualified entity who has been given sufficient information to provide appropriate advice; or

e  is developing or implementing a plan for restructuring the company to improve its financial position.

Accordingly to the explanatory memorandum, ‘reasonably likely’ requires that there is a chance of achieving a better outcome that is not fanciful or remote, but is ‘fair’, ‘sufficient’ or ‘worth noting’.

It is important for directors to appreciate that:

a  the safe harbour provisions do not provide protection in respect of all debts. The provisions only covers debts that are:

• incurred directly or indirectly in connection with any such course of action. According to the explanatory memorandum this would include ordinary trade debts incurred in the usual course of business as well as debts taken on for the specific purpose of affecting a restructure (e.g., fees of a professional turnaround adviser); and
Australia

- incurred during the period commencing at the time the director starts to develop one or more courses of action after starting to suspect that the company may become or be insolvent (start time) and ending at the earliest of the following times: (1) the end of a reasonable period after the start time, if the director fails to take any such course of action within that reasonable period; (2) when the director ceases to take any such course of action; (3) when any such course of action ceases to be reasonably likely to lead to a better outcome for the company; and (4) the appointment of an administrator or a liquidator to the company;

b further, directors cannot rely upon the safe harbour provisions:
- in respect of a particular debt if at the time the debt is incurred, the company is failing to pay employee entitlements when due or comply with its tax reporting obligations, and that failure amounts to less than substantial performance or constitutes one of two or more failures by the company to do any or all of those matters during the preceding 12 months; or
- in respect of any debt if after the debt is incurred, the director substantially fails to comply with certain statutory duties to provide information to any controller, administrator or liquidator that is subsequently appointed to the company, unless, in each case the court orders otherwise, in circumstances where the court is satisfied that the failures were due to exceptional circumstances or that making such orders is in the interests of justice;

c directors will not be permitted to rely upon company books and information in insolvent trading proceedings, if they have previously breached their statutory duties to provide these materials to a controller, administrator or liquidator that is ultimately appointed to the company. This requirement is designed to ensure that where a company eventually goes into controllership, administration or liquidation, the directors do not try to prevent the controller, administrator or liquidator from investigating the company’s activities, by withholding books or information about the company. This rule will not apply if:
- the director did not possess the books or information at the relevant time and there were no reasonable steps the director could have taken to obtain the books or information;
- the controller, administrator or liquidator (as relevant) failed to inform the director of the effect of failing to comply with any request for materials; or
- the court so orders, where the court is satisfied that the failure was due to exceptional circumstances or making such an order is in the interests of justice.

The Bill also provides a safe harbour for holding company liability for the insolvent trading of a subsidiary.

The safe harbour provisions will commence the day after the Bill receives Royal Assent and will apply in relation to debts incurred at or after that commencement.

Ipso facto provisions

If enacted, the Bill will introduce two kinds of stay provisions:

a an automatic stay on the enforcement of certain *ipso facto* rights; and
stay orders in respect of a potentially broader range of rights (e.g., termination for convenience rights), where a court is convinced such rights are or might be exercised or there is a threat that they might be exercised solely because the company has entered administration or a scheme of arrangement.

**Automatic stay for ipso facto rights**

The Bill will introduce new provisions into the Act that create an automatic stay on the enforcement of contractual rights that are triggered merely because:

- the company has publicly announced that it will apply for, has in fact applied for or become subject to, a scheme of arrangement;
- a receiver or other managing controller has been appointed to the whole or substantially the whole of the company’s property;
- an administrator has been appointed to the company; or
- the company’s financial position or any other reason prescribed in the regulations, where one of the above-mentioned circumstances has occurred.

The automatic stay will operate during the following stay periods:

- in the case of a scheme designed to avoid the company being wound up in insolvency, during a period that starts when the company publicly announces that it will or otherwise does in fact, apply to hold a scheme meeting under Section 411, and ends:
  - if the company fails to make the announced application – at the end of three months after the announcement, or such longer period as is ordered by a court;
  - when the application is withdrawn or rejected by the court; or
  - when the scheme ends, unless this occurs because the company is to be wound up, in which case when the company’s affairs have been fully wound up;
- in the case of a receivership or managing controllership, during a period that starts when the receiver or managing controller is appointed and ends when the receiver’s or managing controller’s control ends or such later time as is ordered by the court;
- in the case of an administration, during a period that starts when the company comes under administration and ends the latest of:
  - when the administration ends;
  - if an application is made before the administration ends to extend the period of the stay – when the court so orders; or
  - if the administration ends because of a resolution or order for the company to be wound up – when the company’s affairs have been fully wound up.

In addition, and notwithstanding the above-mentioned stay periods, the Bill also makes provision for rights to remain unenforceable indefinitely against the company (i.e., beyond the expiry of the relevant stay period), where the reason for seeking to enforce the right is:

- the company’s financial position before the end of the stay period;
- the fact that the company experienced before the end of the stay period any of the above-mentioned circumstances that could or did trigger the automatic stay in the first place; or
- a prescribed reason relating to the circumstances in existence during the stay period.

If enacted, these particular provisions (namely Section 415D(4), 434J(4) and 451E(4) of the Act) will be very significant, as they will effectively make the automatic stay permanent. In
the authors’ view, the reason the Bill’s drafters have approached the legislation this way (i.e., introduced an automatic stay that only applies for a defined period; while simultaneously introducing a provision that makes the same rights unenforceable indefinitely) is to ensure the legislation had a concept of a stay period, which could then be used to delimit the concomitant stay on the company’s ability to require new advances of money (discussed further below).

That being said, companies should be aware that:

a The automatic stay will not apply to rights arising under all contracts. The stay will not apply to:
- rights arising under contracts, agreements or arrangements entered into before the commencement of the *ipso facto* provisions (see below for commencement details);
- rights arising under contracts entered into after the court approves the scheme, the receiver or managing controller is appointed or the company comes under administration (as relevant);
- other types of contracts or contractual rights prescribed in the regulations or by ministerial declaration; or
- rights where the scheme administrator, receiver or managing controller or administrator (as relevant) has consented in writing to the enforcement of the right.

b Courts will have the power to lift the automatic stay in respect of certain *ipso facto* rights if satisfied that doing so is in the interests of justice or (in the case of a scheme only) the relevant scheme is not for the purpose of the company avoiding being wound up.

c Contractual counterparties cannot be required to provide the company with additional credit or money during a period where one or more of the counterparty’s own rights cannot be enforced against the company by reason of the automatic stay. As noted above and notwithstanding the comment above regarding the automatic stay ‘effectively’ being made permanent, in the authors’ view, the drafters of the legislation do not intend this concomitant stay on the company’s ability to demand additional credit to extend beyond the expiry of the relevant and above-mentioned stay periods.

**Stay orders in respect of potentially broader range of contractual rights**

The Bill also provides that courts will be able to make orders that for a period of time specified in the order, one or more rights under a contract may only be enforced with the leave of the court or on terms imposed by the court (stay orders), if the court is satisfied that the relevant right:

a is being exercised;

b might be exercised; or

c there is a threat that it might be exercised, merely because the company has experienced any of the circumstances which could or did trigger an automatic stay. It is also possible for a court to make interim orders before deciding an application for a stay order.

While it is clear that stay orders may not be granted in respect of rights specifically carved out from the operation of the automatic stay (see discussion above), as there are no other limitations on the types of contractual rights that may be the subject of stay orders, it appears to be the drafters’ intention that stay orders will be able to be made in respect of a potentially
broader range of contractual rights than the automatic stay. In this regard, we note the drafting note within the Bill that states that a stay order could be sought, for example, in respect of a right to terminate for convenience.

If enacted, the *ipso facto* provisions will commence on a date to be fixed by proclamation. However, if the provisions have not commenced by 30 June 2018 or six months after the Bill receives Royal Assent (whichever is later), the *ipso facto* provisions will commence on the day after that later date.

The Bill also makes some additional amendments to the Act, to ensure, for example that the automatic stay will not interfere with the right of a substantially secured creditor to appoint a receiver during its 13-business-day decision period following the appointment of administrators (discussed above).

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

i Arrium Administration and Mol-Cop sale

One of the most notable collapses in recent times has been that of Arrium Ltd (Arrium). Arrium is an international mining and materials company listed on the Australian stock exchange, with three key business segments: mining consumables, mining and steel. Following an unsuccessful attempt to sell its mining consumables business in 2015 and the group’s inability to secure lender support for a recapitalisation plan (admittedly one that required Arrium’s lenders to agree to a ‘haircut’ of more than 50 cents to the dollar), on 7 April 2016, Arrium and 93 of its Australian subsidiaries appointed voluntary administrators. However, not all companies in the group went into administration. At the time of its collapse, the wider Arrium group included entities located in Australia, Canada, the United States, Mexico, Peru, Chile, Hong Kong and Indonesia that carried on the group’s highly successful mining consumables business known as the ‘Moly-Cop’ business.

The administrators sought to reduce the group’s debt through a number of asset sales. Arrium’s grinding products business, Moly-Cop, not in administration, was sold to US private equity firm American Industrial Partners for US$1.23 billion, completing in the first few days of 2017. This multi-jurisdictional divestment, which included a complex restructure with 65 steps to separate Moly-Cop from Arrium, was a successful outcome after the highly competitive, concurrently run dual-track sale process and IPO (with a trade sale being finally adopted). The multi-faceted, cross-border transaction was coordinated across teams of lawyers from Gilbert + Tobin (lead counsel) as well as lawyers in the US, Canada, Mexico, Chile and Peru.

The remaining Arrium group of companies, including the Whyalla steelworks and east coast steel distribution business, remains subject to a competitive trade sale process with the sale expected to be announced in late June 2017.

ii Emeco recapitalisation and three way merger

One of the largest solvent reconstructions to occur over the past year has been the recapitalisation of mining services rental equipment provider Emeco Holdings Limited (Emeco) and its three way merger with Orionstone and Andy’s Earthmovers. This complicated transaction involved the following notable aspects:

- Noteholder and creditor claims held against Emeco, Orionstone, and Andy’s Earthmovers were exchanged for senior secured notes due 2022 with a face value
of approximately A$465 million and approximately 44 per cent of issued capital in Emeco, with approximately 6 per cent of additional shares on issue provided to major noteholder Black Diamond. The exchange was effected by way of a creditors’ scheme of arrangement, which successfully received court sanctioning under Section 411 of the Corporations Act 2001 (Cth) and involved the restructure of New York law governed notes.

b Emeco’s merger with Orionstone was effected by way of exchange of 100 per cent of Orionstone shares for approximately 10 per cent of issued capital in Emeco. Similarly, Emeco’s merger with Andy’s Earthmovers was effected by way of exchange of 100 per cent of Andy’s Earthmovers’ shares for approximately 5 per cent of Emeco’s issued capital.

c Approximately 6 per of Emeco’s issued capital was issued to a major holdout noteholder of Emeco, Black Diamond, whose support was crucial to the success of the creditor scheme through which the transaction was effected.

d Complex security arrangements for the merged group with a dual security trust structure and security over assets in Australia, Chile, Canada and the US.

e Additional funding for Emeco was achieved through a non-renounceable fully underwritten A$20 million rights offer and the introduction of an A$65 million revolving loan facility following cancellation of commitments under Emeco’s asset backed loan due to expire in December 2017.

As a mining services equipment rental business, Emeco has had significant exposure to fluctuating commodity pricing, particularly on coal and copper. The company also trades in a market environment where there is an oversupply of mining services equipment rentals. Even as commodity pricing has recovered miners have remained cautious attitudes towards supply expansion and committing significant capital expenditure to greenfield projects. Importantly for Emeco, the merger with Orionstone and Andy’s Earthmovers reduced Emeco’s fleet age, which presented the company with the opportunity to achieve lower maintenance capital expenditure costs and achieve much needed margin breathing space.

V INTERNATIONAL

Australian courts cooperate with foreign courts and insolvency practitioners, and will recognise the jurisdiction of the relevant court in which the ‘centre of main interest’ is located. This approach follows the UNCITRAL Model Law on insolvency, which was codified into Australian law through the Cross-Border Insolvency Act 2008 (Cth).

There is also scope under different legislation such as the Act for Australian courts to recognise foreign judgments in Australia. Specifically under Section 581 of the Act, Australian courts have a duty to render assistance when required by a foreign insolvency court. Further, the Act has extraterritorial application; for example, an Australian court has jurisdiction to wind up a foreign company.

Receivers do not have the benefit of taking action in foreign jurisdictions that other insolvency administrators have under the Cross-Border Insolvency Act 2008 (Cth).16 This is because receiverships relate only to a debt owed to the appointer, and, as such, cannot be said to be collective proceedings in terms of the application of the Model Law.

16 Section 8.
VI  FUTURE DEVELOPMENTS

The Basel capital requirements and the desire to exit distressed scenarios with some value will continue to incentivise Australian institutional banks and traditional foreign banks to trade debt. The Australian market will continue to be attractive for credit funds looking to pursue control transactions after acquiring debt positions.

It continues to be anticipated that any large-scale restructures will continue to occur outside formal insolvency procedures, although it is likely there will be a decline in their frequency. The pursuit of debt-for-equity strategies will continue at the instigation of credit funds willing – and often seeking – to take an equity interest in a company (including management roles). This debt-for-equity play is likely to extend to bilateral arrangements over time, should opportunities present themselves. This is likely to be particularly attractive in the small and medium-cap mining space.

The number of formal insolvency appointments at the small to mid-cap level of business will increase as companies continue to struggle with liquidity problems and waning local and international demand.

In terms of future legislative development, the key item to watch out for over the next 12 months is the introduction of the Bill.
Chapter 2

AUSTRIA

Heinrich Foglar-Deinhardstein and Thomas Trettnak

I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

In 2016, Austria's most famous insolvency case ended for the time being with the bondholders accepting a deal. After the surprising drop of all support for the bad bank and the imposition of a debt moratorium in 2015, the legally challenging case of HETA Asset Resolution AG (HETA), the bad-bank vehicle created in the wake of the failed Hypo Alpe Adria, continued in 2016. Finally, creditors owning the predominant debt issued by HETA accepted a discounted offer from the province of Carinthia, the bank's former owner. This deal prevented the unprecedented insolvency of Carinthia in Austria.

Expressed in figures, Austrian insolvency law showed an increase in the number of new insolvency proceedings by 1.5 per cent in 2016 compared with 2015. The number of employees affected by insolvencies in 2016 decreased by 4.3 per cent and the total liabilities amounted to €2.9 billion.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

In insolvency law, Austria is generally considered a creditor-friendly jurisdiction. In order to prevent insolvencies, and to protect the companies themselves and their creditors, the Insolvency Law Amendment Act 2010 entered into force on 1 July 2010. It quite comprehensively changed Austrian insolvency law. Since 2010, the Austrian Insolvency Act has provided for uniform insolvency proceedings. First and foremost, the new insolvency law aims at encouraging companies in financial distress to use the various procedures for restructuring and protecting insolvency as early as possible. In combination with a mandatory

1 Heinrich Foglar-Deinhardstein and Thomas Trettnak are partners at Cerha Hempel Spiegelfeld Hlawati Rechtsanwälte GmbH.
2 After a shortfall of HETA's assets of between approximately €4 billion and €7.6 billion, Austria's Ministry of Finance announced that Austria will no longer provide any additional financial support to HETA. Further, the Financial Market Authority imposed a temporary debt moratorium on all liabilities of HETA until 31 May 2016 to draw up a resolution plan. This was the first time that the new European resolution regime for banks had been applied by a Member State.
3 Insolvency statistic 2016 of the Austrian creditors' representation organisation KSV1870: www.ksv.at/insolvenzstatistiken/insolvenzstatistik-2016-final.
5 Feil, Insolvenzordnung?, Section 1 fn 1 et seq.
filing requirement, delays in filing for insolvency shall be prevented. The Insolvency Law Amendment Act 2010 was well received throughout the insolvency community and has proved to be a success.

i Uniform insolvency proceedings
In Austria, insolvency proceedings are conducted either as restructuring proceedings or as bankruptcy (i.e., liquidation) proceedings. 6

Bankruptcy proceedings
This is the most common form of insolvency proceedings in Austria. It aims at liquidating all assets and distributing the funds generated from liquidation to the debtor’s creditors. When opening bankruptcy proceedings, the debtor loses its rights of administration and disposition, which pass to the insolvency administrator. From that point on the debtor remains the owner of the assets, but the assets form the insolvency estate to be used primarily to satisfy the claims of creditors.

Restructuring proceedings
One of the main objectives of the Insolvency Law Amendment Act 2010 was to improve the debtor’s ability to continue as a going concern. Restructuring proceedings encourage a form of debt settlement that is better prepared and, therefore, rapidly finalised. It aims at continuing the operation of the business of the debtor during and after the proceedings, without liquidating the debtor. If restructuring proceedings fail, they are transformed by court order into bankruptcy proceedings. 7 Additionally, the Austrian Reorganisation Act 8 also provides – at least in theory – provisions for the restructuring of a company suffering financial difficulties. It is directed at companies that find themselves in an early stage of financial distress. According to the provisions of the Austrian Reorganisation Act, a debt-equity ratio of below 8 per cent and a debt amortization period of more than 15 years indicate an impending insolvency. However, these provisions have little practical relevance, as the completion of such procedure requires the consent of all creditors. 9 Nevertheless, the Austrian Reorganisation Act was prominently used during the Hypo Alpe Adria crisis when the Kärntner Landesholding 10 applied for reorganisation proceedings at the competent Regional Court Klagenfurt 11 in order to take certain legal measures on behalf of the Kärntner Landesholding and Carinthia in its function.

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6 The Insolvency Law Amendment Act 2010 adapted Austrian insolvency law to the new economic developments and abolished the practically irrelevant composition proceedings. Now, Austrian law provides for certain types of insolvency proceedings which are, however, all governed by the same regulations subject to a few specifics in each case.

7 This is one of the results of uniform insolvency proceedings.

8 Unternehmensreorganisationsgesetz, BGBl. I Nr. 114/1997, as amended.

9 For a comprehensive summary of this ‘stand-alone pre-bankruptcy proceeding’, see Mohr, "Unternehmensreorganisationsgesetz – URG (1997)"


11 The respective petition can be found at: www.ksv.at/sites/default/files/assets/documents/antrag_auf_einleitung_eines_reorganisationsverfahrens.pdf.
as supervisor as well as potential creditors of liabilities facing several claims in connection with the HETA settlement. The respective petition was withdrawn before a decision was made.

Apart from the aforementioned, out-of-court restructuring efforts and negotiations are very common and usually initiated prior to the opening of (in-court) insolvency proceedings, and conducted mostly on an informal basis. However, Austrian law does not know hybrid court-administered restructuring proceedings or insolvency proceedings, such as the German Schutzschirmverfahren (i.e., special pre-insolvency, court-administered proceedings).

ii Test for insolvency

Under the Austrian Insolvency Act, the opening of insolvency proceedings requires either illiquidity\(^\text{12}\) or over-indebtedness\(^\text{13}\) of the debtor.

Illiquidity

The Austrian Insolvency Act does not provide any definition of illiquidity. Case law, however, qualifies illiquidity as a permanent lack of funds that prevents the debtor from discharging debts that have fallen due for repayment. Accordingly, the Austrian Supreme Court assumes illiquidity in case the debtor suffers from a permanent lack of sufficient funds. A mere delay in payment does not amount to insolvency. Further, illiquidity is indicated in case there is a liquidity gap of more than 5 per cent of the obligations of the debtor.\(^\text{14}\)

Over-indebtedness

This criterion is assessed by means of a two-step test. Austrian law abstains from relying solely on the balance sheets but rather also considers the future commercial opportunities and development of the debtor. Over-indebtedness thus means that the liabilities of a company exceed its assets and that the debtor has a negative going concern forecast. According to case law, the necessity to apply this two-step test is triggered by a finding of negative equity based on the balance sheet of the respective company. Meanwhile, the prevailing view\(^\text{15}\) is that the assets are assessed on the basis of their liquidation value rather than their going concern value. If the company is in a state of calculated over-indebtedness, the second step of the test has to be performed, which has to show a positive going concern forecast (a positive Fortbestehensprognose).\(^\text{16}\) The going concern forecast has to assess future solvency and economic viability of the company. A tool commonly used for preparing such going concern forecast is a standardised template of the Austrian Federal Chamber of Commerce detailing the key elements to be set forth therein as well as the methods to be used for the preparation of such a forecast.\(^\text{17}\) In a nutshell, a business plan has to be prepared, showing – with a preponderance of probability – that the company will (1) become and stay solvent within the first six to 12 months following the date of the going concern forecast, and further, in the long term (i.e., two to three years), (2) be able to achieve economic viability in the form of a sustainable

\(^{12}\) Section 66 of the Austrian Insolvency Act.

\(^{13}\) Section 67 of the Austrian Insolvency Act.

\(^{14}\) OGH 3 Ob 9910/w.

\(^{15}\) Burger, Entwicklungslinien der Rechtsprechung zum Überschuldungstatbestand, wbl 1988.

\(^{16}\) Trettnak/Heimel, Eine Prognose, die beim Weiterleben hilft, Der Standard, Wirtschaft & Recht Journal, 13.10.2016, 14et seq.

\(^{17}\) Leitfaden Fortbestehensprognose Gemeinsame Stellungnahme, March 2016.
turn-around.\textsuperscript{18} With regard to the required ‘preponderance of probability’, Austrian literature recently criticised the lack of methods to help substantiate this factor. Thus, new ideas are currently being developed in order to help assess the preponderance of probability and, consequently, provide sufficient plausibility of the positive going concern forecast.\textsuperscript{19} One of those methods frequently discussed in Austria is the ‘Monte-Carlo’ simulation. Given that there is a two-step test, the debtor is not obliged to file for insolvency in case it provides such positive going concern forecast irrespective of whether or not calculated over-indebtedness has been identified.

According to Section 69, Paragraph 2 of the Austrian Insolvency Act, directors of a company are obliged to file for the opening of insolvency proceedings without undue or culpable delay, but in no case later than 60 days after the insolvency criteria are met pursuant to the Austrian Insolvency Act. In bankruptcy proceedings, the application may either be filed by the debtor himself or by a creditor.\textsuperscript{20} In contrast, an application for the opening of restructuring proceedings may only be filed by the debtor. Moreover, sufficient assets to cover the costs of the proceedings are required to open insolvency proceedings.\textsuperscript{21} In case no sufficient assets are available, the respective insolvency petition is rejected \textit{a limine} and insolvency proceedings are not commenced.\textsuperscript{22} As a consequence, the respective company is dissolved \textit{ex officio} due to the lack of funds and deleted from the Austrian Companies Register.

\begin{itemize}
\item[iii] \textbf{Insolvency and restructuring proceedings}
\end{itemize}

The purpose of the Insolvency Law Amendment Act 2010 in particular was to facilitate the reorganisation of a distressed business.\textsuperscript{23} Austrian law thus provides for two types of restructuring proceedings. Both are aimed at ensuring the continuing survival of the debtor by providing for the restructuring of (some of its) financial obligations. Simultaneously with the application for the opening of restructuring proceedings, a restructuring plan has to be submitted.

\begin{itemize}
\item[iv] \textbf{Restructuring proceedings with self-administration}
\end{itemize}

This restructuring regime gives the debtor the chance of retaining the administration of its own assets, especially being able to continue to manage its own company.\textsuperscript{24} Generally

\textsuperscript{19} Birgmayer-Baier/Piringer/Schützinger, \textit{Die Plausibilisierung der überwiegenden Wahrscheinlichkeit bei Fortbestehensprognosen durch Monte-Carlo-Simulationen}, ZIK 2016/224.
\textsuperscript{20} See Section 70 of the Austrian Insolvency Act.
\textsuperscript{21} With regard to companies the initial cost of the insolvency proceeding is estimated at €4,000. It is, however, not necessary that this amount is available in cash. Tangible assets as well as claims against creditors are considered sufficient for this purpose. Whether or not there are sufficient assets has to be assessed \textit{ex officio}. In case there is a lack of sufficient assets, the competent court requests an advanced payment from the applicant (debtor or creditor). The obligation to provide such an advanced payment relates to the directors as well as shareholders holding a stake of more than 50 per cent.
\textsuperscript{22} In 2016, a total of 2,063 insolvency proceedings were rejected \textit{a limine} because the petitioning entity did not have sufficient assets. This was approximately 40 per cent of all insolvency proceedings in Austria in 2016.
\textsuperscript{23} Restructuring proceedings may already be applied for in case of impending illiquidity.
\textsuperscript{24} The debtor’s right to keep administering its assets is governed by strict rules and only possible for a very brief period of time (see Sections 169 and 170 of the Austrian Insolvency Act).
speaking, the restructuring administrator’s approval is required only for matters outside the ordinary course of business. Self-administration requires the debtor to file an application for self-administration supplemented by certain documents and a restructuring plan that provides for a minimum debt repayment quota to the creditors of 30 per cent of registered debt repayable within two years. The restructuring plan in particular must provide: (1) that the rights of secured creditors as well as the rights of creditors holding a security interest in an asset will not be affected; (2) full payment of all priority claims, any monies advanced by a third party to cover the initial costs of the proceedings and the fees of the administrator; and (3) a quota of at least 30 per cent. Furthermore, the debtor must provide evidence in the application that it is able to fund the priority claims for a period of 90 days following the application.

In order to adopt the restructuring plan, a double majority must be achieved: (1) more than half of the creditors present have to vote in favour of the restructuring plan; and (2) creditors holding more than 50 per cent of the total amount of all current creditors’ claims must consent. The restructuring plan is only adopted if both majorities are achieved; in such a case, dissenting creditors are overruled and have to accept the respective plan.

The restructuring plan has to be approved by the creditors within 90 days of the commencement of restructuring proceedings, otherwise the status of self-administration is lost. However, the proceedings as such still continue as restructuring proceedings with the consequence that the right of administration and disposition pass on to the insolvency administrator.

v Administered restructuring proceedings

In case the debtor submits a restructuring plan, but does not ask for self-administration, proceedings are opened and called administrated proceedings. The same is true in case the court rejects the debtor’s request for self-administration. In case of administration by a restructuring administrator, the debt repayment quota may be as low as 20 per cent of the registered debt (repayable within two years). Again, acceptance of the restructuring plan requires a double majority. Administered restructuring proceedings offer the advantage of a longer period of time for preparing (and financing) a restructuring plan. Hence, the majority of restructuring proceedings are being conducted in this form.

vi General principles

Against the backdrop of wanting to facilitate the reorganisation of businesses, the debtor is also able to submit a restructuring plan even if only ordinary bankruptcy proceedings have

25 Section 169 of the Austrian Insolvency Act.
26 Section 149 (1) of the Austrian Insolvency Act.
27 Section 150 (1) of the Austrian Insolvency Act.
28 Regardless of this 90 days deadline, the court has the right to withdraw the debtor’s right to self-administer its company inter alia if the debtor does not seem trustworthy, is not paying the priority claims in time or has made incorrect statements in its submission for the opening of restructuring proceedings.
29 Section 141 (1) of the Austrian Insolvency Act.
30 In 2016, 438 administrated restructuring proceedings have been initiated compared to 60 restructuring proceedings with self-administration. For further details please see the insolvency statistic 2016 of the Austrian creditors’ representation organisation KSV1870.
been initiated.\textsuperscript{31} This is also in the creditor's interest as the recovery quota is somewhat higher compared to ordinary bankruptcy proceedings. In case the submitted restructuring plan is admissible the court will issue a formal edict opening the proceedings. The court has to set a date for a hearing with regard to the restructuring plan within a period of not more than six weeks. In this hearing the creditors will take a vote on the proposed restructuring plan. In the light of achieving better results for creditors, there is a presumption for keeping the debtor's business in operation. The business itself may only be realised: (1) in case the restructuring plan is not approved within 90 days; (2) if the restructuring plan no longer corresponds to the common interest of the creditors; or (3) the requirements for carrying on with the business are no longer fulfilled. In practice, the continuation of the operations of the debtor's business is only possible in case there are additional sources of financing and any further losses can be avoided.

In case the restructuring plan has been approved with the necessary double-majority, it is further required to receive the confirmation of the competent insolvency court. The court, however, must not force the creditors to accept the plan. Following the acceptance and confirmation of the restructuring plan, the debtor will (again) be vested with all rights in and to the estate. In certain cases, however, the restructuring plan may also provide for a trustee to be appointed to: (1) supervise the fulfilment of the restructuring plan by the debtor; (2) take over the estate with the mandate to fulfil the restructuring plan; or (3) liquidate the estate.

vii Bankruptcy proceedings

In 2016, for instance, a total of 2,665 bankruptcy proceedings were initiated in Austria,\textsuperscript{32} making this liquidation proceeding still the most common type of insolvency proceedings in Austria. In bankruptcy proceedings, the application might either be filed by the debtor himself or by a creditor. The insolvency court has to assess whether the conditions for the opening of the proceedings are fulfilled. In order to avoid that creditor's using filing for insolvency as leverage, the court has to continue with its assessment even if the application has been withdrawn by the creditor as the withdrawal alone does not suffice to rebut the debtor's illiquidity.

In case bankruptcy proceedings are initiated, the insolvency court in any event has to appoint an insolvency administrator. The debtor's right to administer and dispose of the assets passes to the insolvency administrator. Any acts taken by the debtor after the opening of insolvency proceedings are legally void with regard to the insolvency creditors.

The opening of insolvency proceedings is tied to a number of substantive legal consequences that are applicable to all kinds of insolvency proceedings. Once insolvency proceedings are commenced, creditors can only enforce their claims using the rules provided for in the proceedings. Court proceedings and litigation with regard to the insolvency estate are suspended ex lege with the opening of insolvency proceedings; they cannot be commenced or continued. Creditors are further prohibited from obtaining court-ordered security; executions against claims in insolvency are inadmissible.\textsuperscript{33} Further, Austrian insolvency law stipulates a bar on dissolving contracts that are essential for carrying on with the business. Basically such contracts – within the first six months after the opening of insolvency proceedings – may

\textsuperscript{31} This can be done until the termination of the proceedings. See Section 140 (1) of the Austrian Insolvency Act.

\textsuperscript{32} Insolvency statistics for 2016 of the Austrian creditors' representation organisation KSV1870.

\textsuperscript{33} See Sections 6 et seq. of the Austrian Insolvency Act.
only be dissolved for good cause. In this regard it has to be noted that the deterioration of the economic situation of the debtor as well as the debtor’s default in fulfilling claims due before opening insolvency proceedings are not considered to be good causes within the meaning of this provision.\(^{34}\) Further, there are certain limitations on the creditor’s ability to use insolvency as grounds for termination of contractual agreements.\(^{35}\) With regard to bilateral contracts that neither party has completely fulfilled at the time of the opening of the insolvency proceedings, Section 21 of the Austrian Insolvency Act stipulates that the insolvency administrator may elect to either assume or withdraw from said contract. In case the insolvency administrator assumes the contract, any claims of the contractual partner arising out of this contract constitute priority claims.

viii The taking and enforcement of security

The effect of insolvency on security arrangements depends on the exact type of security. The Austrian Insolvency Act distinguishes between the right of separation of assets and the right of separate satisfaction. Generally speaking, both are – subject to voidance claims (see below) – not affected by the opening of insolvency proceedings. In case of an absolute right \textit{in rem} such as in particular retention of title, the respective secured creditor has a claim of separation to receive the asset as this asset does not form part of the insolvency estate.\(^{36}\) Claims relating to an absolute right \textit{in rem} are made against the insolvency administrator. Where the insolvency administrator does not release the asset, an action may be brought against the administrator. With regard to claims for separate satisfaction (such as pledges and securities) the creditors are entitled to receive the value of the assets in case they are sold by the insolvency administrator. The amount received when selling such assets serves as a pool of separate assets and the respective creditors are entitled to preferential satisfaction from the sale proceeds. In case the proceeds are insufficient to satisfy the claim, the creditor has to declare the remaining amount as an insolvency claim with the insolvency court.

ix Duties of directors of companies in financial difficulties

With regard to management liability a distinction needs to be made between a director’s internal liability in regard to the company and potential external liability in regard to third parties. Under Austrian law, directors are obliged to perform their duties with the care of a prudent and diligent business manager.\(^{37}\) Directors may be held personally liable if they negligently or wilfully cause damage to the company. Generally speaking only the company itself, represented by the (remaining) directors, the shareholders or the insolvency administrator is entitled to claim compensation for such damages. Direct claims may be brought by third parties only in specific cases where the director has violated a law protecting the interest of said third parties.

\(^{34}\) The restriction set forth in Section 25a of the Austrian Insolvency Act does \textit{inter alia} not apply to claims for payments from loans and employment contracts.

\(^{35}\) Trettnak, \textit{Vertragsauflösung bei Insolvenz erleichtert}, Der Standard, 07.04.2014.

\(^{36}\) In case the discharge of a secured claim could endanger the business carrying on secured creditors are barred from enforcing their claim prior to the expiry of six months after the restructuring proceedings were opened if such enforcement might endanger the continuation of the debtor’s business operations. See Section 11 (2) of the Austrian Insolvency Act.

\(^{37}\) See Section 25 of the Austrian Act on Limited Liability Companies and Section 84 of the Austrian Stock Corporation Act.
The violation of the director’s duty to file for the opening of insolvency proceedings without undue or culpable delay triggers the liability of directors with regard to all creditors for damages caused by such delay, since the respective provision of the Austrian Insolvency Act qualifies as a protective law to the benefit of the creditors. On one side, the protection covers existing creditors (i.e., creditors whose claims existed prior to the opening of insolvency proceedings). Such creditors are entitled to claim the quota damage, which is defined as the damage resulting from the late application for the opening of an insolvency proceeding. Further, also new creditors (who only become creditors after the opening of insolvency proceedings) are protected. In this regard the Austrian Supreme Court has ruled in several cases that (only) the negative interest may be reimbursed.38

The Austrian Criminal Code also contains provisions on insolvency proceedings. The most important provisions are: (1) grossly negligent interference with creditors’ interests;39 (2) fraudulent intervention with a creditor’s claims;40 (3) preferential treatment of creditors;41 and (4) withholding of social security payments.42

**x Clawback actions**

The Austrian Insolvency Act states that transactions that unduly decrease the assets of the debtor prior to the opening of insolvency proceedings may be contested. All clawback provisions aim to secure the debtor’s assets prior to the opening of proceedings. In this regard, transactions entered into by the debtor and a third party that discriminate against other creditors may be contested.43 The general principles for contesting transactions are as follows: (1) there is a transaction; (2) the transaction is entered into prior to the opening of insolvency proceedings; (3) the transaction unduly decreases the assets of the debtor; (4) the transaction discriminates against other creditors; and (5) a specific contesting provision of the Austrian Insolvency Act is fulfilled. The Austrian Insolvency Act provides for the following contesting provisions:

- **a** Intent to discriminate: This provision applies in case of transactions concluded by the debtor to intentionally discriminate against certain creditors with regard to the others within the past 10 years prior to the opening of insolvency proceedings and if the other contracting party knew of this intent. If the other contracting party should have known of such intent, the period in which to contest the transaction is reduced to two years. Regarding related persons a statutory law provides for a reversal of the burden of proof.

- **b** Squandering of assets: A transaction falls under this provision if the other contracting party must or should have known that the transaction squanders the company’s assets and the transaction was entered into within the last year prior to the opening of insolvency proceedings.

- **c** Dispositions free of charge: This provision relates to transactions that were made free of charge (gifts) and were entered into within the last two years prior to the opening of insolvency proceedings.

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38 OGH 4 Ob 31/07y.
39 Section 159 of the Austrian Criminal Code.
40 Section 156 of the Austrian Criminal Code.
41 Section 158 of the Austrian Criminal Code.
42 Section 153c of the Austrian Criminal Code.
43 See Sections 27 to 32 of the Austrian Insolvency Act.
Preferential treatment of creditors: Transactions concluded within the last year preceding the commencement of insolvency proceedings but after material insolvency or the petition for opening insolvency proceedings or in the last 60 days may be challenged if said transaction was objectively preferential or was intended to be preferential and thus discriminates against one creditor with regard to the others.

Knowledge of illiquidity: A transaction carried out within the last six months preceding the commencement of insolvency proceedings but after material insolvency or the petition for opening insolvency proceedings may be challenged if the other contracting party knew or was negligent in not knowing of the debtor's illiquidity or the filing of the petition for opening insolvency proceedings, respectively. Further, it is necessary that the respective legal act either constitutes satisfaction or securing of a creditor or is deemed to be disadvantageous.

The claim contesting a transaction must be filed within one year of the opening of insolvency proceedings by claim or objection by the insolvency administrator. It must seek a declaration of ineffectiveness of the contested transaction.

III RECENT LEGAL DEVELOPMENTS

Currently, a comprehensive reform of debt settlement proceedings for natural persons is being prepared in Austria. Since 1 January 1995 natural persons have the possibility of debt relief within the framework of debt settlement proceedings. This is a special form of insolvency proceedings for natural persons, irrespective of whether they are consumers or individual entrepreneurs. The aim of the debt settlement proceedings is the ability to offer a person who is insolvent a realistic chance to – commercially speaking – ‘start all over again’ and to become debt-free after seven years. During this period a minimum debt repayment quota of 10 per cent should be achieved. The main focus of the reform proposals is the abolition of such minimum quota of 10 per cent.

In addition to certain specific topics in company insolvency law, such as the possibility for a call for a debt-to-equity swap for creditors, the introduction of specific hybrid preventative proceedings (similar to the German Schutzschirmverfahren), and group insolvency proceedings are being discussed on an ongoing basis. However, the above are very specific topics that are generally found to be applicable in too few instances that would merit the creation of a specific profound legal basis in Austria. In addition, similar topics are often also discussed on an international or EU level, for example, group insolvency proceedings.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

In 2016, 5,226 companies became insolvent and a total of 58,800 creditors were affected by insolvency proceedings. Approximately 50 per cent of all insolvency proceedings concern companies established less than 10 years ago. After the high number of employees affected by insolvency proceedings in 2015 (which was mostly due to the failing of supermarket chain Zielpunkt, the third-largest in Austria), 2016 showed a decrease in this regard of

44 Sections 181 et seq. of the Austrian Insolvency Code.
approximately 12 per cent. The extraordinary increase in liabilities in 2016 is the result of the two major insolvency proceedings, the one concerning ActivSolar GmbH (€690 million) and the other SLAV Handel, Vertretung und Beteiligung AG (€126 million). These two Vienna-based holding companies had to file for insolvency due to their investment exposure in Ukraine. There is – pursuant to our perception – no specific emphasis of insolvency activity in any specific industry in Austria.

Austria’s economic growth is picking up, and, therefore, it is estimated that 2017 will be characterised by a similar or even smaller number of insolvencies compared with 2016, again with a slight increase in restructuring proceedings over bankruptcy proceedings, proving that the reform in 2010 has actually had an impact on the economy.

V INTERNATIONAL

On 20 May 2015, a new regulation amending EC Regulation 1346/2000 on insolvency proceedings was introduced, and became applicable to relevant insolvency proceedings from 26 June 2017 onwards. Importantly, the Regulation *inter alia* establishes new rules for insolvency proceedings opened in relation to a member of a group of companies. The EU has opted for a coordination procedure between the insolvency proceedings involving different companies of the same group. Furthermore, the new law includes a clarification of the definition of the ‘centre of main interest,’ which is one of the key connecting factors in European insolvency law. The Regulation further provides for two different means to refuse or postpone the request to open secondary proceedings. Generally speaking, however, the reform does not modify, but merely specifies, the fundamental framework of cross-border insolvency adopted by Regulation 1346/2000.

VI FUTURE DEVELOPMENTS

On 22 November 2016, the European Commission issued a proposal for a directive on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures. If enacted, the Directive would be the first serious step towards the harmonisation of domestic insolvency laws of EU Member States. The core element of the proposal sets out rules aimed at ensuring ‘that viable enterprises in financial difficulties have access to effective national preventative restructuring frameworks which enable them to continue operating.’ The basic idea is to create a pre-insolvency reorganisation procedure in which the debtor negotiates a plan with creditors or select classes of creditors and that – if voted on by the prescribed majority and approved by designated national administrative agencies – becomes binding, even on dissenting parties to the plan. To facilitate negotiations, the debtor would be able to apply for a stay on enforcement action by creditors, and the commencement of insolvency proceedings. Further, the proposal provides for a safe harbour for transactions that are made in connection with the restructuring and are not carried out fraudulently or in bad faith. Protection is awarded in particular to interim

46 For a comprehensive overview see Nummer-Krautgasser/Graber/Jaufer, Grenzüberschreitende Insolvenzen im Europäischen Binnenmarkt (2017).
financing and new financing that is granted in connection with a restructuring process. The grantors of such financing shall be protected from voidance action, as well as liability under criminal or civil law, to which they could be exposed under the existing laws of certain Member States. Those proposals and recommendations are mostly unknown to Austrian insolvency law. Thus, it remains to be seen how the Austrian legislator will implement those recommendations into national law.

One of the issues set forth in the work programme 2017/2018 of the Austrian government concerns the out-of-court restructuring of companies. In this regard, two proposals on how to implement such proceedings have been issued. The first proposal, submitted by the Austrian creditors’ representation organisation KSV1870, abstained from a stand-alone proceeding and opted for a prolongation of the 60 days deadline for filing to commence insolvency proceedings as set forth in Section 69(2) of the Austrian Insolvency Act. The second proposal issued by ReTurn, however, outlined independent restructuring proceedings that bear a certain resemblance to the British scheme of arrangement. However, due to current inner political developments and new parliamentary elections in Austria in October 2017, it is doubtful whether or not this concept of an out-of-court restructuring proceeding will be pursued further.

48 ReTurn is an independent forum of experts dealing with restructuring, reorganisation and turnarounds.
Chapter 3

BELGIUM

Bart De Moor and Marie Keup

I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

An overall decrease of the number of bankruptcies has been observed in the last three years. For the whole Belgian territory, 10,736 bankruptcy proceedings were opened in 2014, 9,762 in 2015 and 9,170 in 2016. The bankruptcy ratio across all industries in 2015 was 1 bankruptcy for 110 active companies against 1 bankruptcy for 103 active companies in 2014. However, according to the Belgian Federal Public Service Economy, an increase of 2.6 per cent of the number of bankruptcies has been observed in the period from November 2017 to April 2017 compared to the same period last year. The sectors in which high bankruptcies ratios are still observed are the hotel and catering industry, retail, transport and construction sectors.

This positive evolution is confirmed by a high recovery rate. In June 2016 Commissioner Jourovà stated that according to the World Bank indicators recovery rates of 90 per cent had been observed in Belgium. As he suggested, this can be explained by the fact that restructuring proceedings remain the most common insolvency proceedings in Belgium.

Another interesting fact is that according to a European Central Bank survey on access to finance by enterprises in the eurozone area, Belgian enterprises have a positive record for access to bank financing. It appears that the reluctance of banks to grant loans following the financial crisis of 2008 is over in Belgium. A study conducted in Belgium at the initiative of the Belgian Federal Public Service Economy shows a less positive picture of access to bank financing for small and medium-sized enterprises, especially for micro-enterprises and starters.

Recent market trends in restructuring and bankruptcy proceedings as well as numbers and figures on formal proceedings are discussed further below.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

In Belgium, insolvency situations are governed through separate laws that all provide for specific types of proceedings. All these proceedings as referred to in Article 2(4) of the EU Insolvency Regulation 2015/848. Transition from one type of proceeding to another is possible during the insolvency process of a company, which often causes difficulties, as the provisions of the separate laws are not always fully compatible. As such, the law is often criticised, and many have urged that the Belgian insolvency laws be harmonised and unified.

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The Belgian Federal Public Service Justice is currently conducting a review of the Belgian insolvency laws. The law will be inserted in the recent codification, the Code of Economic Law. No fundamental changes in the principles of Belgian insolvency law are to be expected. A main distinction is made between proceedings involving the winding up of a company and proceedings aiming at the reorganisation and turnaround or transfer of undertakings of a company.

i  Formal proceedings

In Belgium, the formal proceedings as referred to by Article 2(4) of the EU Insolvency Regulation are:

- bankruptcy proceedings;
- judicial reorganisation through the adoption of an amicable agreement;
- judicial reorganisation through a vote on a restructuring plan;
- judicial reorganisation through a transfer of undertakings;
- insolvency proceedings for non-commercial individuals;
- voluntary liquidation;
- judicial liquidation; and
- provisional dispossession of the directors.  

Bankruptcy proceedings

Bankruptcy proceedings are governed by the Bankruptcy Law, and involve the winding up of an enterprise. For the time being only commercial companies and commercial physical persons can be declared bankrupt. This is likely to change when new insolvency legislation will be adopted. Foreign companies and branches of foreign companies in Belgium are not subject to the Belgian Bankruptcy Law unless their centre of main interest is located in Belgium.

Bankruptcy is pronounced upon the fulfilment of the conditions on cessation of payment and the ongoing lack of credit from either creditors or financial institutions. The court makes its decision upon the request of a creditor or the public prosecutor, or upon the declaration of the cessation of payment by the debtor.

Directors of a company under an ongoing cessation of payment have a legal obligation to immediately declare that situation to the commercial court, which then decides whether to open bankruptcy proceedings. Absence of such declaration for more than one month following the cessation of payment is criminally sanctioned. The period between the cessation of payment and the opening of bankruptcy proceedings is called the ‘suspect period’, as the debtor or its directors may be inclined to take certain actions that are detrimental to the creditors or in the personal interest of the directors only. Acts and engagements of the debtor after the date of cessation of payment and before the opening of the bankruptcy proceedings are, therefore, subject to clawback actions by the liquidator to have the commercial court declare that the engagements are not binding upon the estate. The law distinguishes between acts that will be automatically declared non-binding by the court (for instance, payments to a creditor before the due date or payments in kind) and less suspect acts that are potentially declared not binding (mainly acts undertaken towards a creditor who had clear knowledge of the cessation of payments).

2 Provided for in Article 8 of the Bankruptcy Law of 8 August 1997 (Bankruptcy Law).
The management or board of directors is dispossessed of their power, and an independent liquidator appointed by the court takes over all powers under the control of a supervisory judge and the commercial court. Depending on the matters involved, the supervisory judge and the commercial court have to approve certain actions of the liquidator, *inter alia*, settlements that the liquidator wants to conclude to terminate disputes. In order to fund the operations, the liquidator can engage the estate. Debts ‘of’ the estate are immediately payable, contrary to debts dating from before the opening of the bankruptcy proceedings (termed debts ‘in’ the estate). The liquidator must ensure, under his or her personal liability, that the necessary funding is available in the estate and that the engagements taken are not detrimental to the creditors.

Upon the opening of the bankruptcy proceedings, all claims against the debtor are halted. Enforcement is suspended and interest calculation is stopped.

The liquidator realises the assets of the debtor, then distributes the proceeds taking into account the privileges and securities of the creditors. The opening of bankruptcy proceedings triggers a concursus creditorum. Proceeds are distributed according to the legal rank of the creditors. Creditors of a same rank are treated on a *pari passu* basis.

Creditors having a right *in rem* can be entitled, under certain circumstances, to enforce their rights directly, not being subject to the bankruptcy proceedings and even without the intervention of the liquidator. However, this is rarely what they want. In general, creditors prefer that the liquidator undertakes all necessary actions, and then pays out these creditors taking into account their rights *in rem*.

Creditors of the estate are paid out of the estate prior to creditors in the estate. Taking into account the interest of the estate, ongoing contracts can be terminated or continued by the liquidator. Creditors are entitled to force the liquidator to make such decision within one month following their request.

In cases where the activities or a part of these can be continued and transferred to an other entity, the liquidator can be authorised by the commercial court to continue such business. This is subject to the condition that the continuation is not detrimental to the creditors. That is rarely done, as the liquidator is personally liable for the loss of value for the creditors should the transfer of undertakings not be successful or should the continuation of the business generate more costs than profits. Therefore, liquidators will require financial guarantees from candidate purchasers who wish the liquidator to continue the business while the transfer is negotiated.

The typical legal instrument to transfer undertakings from an insolvent company is a judicial reorganisation under the authority of the court. A transfer of an undertaking after bankruptcy is also an alternative, and opinions are divided as to whether the judicial reorganisation or the bankruptcy is the most efficient procedure.

Liquidation proceedings can take a long time, as they cannot be closed as long as legal proceedings regarding disputes are ongoing.

**Judicial reorganisation**

A judicial reorganisation aims at saving an enterprise, or at least its viable activities, thereby avoiding the stigma of bankruptcy. Judicial reorganisations are governed by the Law on the Continuity of Enterprises adopted in 2009 and modified in 2013.

A company that is unable to meet its obligations and that is potentially threatened by enforcement by its creditors can apply for judicial reorganisation. Bringing the request before the court already provides a temporary protection and, when opening the reorganisation
Belgium

proceedings, the court orders a suspension of the debt existing at the time of the opening of the proceedings for an initial maximum period of six months. This period is meant to grant the company the time needed to elaborate and execute measures to allow it to realise its turnaround. Such measures can be the reduction or restructuring of the debt and other economic measures to improve the business.

Three types of judicial reorganisation proceedings are available.

The simplest type of proceeding involves the conclusion of an amicable agreement with two or more creditors who are parties to the agreement. Sometimes a restructuring, reduction or rescheduling of the debt with a few creditors can be sufficient to turn around the company without the involvement of all the other creditors.

The second type of proceedings involves all creditors, and is, therefore, more burdensome. It comprises the drafting of a restructuring plan and the approval by a positive vote of all the creditors. The plan must be approved by at least half of the number of creditors representing half the amount of all claims. Equal treatment of all creditors is not mandatory: creditors can be put into different categories and treated differently, and the reduction of the debt of one category (at a minimum of 15 per cent of the amount) can allow the debtor to offer a higher dividend to another category, thus winning its positive vote. Equal treatment of all creditors within one category is, however, necessary. Transformation of debt into capital as part of the plan is also possible.

The third type of proceedings consists of a transfer of undertakings. It is essentially meant for situations where no restructuring plan can be expected to be accepted by the vote of the creditors. The viable part or parts of the activities can be transferred to one or more other legal entities. The price to be paid for (the part of) the undertakings is presumed to be higher than the price a liquidator would obtain in bankruptcy proceedings. Therefore, this type of insolvency proceedings is deemed to be beneficial for the creditors and is preferred over bankruptcy. In this type of proceedings, the activities and assets are transferred free of charges: all rights of creditors, including rights in rem, are transferred to the price paid for the transfer.

In most cases of transfer of undertakings, when all viable activities have been transferred, the debtor company will be an empty shell or an entity without any viable activity. It will have to be liquidated through bankruptcy or voluntary liquidation. As such, this third type of judicial reorganisation is to be considered as a liquidation proceeding rather than as a reorganisation proceeding in the sense of the EU Insolvency Regulation. In some cases, however, not all viable parts are transferred, and the price paid for the transferred part of the undertakings may provide the surviving company with the necessary funding for a successful turnaround. In such case, no liquidation or bankruptcy will follow the judicial reorganisation.

New debt arising after the opening of the reorganisation proceedings for new services or deliveries, whether through new contracts or through existing contracts, is not suspended and is immediately payable by the debtor. This is logical, and ensures that suppliers of goods or services will still deliver. To offer a maximum incentive to contractors of the debtor to continue their commercial relationship, the law expressly provides that should such debt nevertheless not be paid and should bankruptcy of the debtor occur, the creditor concerned will be considered as a creditor of the estate in the bankruptcy proceedings. A major concern arises when, in such case, at the opening of the bankruptcy proceedings, the value present in the estate appears not to be sufficient to pay all debts of the estate created by the application of this provision. Such situation does not necessarily point to any responsibility of the
debtor. Indeed, it is difficult (if not impossible) for the debtor in the course of reorganisation proceedings to predict whether bankruptcy will follow and how much value will be available in the estate. This provision in the law could be used as a basis for debtor-in-possession financing. New loans granted to the debtor following the opening of the reorganisation proceedings, which would not be paid back, could be considered as debt of the estate. In cases where this funding would have been used to increase the value of the assets, the creditor would even be preferred over the existing creditors, having rights *in rem* on said assets.

**Insolvency proceedings for non-commercial individuals**

Insolvency of non-commercial individuals, which aims to reduce their debt, falls outside the scope of this chapter.

**Voluntary liquidation**

In principle, voluntary liquidation is meant to terminate the activity of a solvent company. A voluntary liquidation is governed by the provisions of the Belgian Companies Code. A company under a liquidation proceeding can appear to be insolvent during the course of the proceedings; in such case, previously, the company would necessarily have to be declared bankrupt. However, due to the evolution of the jurisprudence of the Court of Cassation, the voluntary liquidation can be continued if this is not detrimental to the creditors. A voluntary liquidation can be insolvent from the beginning if the creditors consent to the proceeding, or if, at least, the creditors are better off with the voluntary liquidation than with bankruptcy proceedings. Over the past few years, many voluntary liquidations were continued although insolvency appeared after the opening of the proceedings. Moreover, voluntary liquidations of companies are now also conducted although they are clearly insolvent from the opening of the liquidation proceedings if this is more advantageous to the creditors than a bankruptcy.

Voluntary liquidation is triggered by the shareholders deciding to dissolve the company, and is a deliberate choice of the shareholders not to opt for bankruptcy proceedings and to prefer a voluntary liquidation. The general assembly of shareholders appoints one or more liquidators who may be former employees or directors of the company or external liquidators. After its dissolution, the company is deemed to exist merely for the purpose of its liquidation. The legal capacity of the company is reduced to the acts needed to execute and terminate the liquidation. Each year, the liquidator must submit the annual accounts of the company to the general assembly, and must clarify the reasons why the liquidation has not yet been completed.

Creditors’ rights in an insolvent voluntary liquidation are comparable to their rights in bankruptcy proceedings. The main difference resides in the fact that the liquidator (often a former employee or director of the company) is less independent than a court-appointed liquidator in bankruptcy proceedings. The court-appointed liquidator will be less likely to refrain from investigations and possibly legal action against the former board of directors of the company.

**Judicial liquidation**

Under specific circumstances, and independently of whether the company is insolvent, the court can order the liquidation of the company and appoint a judicial liquidator. A judicial liquidation is governed by the provisions of the Belgian Companies Code.
Belgium

The commercial court can order the judicial liquidation of a company for serious reasons upon the request of any shareholder or any interested stakeholder. Moreover, if the value of the net assets of the company has fallen below the minimum capital amount, any interested stakeholder is entitled to ask the court to order the dissolution and liquidation of the company. In cases where the company did not file its annual accounts for three consecutive years, any interested third party or the public prosecutor can request that the company be liquidated under court supervision, unless this situation is resolved before the liquidation has been ordered.

Provisional dispossession of the directors

In cases where a company is virtually bankrupt, and serious doubts arise that the debtor or its administrators got away with the assets of the company, the commercial court can, based on Article 8 of the Bankruptcy Law, suspend the debtor’s rights and appoint a provisional administrator to represent the debtor. The court can act ex officio or upon request of a creditor. This suspension will automatically end after a period of 15 days unless the provisional administrator or the creditor files a request with the court to have the company declared bankrupt.

A similar provision is provided for in the Law on the Continuity of Enterprises, it being understood that the aim of the appointment of the provisional administrator is to contribute to the company’s turnaround and not its liquidation.

Informal proceedings

Informal proceedings entail negative publicity, and in most cases add to the difficulties of a company that is already in trouble. Therefore, the legislator has put a strong emphasis on informal proceedings. The absence of negative publicity also creates an incentive for the management of the company to undertake action at an earlier stage of the distress, thus increasing the chances of success.

Chamber of the court in charge of commercial investigations

The court, being an instrument of the state of public service to the business community, conducts research to detect companies in distress on the basis of specific economic indicators. The directors of these companies are invited to explain to a judge in charge of commercial investigation on a confidential basis the company’s situation and the measures they will adopt to turn around the company. If the response of the directors is not satisfactory, the court can inform the public prosecutor, who can initiate insolvency proceedings.

Amicable agreements (without judicial reorganisation proceedings being opened)

In cases where the company is not threatened by enforcement by the creditors and a suspension of the debt is not necessary, an agreement to rearrange the debt or to take other measures concluded with a few carefully selected creditors may be sufficient to turn around the company. The amicable agreement presents several advantages: the negotiations can be kept confidential; not all creditors should be alerted to the distress of the company; and there is no court involvement, and thus no long and costly proceedings to be put in place.

The reason why, prior to the adoption of the Law on the Continuity of Enterprises, creditors would not engage in such negotiations is that they feared possible clawback actions by the bankruptcy liquidator should the turnaround not be successful and the company
afterwards be declared bankrupt. As such, the Law on the Continuity of Enterprises provides legal protection for such amicable agreements under specific conditions. In cases where bankruptcy proceedings are opened within six months following the amicable agreement, the bankruptcy liquidator will not be entitled to engage in clawback actions based on Article 17, No. 2 or Article 18 of the Belgian Bankruptcy Code. This means that the liquidator will not have the possibility to challenge the agreement for the reason that payment to a creditor was done before the due date of the claim, thereby preferring one creditor over the others (Article 17, No. 2). Nor will the liquidator have the right to challenge the agreement for the reason that payment was received by one creditor, who was clearly aware of the distress of the company, to the detriment of other creditors who did not receive payment (Article 18). No protection is granted for gifts and payments in kind whose value is higher than the debt (Article 17, No. 1), for agreements by which an existing creditor adds new security to previous debts (Article 17, No. 3) and against legal action of the liquidator based on the actio Pauliana.

The conditions to obtain this legal protection are that the amicable agreement must expressly be qualified as such in the agreement and that express mention is to be made that the agreement aims at the improvement of the financial health of the company, subject to control by the court. The amicable agreement also has to be filed at the court.

Company mediator

Article 15 of the Law on the Continuity of Enterprises provides for the possibility of having a mediator appointed by the President of the Commercial Court or the President of the Chamber of Commercial Investigation to facilitate the negotiations regarding the turnaround of a company. The law is deliberately silent about the precise mission of the mediator, allowing the court to decide on a case-by-case basis.

The benefits of such appointment are multiple. The combination of the confidentiality of the measure, the expertise, independence and credibility of the mediator, and the fact that the decision-making power of the management is not affected, make it a strong instrument.

The Belgian legislator is the first in Europe to expressly introduce mediation in its insolvency legislation. The main difference between mediation in general and the mediation aimed at in the framework of the Law on the Continuity of Enterprises is that the scope of the activity of the company mediator is broader than in ordinary mediation. Parties in the mediation are not necessarily involved in a dispute. There may just be functional tensions (for instance where one party, a bank or a creditor in general is expecting payment and the other cannot pay). Tensions can also exist between the company’s directors or management and the shareholders. A company mediator can help to find a solution while respecting the interests and needs of all parties involved.

iii Taking and enforcing security

Depending on the assets available, different types of securities can be granted to creditors. A mortgage on real estate requires a notarial deed of mortgage and registration in a public register. The registration duties and notarial fees are determined by the amount of the secured debt. A pledge on shares needs to be registered. A statement of the pledge or notification should be entered in the company’s share register. A pledge on receivables (bank accounts, receivables, contractual rights) is effective and enforceable, and binding upon third parties, as soon as it is entered into. To make a pledge on receivables binding upon the underlying debtor, a notification is legally required. A pledge on intellectual property requires filing
with the appropriate intellectual property office or offices. A pledge on the whole business is possible in favour of financial institutions only. The business comprises all instruments and assets needed to run a commercial activity. The pledge covers all these assets and instruments, with a limitation of 50 per cent of the stock. A pledge on a business must be registered in the public mortgage register to be binding upon third parties.

Creditors can also benefit from privileges granted by the law without any contractual provision being required. That is the case for numerous creditors, for instance employees, the Treasury and the Social Security. The law distinguishes between general and specific privileges. General privileges grant priority to the creditor on all moveable or immoveable assets (depending on the law). Specific privileges grant priority to the creditor over only one asset, but are higher ranked than general privileges.

The law determines the priority of claims of creditors in a concursus creditorum (for instance, in the case of bankruptcy). First in rank are the costs and debts incurred by the liquidator during the bankruptcy proceedings, including the liquidator’s fees. Second in rank are the creditors benefiting from a specific privilege, followed by those creditors benefiting from a general privilege. Last in rank, if any proceeds are still available, are the unsecured creditors.

iv Duties of directors of companies in financial difficulties

In limited liability companies, shareholders and company directors are not personally liable for the debts of a company. As they have an active role in the administration of the company, however, directors can be held liable for shortcomings or torts committed in that role. The Belgian legislator provides for a well-calibrated system of liabilities, depending on the type of obligation that the director failed to respect.

III RECENT LEGAL DEVELOPMENTS

i General

The Belgian Bankruptcy Law was adopted in 1997 and has not undergone significant modifications since. The Belgian law on reorganisation, called the Law on the Continuity of Enterprises, was adopted in 2009 and was slightly amended in 2013. The aim of this modification was the better prevention and detection of companies in financial distress, as well as the elimination of a number of abuses by introducing a legal obligation on the debtor to submit a range of documents as from the filing of its petition; a new financial threshold (costs in advance of €1,000 must be paid as from 1 January 2015 when submitting the petition for the initiation of judicial reorganisation proceedings); and an obligation on the external auditors, accountants and tax advisers to inform the debtor in detail of any significant and corresponding facts that may jeopardise the continuity of the debtor’s enterprise.

ii Implementation of the Belgian insolvency register

Since 1 April 2017, a digital insolvency register, ‘RegSol’ (www.regsol.be), established by the Law of 1 December 2016 amending the Judicial Code and the Law of 8 August 1997 on bankruptcies (published in the Belgian Official Gazette on 11 January 2017), has gone live. The insolvency register is managed jointly by the Belgian French and German-speaking Bars and the Belgian Flemish Bars (Article 5/2 of Law on Bankruptcies). As from that date all creditors, apart from a few exceptions, have to file their claim through this platform. Foreign legal entities, however, are still allowed to file their claims by registered mail sent to the
insolvency practitioner. According to the law, foreign legal entities may also use the platform but in practice, access by foreign legal entities to the platform is currently problematic due to issues of authentication of these entities. The problem is expected to be solved when the European registration platform is put in place. An implementing royal decree is currently being prepared and will tackle the following issues: (1) protection of personal data, (2) access to register per category of user, (3) costs of the register, and (4) the format of the claim.

iii Upcoming reforms

A reform of the Bankruptcy Law and the Law on the Continuity of Enterprises may be expected in the nearby future. The main criticism is that these laws are not a perfect match and legal scholars plead for one insolvency act that governs both bankruptcy and reorganisation proceedings (see Section VI, infra). Another criticism is related to the fact that the current legal system for the remuneration of bankruptcy liquidators does not incentivise them to take legal action, for instance, engaging in legal proceedings on the basis of directors’ liability. Draft texts are currently being discussed. Unfortunately few substantial changes will be made to the current principles governing the law and the two aforementioned main criticisms are not likely to be addressed.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

Each year, 50,000 Belgian companies face critical financial distress. According to figures published by Graydon and the Federal Public Service Economy, in 2016, 9,170 companies were declared bankrupt. The number of bankruptcies in 2016 decreased by 6.06 per cent in comparison with 2015. This decrease is a result of a number of initiatives of the courts, especially the courts of Brussels, such as the increased search for and detection of companies in distress; the slight economic recovery at the international level, which has an impact on export-import sensitive sectors; and the effect of the modification in 2013 of the Law on the Continuity of Enterprises. The highest number of bankruptcies are situated in the hotel and catering industry, retail and transport, followed by the building industry.

V INTERNATIONAL

The activities of companies are no longer confined to one country: either the assets of companies are spread over different states or companies have centres of activities established in different countries. Therefore, the number of international insolvency proceedings has greatly increased.

International insolvency proceedings raise two main questions. On the one hand, where should the opening of the insolvency proceedings be requested and which law applies to the insolvency proceedings? And on the other hand, to what extent will a foreign insolvency decision be recognised in another state, and what powers will a foreign liquidator have in another state?

Under Belgian law, these questions are governed by Chapter XI of the Belgian Code of Private International Law, which is enshrined in the Law of 16 July 2004. Article 116 of the Code states that Chapter XI is applicable to both bankruptcies and judicial reorganisations.
However, the scope of the Belgian provisions is quite limited due to the adoption in 2000 of the EU Insolvency Regulation 1346/2000, and the adoption in 2015 of the new EU Insolvency Regulation 2015/848, entering into force in 2017, as well as the existence of a range of bilateral and multilateral treaties.

### EU Insolvency Regulation

The EU Insolvency Regulation deals with international jurisdiction, applicable law, recognition and cooperation. It is applicable whenever the debtor has its centre of main interests (COMI) within the EU. The effect of the regulation will, however, be limited to the assets located in the EU.

#### Jurisdiction of the Belgian courts

The EU Insolvency regulation distinguishes between main insolvency proceedings, which have universal scope and aim at encompassing all the debtor’s assets, and territorial insolvency proceedings, which cover only the assets located in the state of opening.

Pursuant to the EU Insolvency regulation, the Belgian courts will have jurisdiction to open main insolvency proceedings if the concerned company has its COMI in Belgium. If a company has an establishment and assets in Belgium, a territorial insolvency proceeding may be opened in Belgium but its effects will be limited to those assets that are located in Belgium.

#### Law applicable

The law applicable to the conditions for the opening of the insolvency proceedings, their conduct and their closure is that of the Member State of the opening of the proceedings (lex concursus). The EU Insolvency regulation, however, provides a range of exceptions to the lex concursus aiming at the preservation of the rights of the third parties that are located in another Member State than the Member State of the opening of those proceedings.

#### Duty of information and cooperation

The EU Insolvency regulation requires the liquidators of main and secondary proceedings to cooperate and exchange information.

#### Efficacy of foreign judgments

Any decision relating to the opening, the conduct or the closure of insolvency proceedings, as well as decisions deriving directly from the insolvency proceedings or closely linked with them as well as any preservation measures shall be automatically recognised in Belgium with no further formalities. The enforcement of these decisions is, however, subject to a prior judicial review by the Belgian commercial courts.


If the business centre of the debtor is located outside the EU, bilateral or multilateral treaties will be applicable.
ii Bilateral and multilateral treaties

Besides the EU Insolvency Regulation, Belgium is a party to bilateral and multilateral conventions that deal with international insolvency proceedings, in particular recognition and enforcement issues. Following the entry into force of the EU Insolvency regulation, the relevance of these treaties has been limited.

If neither the EU Insolvency Regulation nor one of these treaties is applicable, the Belgian rules of private international law will be applicable.

iii Chapter XI of the Belgian Code of Private International Law

International insolvency proceedings are governed by Chapter IX of the Belgian Code of Private International Law (Articles 116 to 121).

These provisions were inspired by the EU Insolvency Regulation and the UNCITRAL Model Law. However, some specificities exist.

Jurisdiction of the Belgian courts

Article 118 of the Belgian Code of Private International Law of the Belgian Code of Private International Law determines the cases in which the Belgian courts will have jurisdiction other than those cases where such jurisdiction derives from the EU Insolvency Regulation. In such cases, the opening of the insolvency proceeding, its progress and its closing will be governed by Belgian law.

This provision draws a distinction between main insolvency proceedings and territorial insolvency proceedings.

The main insolvency proceeding is defined by Article 117, No. 2 of the Code of Private International Law as the insolvency proceeding whose effects extend to the assets of the debtor as a whole. Belgian courts have jurisdiction to order the opening of a main insolvency proceeding when the main establishment or the registered office of the debtor is located in Belgium.

The territorial proceeding is defined by Article 117, No. 3 of the Code of Private International Law as the insolvency proceedings whose effects are limited to the assets of debtors that are located on the territory of the state in which the said proceeding is opened. Belgian courts have jurisdiction to order the opening of territorial insolvency proceedings when the debtor has an establishment in Belgium.

Duty of information and cooperation

Article 120 of the Belgian Code of Private International Law imposes on the liquidator of a main proceeding or of a territorial proceeding opened pursuant to Article 118 of the Code a duty to cooperate and exchange information concerning the management of foreign insolvency proceedings.

This duty is, however, subject to a condition of reciprocity, meaning that such duty will only apply where the foreign state provides for such duty in its own laws. Moreover, the liquidator will not be bound by this duty if the inscription, publication and cooperation costs are unreasonable compared with the assets of the debtor.

This cooperation duty also implies that if the liquidation of the assets of a territorial proceeding is sufficient to pay all the admitted claims of the creditors, the liquidator designated
in this proceeding will have to transfer without delay the excess of assets to the administrator of the main proceeding on the condition that there exists reciprocal cooperation and exchange of information in said proceeding.

**Efficacy of foreign judgments**

Article 121 of the Code of Private International Law deals with the issue of the recognition of foreign insolvency decisions when the EU Insolvency Regulation or a bilateral or multilateral convention do not apply.

Pursuant to Article 121 of the Code of Private International Law, a foreign decision relating to the opening, progress or closing of an insolvency proceeding that was not delivered on the basis of the EU Insolvency Regulation is recognised or declared enforceable in Belgium provided that:

- **a** as a decision of a main proceeding, the decision was rendered by a court of the state in which the main establishment of the debtor was located at the time of the introduction of the proceeding;

- **b** as a decision of a territorial proceeding, the decision was rendered by a court of a state in which the debtor has an establishment other than its main establishment; and

- **c** the effect of the foreign decision is not contrary to the rights of the third parties provided for in Article 119, Sections 2 to 4.

**Powers of the foreign liquidator**

In cases of recognition, the liquidator may exercise the powers granted to him or her by the foreign decision, such as requesting the opening of a territorial proceeding in Belgium, or any provisional and conservatory measures in his or her capacity as liquidator in the foreign main proceeding.

The foreign insolvency decision must not be formally recognised in order for the foreign liquidator to exercise his or her powers. It is only in cases where the insolvency decision is challenged that the foreign liquidator might have to request the formal recognition of said decision and his or her mandate.

**VI FUTURE DEVELOPMENTS**

The current insolvency legislation in Belgium is quite recent, with laws dating from 1997 for bankruptcy proceedings (the Bankruptcy Law) and 2009 and 2013 for reorganisation proceedings (the Law on the Continuity of Enterprises). A reform of the Bankruptcy Law may be expected in the nearby future. Draft texts are currently being discussed. Unfortunately few substantial changes will be made to the current principles governing the law and the two beforementioned main criticisms are not likely to be addressed. It might be hoped that future reforms of the law on bankruptcy will include a better fit with the Law on the Continuity of Enterprises. Indeed, unsuccessful reorganisations often end in bankruptcy, and successful reorganisations on the basis of a transfer of undertakings also end up in the bankruptcy or voluntary liquidation of the remaining (almost empty) shell. Ideally, the Belgian legislator would adopt a completely new law including and coordinating both provisions on the bankruptcy and the reorganisation of companies in distress.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

In Brazil, Federal Law 11,101/2005, known as the Brazilian Bankruptcy and Restructuring Law (BRL), came into effect on 9 June 2005, bringing significant changes to the legal treatment of Brazilian companies that are insolvent or facing financial difficulties.

Throughout its 12 years of effectiveness, several periods of judicial restructuring trends can be identified, directly related to the economic and financial crisis in Brazil and the rest of the world, as well as the evolution of the proceedings and case law. These are as follows:

a first period: airline companies, such as Vasp, Varig and BRA;
b second period: meatpacking and agribusiness industries, such as Arantes, Independencia, Quatro Marcos and Nilza;
c third period: electric power companies, such as Celpa and Grupo Rede;
d fourth period: oil, gas and mining companies, such as OGX, OSX and Eneva; and
e fifth period: infrastructure, construction, engineering and communication companies, such as OAS, Galvão Engenharia, Schahin, Sete Brasil, Oi, Viver, PDG and Abengoa.

In terms of the proceeding itself, smaller companies tend to be more successful in restructurings, since the smaller company’s structure and its number (and size) of creditors tend to facilitate the process. However, for both small and large companies, the financial conditions in which the company entered the restructuring proceedings is the decisive factor for a possible recovery.

Over the past three years, the Brazilian investigation known as Operation Car Wash has led the country to an unprecedented political and economic crisis, leading construction companies and companies in the infrastructure sector, whether involved or not in the investigation, to request its judicial restructuring.

A consequence of such crisis was that, according to Serasa Experian, 2016 had a record number of judicial restructuring requests since the BRL came into effect, with an increase of 44.8 per cent compared with 2015. In the first quarter of 2017, however, the number of reorganisation proceedings in Brazil fell by more than 30 per cent compared with the first quarter of 2016.
II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Brief description of the proceedings

The BRL applies to entrepreneurs and business companies in general. It is not applied to state-owned companies, mixed-capital companies, financial institutions, insurance companies and some other entities expressly excluded by the law, which are subject to specific insolvency proceedings.

The BRL establishes three major mechanisms that may apply to companies in difficulty: (1) judicial restructuring; (2) out-of-court restructuring; and (3) forced liquidation. As one of its main features, the BRL offers the debtor company flexibility and, in most situations, continuity of management and an opportunity for rehabilitation.

The mechanisms of judicial restructuring and out-of-court restructuring, which replaced the old concordata (a court-relief system for debtors), are used when a particular business can be maintained in operation, even with the change of corporate subject or reduced operation, and may overcome its financial crisis.

The forced liquidation proceeding shall apply when a particular business is no longer viable. In this case, as a rule, the debtor (either an individual businessman or a company) is removed from its activities and the existing assets are attached and sold by a judicial administrator (that may continue the debtor activities if it is understood by the Bankruptcy Court to be beneficial for the creditors). Any proceeds derived from the sale of assets are distributed among different creditors according to a preference order established by law.

Judicial restructuring proceeding

Any debtor that meets certain conditions specified in the BRL may apply for judicial restructuring proceeding. The application must be accompanied by several documents and information, including explanations about the financial difficulties faced by the debtor, financial statements, a list of creditors and a list of employees.

If the application is in proper form, the court will authorise the initiation of judicial restructuring proceeding. A public notice will then be included in the official gazette containing, among others: a summary of the request made by the debtor; a list of creditors; and a warning about the applicable term for any challenges to the list of creditors, including requests for adjustments and inclusions.

In relation to the judicial restructuring proceeding, the BRL establishes that:

a only the debtor may file a court application for restructuring;
b there is a non-automatic 180-day stay period for credits subject to the proceeding, applied when the court authorises the proceeding;
c tax and few other types of debts are not subject to the proceeding and creditors holding such debt may initiate or proceed with collection lawsuits against the debtor;
d the BRL does not provide for a specific status such as ‘debtor in possession’ as in the Chapter 11 of the US Bankruptcy Code. As a general rule, the existing management of the debtor continues to operate the business and regular business acts are allowed, except that any sale of ‘permanent’ assets is only allowed if authorised by the Bankruptcy Court or permitted in the reorganisation plan approved by the creditors;
e the appointment of a creditors’ committee is optional and has more of a supervisory than decision-making role;
while a judicial administrator nominated by the Court monitors the activities performed by the debtor, he or she mainly manages the judicial procedure acts, instead of replacing the management of the debtor company in operating the business;

a judicial manager is only appointed when the debtor’s existing management has been removed from their positions. This may occur in exceptional legal cases, such as when:

- there are indicia of bankruptcy crimes;
- some acts were performed with wilful misconduct or engaged in fraudulent schemes against creditors;
- the managers have been making personal expenditures that are not compatible with their income; or
- the management removal is specified in the reorganisation plan; and

the general meeting of creditors is essential to the process, since it has the power to approve or reject the reorganisation plan.

The debtor company shall submit a reorganisation plan within 60 days from the publication of the court order authorising the initiation of the proceeding. If the plan is not submitted in due time, the debtor shall be declared bankrupt (as forced liquidation). The reorganisation plan must contain: a detailed description of restructuring mechanisms to be used, which may include debt rescheduling, corporate reorganisation, transfer of corporate control, partial sale of assets, leasing of going-concerns, and a series of other measures; demonstration of the economic feasibility of the debtor’s business; and a report on the debtor’s assets prepared by an expert appraiser or company. The plan cannot provide that overdue labour credits and credits deriving from accidents at work will be paid in a term longer than one year from the ratification of the approved plan by the Bankruptcy Court.

Creditors will be informed about the reorganisation plan and the applicable term to challenge it through a public notice. If any objection to the proposed plan is submitted by any creditor, the court shall call a general meeting of creditors. In the meeting, creditors may:

1. approve the plan as originally proposed;
2. approve a modified version of the plan; as long as there is no opposition from the debtor and no harm to absent creditors; or
3. reject the plan, in which case the debtor should be declared bankrupt (as forced liquidation).

Any reorganisation plan must be approved by the following four categories of creditors in a general meeting of creditors: (1) labour creditors and creditors from accidents at work; (2) secured creditors; (3) unsecured creditors, creditors with special or general preference, and subordinated creditors; and (4) small business creditors (companies that have a yearly revenue up to a specific amount provided by law).

The plan must be approved by all four categories. In the first and fourth classes of creditors, approval is achieved with the favourable vote of the majority of creditors present at the meeting (by head), regardless of the amount of their credits. In the other two classes, approval is achieved with the favourable vote of both the majority of creditors present at the meeting (by head) and the majority of creditors representing more than half of the credit amounts represented at the meeting (by amount).

If certain vote combinations specified in the BRL are obtained in the general meeting of creditors, the court may grant the judicial restructuring, even when the plan was not approved pursuant to the quorum requirements explained above, if some requirements are fulfilled (cramdown).
The reorganisation plan may provide for a judicial sale of branches or individual going-concerns belonging to the debtor. The judicial sale may take the form of an auction, be effected through proposals submitted in sealed envelopes, or be a combination of the former two options.

Once the judicial sale is effected, the relevant branch or going-concern will, in principle, be free and clear of any liens and encumbrances, and the purchaser will not succeed the debtor with respect to any indebtedness. As a consequence, creditors from a debtor that is subject to judicial restructuring will not be able to claim any amount from the purchasers of branches or going-concerns, and the corresponding assets will not be attached to satisfy their credits. Therefore, creditors will simply retain their original claims against the debtor.

Judicial restructuring proceedings shall remain in place until all obligations maturing within two years that are specified in the plan are fully complied with by the debtor. If the debtor fails to comply with any obligation within such period, its forced liquidation shall be declared. Any obligation unfulfilled after the two-year period entitles creditors to initiate collection proceedings or request the declaration of the debtors’ forced liquidation.

Verifying that all obligations matured within two years after the approval of the plan were fulfilled, the Court shall order the termination of judicial restructuring proceeding. It should be noted that, although no longer subject to court proceedings, the debtor remains liable for all obligations specified in the plan that are still outstanding.

**Out-of-court restructuring proceeding**

Any debtor that meets certain conditions specified in the BRL may propose and negotiate with its creditors an expedited reorganisation plan, also called out-of-court reorganisation plan, and request its judicial ratification, with the possibility of enforceability towards creditors whose credits are treated in the plan and who did not adhere to it, if a certain quorum of adherence is obtained.

In other words, despite being deemed ‘out-of-court’, the plan must be ratified by a Bankruptcy Court to bind creditors who did not even adhere to the plan. This does not mean that the plan will be conducted within the context of court proceedings. It just needs to be ratified.

To produce effects with respect to all creditors contemplated in the plan, including those that have not expressly adhered to the settlement, the BRL provides that the ratified plan must have been approved by creditors representing more than three-fifths of credits in each species of creditors contemplated by the plan.

Once the debtor requests the ratification of the plan, the creditors will have the opportunity to challenge such ratification. Nevertheless, any challenges may be based solely on an alleged illegality or a failure by the debtor to comply with all necessary legal requisites or formalities and not on the economic feasibility of the plan.

If the challenges are not accepted by the Court, the out-of-court reorganisation plan will be ratified and bind all creditors contemplated in the plan. The plan’s provisions and obligations are judicially enforceable after the ratification decision.

**Bankruptcy or forced liquidation**

According to the BRL, debtors that are facing a financial crisis and do not meet the conditions to benefit from judicial restructuring or out-of-court restructuring proceedings should request the declaration of their own forced liquidation. The prerequisite of a forced liquidation
request is related to the company's financial and economic situation. In other words, the main condition that shall be analysed by the Court in terms of the forced liquidation declaration is the self-management ability of the company as well as its financial and economic viability.

In this case, the debtor has the duty to explain the reasons why the company cannot continue with its economic activities. Further, the debtor must present to the Court several related documents, which are listed in the BRL.

In addition, any creditor may request the forced liquidation of a debtor in certain circumstances, including the following:

\( a \) failure by the debtor to comply with payment obligations in excess of 40 times the prevailing Brazilian minimum wage, provided that a protest with a public registry has been lodged with respect to the corresponding indebtedness. To reach the above threshold, two or more creditors can combine their credits;

\( b \) the existence of debt collection proceedings against the debtor where no assets have been attached or no money has been deposited to secure payment of the relevant obligations;

\( c \) the debtor has engaged in actions such as unjustified sales of assets or fraudulent schemes against the interests of creditors; and

\( d \) the debtor has failed to comply with obligations under a judicial reorganisation plan.

The forced liquidation proceeding is conducted by the Bankruptcy Court, the public prosecutor, the judicial administrator and creditors. The Bankruptcy Court will appoint the judicial administrator that will manage the bankruptcy estate, attach and sell all the company's assets, so there is no need for the company to appoint a liquidator or administrator (and no due diligence required).

According to the BRL, the payment to creditors in a forced liquidation proceeding is made after all restitutions and payments of non concurrent credits and should observe the list of creditors produced by the Court according to the order of preference under the BRL.

The order of preference for payments to creditors in the forced liquidation proceeding established in the BRL is as follows:

\( a \) labour claims of up to 150 times the prevailing minimum wage for each creditor, and claims deriving from accidents at work;

\( b \) secured credits up to the value of the relevant collateral;

\( c \) tax debts;

\( d \) credits with special privileges;

\( e \) credits with general privileges;

\( f \) unsecured credits;

\( g \) contractual penalties, tax penalties and fines deriving from violations of legal provisions; and

\( h \) subordinated credits (as considered by law or agreement, and shareholders' and certain managers' credits).

Some credits should be honoured and paid before all of those mentioned above, in the order set forth below:

\( a \) the compensation payable to the judicial administrator and his or her assistants, and labour-related claims or occupational accident claims referring to services rendered after the decree of the forced liquidation;

\( b \) sums provided to the bankruptcy estate by the creditors;
c expenses with schedules, management, asset sale and distribution of the proceeds, as well as court costs of the forced liquidation proceedings;
d court costs with respect to actions and enforcement suits found against the bankruptcy estate; and
e obligations resulting from valid legal acts performed and contracts agreed during the judicial restructuring proceeding, such as loans and continuity of supply, or after the decree of the forced liquidation, and taxes relating to triggering events postdating the decree of the forced liquidation.

In addition, if the debtor is in possession of assets (including money) that belong to third parties at the time the forced liquidation is decreed (by a leasing or fiduciary sale agreement or advance of foreign exchange currency agreement, for example), rightful owners may request restitution of their assets before the payment of any creditor, which may be understood also as a priority over the order of preference of the BRL. This is the case because such assets (which may include money) are understood by law and case law to not belong to the debtor, and, therefore, cannot be included as part of the bankruptcy estate.

In those situations where assets to be repossessed no longer exist, the owner will be entitled to receive an equivalent amount in cash. The same will occur when a bank has disbursed funds to the debtor pursuant to an advance of foreign exchange agreement. In such cases, any restitution in cash will have priority and will only be subject to the previous payment of labour claims that have matured three months before the declaration of forced liquidation, up to a limit of five times the prevailing minimum wage per employee.

After the forced liquidation is judicially decreed, the debtor company will be liquidated so that its assets can be attached and sold by the judicial administrator, and the amount obtained will pay the creditors. Only after the extinguishment of all obligations may the shareholders request the rehabilitation of the company, in order to explore its activity once again.

All the debtor company’s obligations will be considered extinguished if it is able to pay all of its debts, if it is able to pay up to 50 per cent of its unsecured debts, after five years of the end of the proceeding, or after 10 years of the end of the proceeding if there was any conviction for a bankruptcy crime.

The forced liquidation proceeding is a case of total judicial dissolution of the company. If, after the selling of all assets and the payment of creditors, there is any amount left – which is very difficult to identify – this amount will be given to the shareholders in proportion to their participation in the company’s equity.

ii Taking and enforcement of security

In Brazil, there are several types of security over assets. The main ones are: mortgage (over real state assets), pledge (over moveable assets) and fiduciary transfer of assets (real estate and moveable).

In judicial restructuring proceedings, credits secured by mortgage and pledge and existing at the date of the filing will comprise the secured creditors category, to the extent of the security it holds. Any disposal of collateral by the debtor should be previously approved by the relevant secured creditor. All the categories of creditors are paid according to what is established in the reorganisation plan. Therefore, the secured creditors subjected to the proceeding do not have alternative recourse to seek remedies for protection of their collateral,
other than negotiating the payment of the respective credit under the reorganisation plan. If the secured credit is not subject to the proceeding because of time limitation (credits constituted after the filing), it can be enforced.

Some creditors are not subjected to the judicial restructuring proceeding because of the security they hold: creditors secured by fiduciary transfers of assets, lessors, sellers in irrevocable real estate purchase agreements with instalment payments, and sellers of goods with title retention. This is because in such situations, the creditor is indeed the actual owner of the assets, even when the assets are being used by the debtor. Thus, the original contractual arrangements and corresponding debts remain in place, and the guarantee can be enforced in case of default. The only restriction is that for a period of 180 days from the authorisation of the judicial restructuring proceeding by the Bankruptcy Court, the sale or removal of assets that are essential to the activities carried out by the debtor is prohibited.

In forced liquidation proceedings, credits secured with mortgage and pledge (limited to the value of the collateral) are ranked behind labour credits (limited to 150 times the prevailing minimum wage) and credits deriving from accidents at work, but ahead of tax credits and unsecured credits. Also, credits with fiduciary transfer of assets are not subject to the legal preference order of payment in the forced liquidation proceeding and the respective creditor may request the restitution of their assets before the payment of any creditor.

For credits secured by mortgage or pledge that are not subject to the proceeding, the creditor may, if all requirements are fulfilled, file an enforcement proceeding against the debtor company by means of enforcement of the security and the credit, pursuant to the Brazilian Code of Civil Procedure. In such an enforcement proceeding, the creditor is able to seize and attach the guarantees granted by the debtor company and other assets, up to the full amount of the debt if necessary. The judicial enforcement proceeding may take a couple of years to be concluded, especially if there is a judicial restructuring in course, if enough assets are duly seized, attached and sold. If not, and the creditor has difficulty finding assets of the debtor company, it may take several years.

For enforcement of fiduciary transfer of real estate assets, when the debtor is not under forced liquidation, the mechanism applicable in case of default is provided by Law 9.514/97. The debtor shall be notified by the real estate registry office, upon request of the creditor, to pay the total debt and solve the arrears within 15 days. The payment has to be made to the real estate registry office, to be delivered within three days to the creditor, discounted the costs for collection and summons.

If the debtor does not make the payment, the real estate registry office shall certify this fact and register the consolidation of the asset ownership in the name of the creditor, after the payment of the correspondent transfer tax. The creditor will then have 30 days to promote public auction for the forced sale of the property.

In a first auction, the property can only be sold for an amount equal to or higher than the value of the asset stated in the agreement. If the asset is not sold in a first auction, another auction will be held within 15 days. In the second auction, the property can only be sold for an amount equal to or higher than the amount of the debt and related charges and expenses.

If the selling of the asset in a public auction occurs, the creditor will give the debtor the amount left after debt settlement and related charges and expenses are solved. If the property is not sold in the second auction, the claim or credit will be extinguished and the ownership of the real estate asset, which had been consolidated in the name of the creditor, will remain with him or her.
Also, Law 9.514/97 provides the possibility for the debtor to offer the creditor its right to the property of the asset, after the default and proceedings for the early maturity of the whole debt amount, making the proceeding of public auction dispensable. According to the referred legal proceeding, there is a risk that after the sale of the real estate asset in public auction and with the payment of the price, it could be considered a full discharge of all secured obligations and debt amounts, even if the outstanding debt is higher than the proceeds obtained, considering what is provided in Law 9.514/97. Recent case law defends that the full discharge only applies to housing finance.

For operations of fiduciary transfer of moveable assets by financial companies, the applicable proceeding is the one provided in Law 911/69, being the adequate proceeding to obtain the possession of the asset a lawsuit for search and apprehension of the assets. For operations of fiduciary transfer of moveable assets by non-financial companies, the applicable law is the Brazilian Civil Code. It provides that, if the debt is not paid in due time, the creditor shall sell, judicially or not, the assets to third parties, use the price obtained to pay the debt plus charges and expenses, and deliver the balance to the debtor, if any. In this case, the Civil Code provides that, if the price obtained with the selling of the assets is not enough to pay the debt, the debtor remains obligated to pay the remaining amount of the debt.

iii Duties of shareholders and directors of companies in financial difficulties

In forced liquidation proceedings, shareholders, controlling shareholders, directors and executive officers may be considered liable for debts and acts if the Court understands that some requirements have been fulfilled.

Regarding this topic, the BRL provides that the Bankruptcy Court may investigate and determine the shareholders’ and managers’ liability if it verifies that they performed any act or omission that contravenes Brazilian law – for example, corporate laws, tax laws and labour laws – regardless of the collection of the assets and impossibility to pay all the creditors of the company.

As an example, the Brazilian Corporate Law sets forth the definition and the rules of conduct that shall be observed by the controlling shareholder, and provides the liability rule applicable to the controlling shareholder. Also, the BRL provides the duties of the company’s directors and executive officers, and in case of violation of such duties or illegal acts in conducting the businesses, managers shall be deemed liable for their acts.

In principle, if the company’s shareholders or managers have contravened one of the legal provisions mentioned above, the Court may deem them liable for certain obligations or acts.

The BRL predicts that in those cases, a responsibility lawsuit will begin in the Bankruptcy Court, and in this lawsuit, the defendant’s assets can be blocked in compatible amount to the damage caused, until the final judgment. The term for the filing of a responsibility lawsuit ends two years after the decision that ends the forced liquidation proceeding becomes unappealable.

According to the Civil Code, the Court may disregard the company’s corporate veil if it considers that there was an abuse of its legal personality (in case of equity confusion and misuse of purpose). In this case, the shareholders would be considered liable for all of the company’s debts.
In limited liability companies, the shareholder’s liability is initially limited to the price of the stocks emission or to the full payment of the company’s capital (stock). As a rule, the company’s estate cannot be confused with the shareholder’s estate, and the company is the only one that responds for their obligation.

The possibility of piercing the corporate veil was created as an exception to the limited liability of the shareholders, and once decreed by the judge, the shareholders shall respond with their own assets for a specific obligation. This possibility is foreseen in the Civil Code, and can also be applied to a company that is bankrupted.

The essential requirements are: abuse of the corporate veil, with deviation of the company’s purpose or estate confusion between company and shareholders. In each concrete case, the judge will analyse the presence of such requirements – these requirements are more objective than just ‘fraud’ or ‘abuse’, but the decision by the Court remains very subjective.

Finally, if the public prosecutor understands that the shareholders, officers or directors committed a bankruptcy crime, he or she may file a criminal action. The BRL sets out several criminal offences related to bankruptcy, whose penalties can vary from one to six years of imprisonment, plus a fine.

iv Clawback actions

In case of forced liquidation, the BRL contains a list of actions that shall produce no effects with respect to the bankruptcy estate, regardless of whether the parties were aware of the financial difficulties facing the debtor or whether there was any fraudulent intent. Such actions are deemed incompatible with the reasoning underlying the BRL. Accordingly, they may be disregarded automatically by the court or at the request of any interested party.

Actions considered ineffective include, for instance: payment of unmatured debts during the suspect period; payment of overdue debts effected during the suspect period in a manner that is different from what was established in the original agreement; the creation of security interests during the suspect period to secure payment of preexisting indebtedness; and donations and other equivalent actions effected within the period of two years preceding the forced liquidation.

In addition to those actions deemed automatically ineffective, any action aimed at intentionally defrauding creditors may be revoked. In this case, however, the party seeking the revocation must prove, in a separate lawsuit, that there was a fraudulent scheme arranged between the debtor and a third party, and that the bankruptcy estate actually suffered damages as a result of such scheme.

The bankruptcy legal term, also known as the ‘suspect period’ or ‘look-back period’, shall be set by the court upon the declaration of forced liquidation. It may apply retroactively until 90 days before: the forced liquidation request; the application for judicial restructuring later converted into forced liquidation; or the first protest for non-payment lodged against the debtor.

III RECENT LEGAL DEVELOPMENTS

The BRL has been in effect for 12 years. In this time, it has only seen a few amendments and complements. The main ones are:

a Complementary Law No. 147/2014, which amended the BRL in relation to ‘small businesses’ (which are categorised as such by Brazilian law based on yearly revenues).
Small businesses are now a specific class of creditors and are classified as credits with special privileges, and now have specific provisions when companies are debtors in insolvency proceedings;

\textit{b} Federal Law No. 13.043/2014, which provides for a specific federal tax relief system for companies under judicial restructuring proceeding (REFIS). To be able to benefit from this relief system, some specific requirements must be fulfilled (such as not judicially discussing the tax debt to be renegotiated), and if the request is approved by the federal tax authorities, the debtor company will be able to pay its tax debts in up to 84 instalments. The first 12 instalments must correspond to 0.666 per cent of the debt; from the 13th to the 24th, the instalments must correspond to 1 per cent of the debt; from the 25th to the 83rd instalments, each shall correspond to 1.333 per cent of the debt; and the last instalment must correspond to the remaining amount of the debt. Also, the debtor company can only request this benefit once in each judicial restructuring proceeding, and it must refer to all of its federal tax debts.

\textit{c} Federal Law No. 12.767/2012, which determined that the proceeding of judicial and out-of-court restructuring are not applicable to public electricity service concessionaires, due to the negative effects of the judicial restructuring of Celpa. This is likely to occur in the future with other types of concessionaires.

\section*{IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES}

As mentioned above, Operation Car Wash, among other factors, led Brazil to a severe political and economic crisis, and several important infrastructure companies in Brazil requesting judicial restructuring proceedings. The most significant restructuring in 2016/2017 was Oi judicial restructuring proceeding, in which the debts exceeded 65 billion reais. It is so far the largest restructuring in Latin American history and will most likely be considered one of the most innovative judicial restructuring, since it will set new parameters and standards for such proceedings in Brazil, including changes in case law, that has evolved in the past years, and develop the proceeding itself, since adjustments have been made to be able to adapt to such a large restructuring.

The judicial restructuring of Abengoa is also a very significant judicial restructuring of the past year, along with PDG and Viver judicial restructurings, from the construction sector.

\section*{V INTERNATIONAL}

The Brazilian Bankruptcy or Restructuring Law does not contain any specific rules dealing with extraterritorial bankruptcy or insolvency proceedings or provisions regarding the recognition of other countries insolvency proceedings, unlike Chapter 15 of the US Bankruptcy Code, for example.

In fact, bankruptcy and restructuring proceedings involving Brazilian companies, with its centre of main interest in Brazil, or subsidiaries of foreign companies in Brazil, must necessarily be administered by a Brazilian court. The cases in which foreign companies (with no subsidiaries in Brazil) have had insolvency proceedings accepted by Brazilian bankruptcy courts are specifically related to companies that are part of Brazilian economic groups, established in other countries just for investment purposes, with no operation abroad.
Brazil has not adopted the UNCITRAL Model Law or any other treaty related to cross-border or multijurisdictional insolvency proceedings. As a result, any effects and consequences in Brazil of possible ancillary or parallel proceedings taking place in foreign jurisdictions must be dealt with on a case-by-case basis, subject to applicable conflicts of law provisions in cross-border matters.

There are, however, provisions in Brazil that allow recognition and enforcement of foreign decisions (interlocutory or final) by the Superior Court of Justice, once legal requirements are fulfilled, but not recognition of processes themselves. The decision must be in compliance with the Brazilian public policy, sovereignty and principles of morality, such as human dignity, and some formalities must be observed, such as sworn translation of the decision and notarisation or consularisation of signatures. Also, there must be an identified counter party, that has the right to present a defence.

VI FUTURE DEVELOPMENTS

The current economic and political crisis in Brazil, the volatility in the global market and the rise in corporate restructurings have had no impact on Brazil’s insolvency regime so far – only in the increase of the requests for judicial and out-of-court restructurings, due to the financial crisis the companies are going through.

However, these events have had a significant impact on the analysis made by the courts when judging appeals related to insolvency proceedings, with stricter control over the companies and higher interference in the commercial relations of the debtor companies.

There are several legislative bills and studies in course for major alterations of the LRF, to adjust its provisions to the current – and future – Brazilian political and economic scenario. The main one is being coordinated by the Ministry of Treasury and seeks to bring more protection for investing creditors. Also, the government is considering enacting a provisional measure or starting a legislative bill to allow intervention of the government in public telecom service concessionaries under judicial restructuring – motivated by the judicial restructuring of Oi.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

In 2017, the British Virgin Islands (BVI) was ranked as the world’s third most important funds, trusts and corporate services jurisdiction beaten only by the UK and Hong Kong.\(^1\) A survey of many key industry stakeholders returned the clear message that the BVI is likely to remain ahead of many other important jurisdictions, such as the Cayman Islands, Jersey and the US, for the foreseeable future, its prominence in the offshore market challenged only by the massive growth that is anticipated in Hong Kong and the interest surrounding developments in the UK.\(^2\) Because of its position and market share, the BVI has been described as a ‘super-jurisdiction’,\(^3\) and despite the growth in Hong Kong and the UK, it is still thought of as ‘the go-to for most structuring conduits.’\(^4\)

For the past three decades, the BVI has seen tremendous growth in its financial-services sector and in the incorporation of new companies. It is estimated that roughly 45 per cent of all offshore companies in the world are incorporated in the BVI,\(^5\) and in 2014, it was estimated that the BVI was the domicile for five times more incorporated companies than its nearest competitor.\(^6\) In addition to its pre-eminence in company incorporations, the BVI is establishing itself as a leader in the provision of fiduciary services, asset management, trust and estate planning and fund administration, as well as having a highly regarded legal system.

According to official statistics, there are 431,776 active BVI companies as of 31 March 2017, together with 1,139 private trust companies and 787 limited partnerships, and the first quarter of 2017 has shown a marked increase in company incorporations and the formation of limited partnerships on comparable periods in 2015 and 2016.\(^7\) In addition to...
corporate vehicles, the BVI promotes a number of regulated financial services, including the formation and regulation of offshore investment funds. The BVI is the second-largest offshore territory for offshore investment funds, with 1,426 active funds as at 31 March 2017. In 2007, the Financial Times published a survey showing that the BVI was the second-largest source of foreign direct investment worldwide, after Hong Kong.

Regulatory development is also gathering pace in the BVI as the Organisation for Economic Cooperation and Development continues to push for greater transparency and offshore financial centres come under increasing scrutiny both from international organisations and the general news media. The continued success of the BVI financial services industry is therefore dependent on safeguarding rigorous standards, remaining ahead of the curve in relation to its offshore peers, preserving its tax status, and ensuring the expertise, integrity and independence of its professional service providers.

II  GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i  Formal insolvency and restructuring procedures

Formal insolvency in the BVI was codified in January 2004 when the Insolvency Act 2003 (IA) came into force. The primary restructuring tools in the BVI continue to be schemes of arrangement and plans of arrangement. BVI legislation does not possess an equivalent regime to the United States’ Chapter 11 or the United Kingdom’s administration. Contrary to jurisdictions such as the Cayman Islands and Hong Kong, the use of provisional liquidations in the BVI continues to be the process of choice to deal with instances of risk of dissipation of assets and do not carry the same emphasis as a light-touch restructuring tool.

However, in this regard, we believe that following an increase in successful provisional liquidation appointments in the Cayman Islands, Hong Kong and Bermuda for the purposes of restructuring, the BVI may revisit the limitations of a provisional liquidation. Case law from other jurisdictions has evolved to provide more certainty on the powers of provisional liquidators, including the power to promote schemes of arrangement in the course of their appointment, or in the absence of finding a ‘white-knight’ for a prolonged period of time, and it may be that the BVI begins to follow this trend before too long, though legislation may be necessary.

At present, however, the most common ways in which a BVI company will seek to implement arrangements or reorganise or restructure its debts are the use of schemes of arrangement under the BVI Business Companies Act 2004 (BCA), plans of arrangement under the BCA, and the various liquidation procedures available under the BCA and IA.

9 Ibid, p. 4.


11 For example, the Hong Kong Court of Appeal in the case of Re Legend International Resorts Ltd [2006] 2 HKLRD 192 (HKCA) at 203f to i. [35] (Rogers VP); and Re Luen Cheong Tai International Holdings Ltd [2003] 2 HKLRD 719.

Schemes of arrangement

The BCA’s definition of ‘arrangement’ is very wide and includes reorganisations, mergers, consolidations, separations of businesses, dispositions of assets or businesses, dispositions or exchanges of shares or securities, amendments to memoranda and articles of association, dissolutions and, importantly, any combination of these. The purpose of a scheme of arrangement is for the company to agree a compromise with its creditors or shareholders to enable it to carry on as a going concern without entering into formal insolvency proceedings. A scheme may be initiated by the company, its creditors, its shareholders, or (if one has been appointed) its liquidator.

The BCA does not contain a great deal of detail with regard to the procedure for obtaining the court’s sanction of a scheme of arrangement. The BVI court has, therefore, tended to adopt the practice followed by the English courts and, in particular, in the Chancery Division’s Practice Statement (Companies: Schemes of Arrangement) [2002] 1 WLR 1345.

To initiate a scheme of arrangement, the company must be incorporated under the BCA (this includes BVI companies incorporated under the previous legislation and foreign companies validly continued as BVI companies). Dissolved companies and companies that have migrated away from the BVI cannot enter into schemes of arrangement; however, insolvent companies, companies at risk of insolvency and companies that have migrated to the BVI may.

A scheme may be proposed by the company, a creditor, a member, or a liquidator (if one has been appointed, whether solvent or insolvent). Once a scheme is proposed, an application must be made to the court for an order that a meeting of creditors or shareholders be convened. At the hearing of this application (known as the convening hearing) the court will consider issues of class composition and jurisdiction. As with an English scheme of arrangement, members and creditors are divided into classes depending on the respective rights that exist between them and the company, and the extent to which those rights stand to be varied by the scheme. The result is that often different classes of creditors and members are treated differently and a separate scheme meeting will be required for each different class.

If, at the meetings, a majority in number representing 75 per cent in value of the company’s creditors or shareholders (or class thereof) present or by proxy vote to approve the scheme, the scheme will bind:

- all creditors or shareholders (as the case may be);
- the company;
- any liquidator that has been appointed; and
- any contributory, subject only to the court’s approval.

If the scheme does not get the necessary majority, it will not be approved. If the creditors or shareholders vote to approve the scheme, then an application must be made for the court’s approval. The court will not then rubber-stamp the scheme simply because it has been approved at the scheme meeting: it will have to be satisfied that the scheme is fair and reasonable, and that it will be efficacious.

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13 Pursuant to Section 179A BCA.
14 Section 179A(2) BCA.
15 Section 179A(3) BCA.
16 Section 179A(3) BCA.
Once the court’s sanction has been obtained, every copy of the company’s memorandum and articles of association issued thereafter must have a copy of the order approving the scheme attached to it. Unless the company is insolvent when it proposes to enter into a scheme of arrangement, the directors will remain in control of the company; if the company is in liquidation, the liquidator will have control.

There is no fixed duration for a scheme of arrangement, and its length will be determined by the directions given by the court, the expedience with which meetings are convened, and the terms contained within the scheme itself.

In the BVI, the process of devising and obtaining sanction of a scheme of arrangement outside liquidation is not protected by any moratorium on creditors’ claims; however, once the court sanctions the scheme, it becomes binding on all creditors and shareholders, and the provisions of the BCA relating to mergers and consolidations of companies, plans of arrangement, disposition of large assets, redemption of minority shareholdings, and the rights of dissenters cease to apply.\(^\text{17}\) A scheme cannot be varied after its approval unless it contains an express provision to that effect.\(^\text{18}\)

Only creditors whose claims arise subsequently will be able to claim against the company during the term of the scheme. The company therefore remains at risk of aggressive creditors’ action unless it persuades the court to use its extensive discretionary powers to stay any proceedings or suspend the enforcement of any judgment or order for a specified period of time.

Although untested in the British Virgin Islands, it is to be hoped that the English case of *Bluecrest Mercantile BV and another v. Vietnam Shipbuilding Industry Group and others*\(^\text{19}\) will be followed. In that case Mr Justice Blair held that his discretion to grant a stay could be exercised in order to protect a proposed scheme of arrangement. Materially, he held that:

> It is clear that a vast amount of work has gone into this restructuring and, now that the requisite majority of lenders are agreed and 25 June 2013 is provisionally booked for the hearing, there is at least a reasonable prospect of the scheme finally going ahead. I agreed with [the Applicant] that matters have now reached a delicate stage. I am satisfied that unless I grant a stay now, there is a risk of exactly the kind of free-for-all that Thomas J feared in the Garuda Airlines case. The balance, in my view, is in favour of the proceedings.\(^\text{20}\)

**Plans of arrangement**

In contrast to schemes of arrangement and creditors’ arrangements which are based on English law, plans of arrangement were developed under Canadian law and first introduced into the BVI by the International Business Companies Act 1984.

If a company’s directors conclude that it is in the best interests of the company (or the members or creditors of the company) to enter into a plan of arrangement with the company’s creditors, they may formally adopt the proposed plan, after which an application

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\(^{17}\) Section 179A(8) BCA.

\(^{18}\) *Sport Financiera SA v. Olympic Gold Holdings Limited* BVIHC (Com) 452 of 2009, unreported (3 October 2013).

\(^{19}\) [2013] EWHC 1146 (Comm) (22 April 2013).

\(^{20}\) Ibid at [41].
must be made to the BVI court for approval. The court will issue certain directions such as which creditors or members should be notified, whether or not any approvals are needed, and whether or not any shareholders should be able to exercise their statutory right of dissent.

The directors will then confirm the plan and submit it to any other person whose approval the court directs must be obtained. Once all necessary consents have been obtained, the company must execute articles of arrangement and file copies with the Registrar of Corporate Affairs, who will register them and issue a certificate.

If dissenting shareholders who hold a simple majority vote against the plan, they have the power to prevent it from proceeding. If, however, a majority of shareholders votes in favour and the plan proceeds, any dissenting minority is bound by the majority, but dissenters have the statutory right to payment of the fair value of their shares.

As with schemes of arrangement under the IA, the process of proposing and applying for approval of a plan of arrangement does not trigger any moratorium, so companies remain vulnerable to creditors’ claims.

In the case of \textit{In re B&A Fertilisers Ltd; In re Rio Verde Minerals Development Corp}, a plan of arrangement was used as an alternative to the merger provisions under Sections 170 to 173 of the BCA. B&A Brazil wished to take over Rio Verde with the consent of Rio Verde’s board. The parties therefore proposed a plan of arrangement pursuant to which each member of Rio Verde would have its shares in Rio Verde exchanged for the equivalent number of redeemable shares in B&A. These redeemable shares would then be redeemed by B&A at the same share price as Rio Verde’s then share price the next business day. The effect of the plan of arrangement would be to achieve the takeover of Rio Verde by B&A.

This route was chosen as a means of enabling Rio Verde to divest itself of its obligations to the holder of some 18 million warrants. The original plan of arrangement had proposed that upon the merger each of the warrants were to be repurchased and cancelled by B&A for no consideration. The Commercial Court judge, however, rejected this proposal on the basis that it amounted to forfeiture, saying, ‘[T]here is nothing in Section 177 which permits a company to promote an arrangement under which property of any person is forfeited or confiscated and … the Court could not approve an arrangement which purported to have any such effect.’

The court gave directions that any plan would have to be subject to the approval of the warrant holder and that any plan affecting the warrant holder must entitle members of Rio Verde and the warrant holder to dissent in accordance with the provisions of Section 179.

\textit{Rio Verde} is significant for several reasons:

Firstly, Section 177 of the BCA does not provide that a threshold number of shareholders must approve the plan. This is in contrast to the 75 per cent in value test under a scheme of arrangement. Under Section 177(2) it is the directors of the company that determine whether or not the proposed plan is in the best interests of the company; however, the Court will not merely rubber stamp a plan of arrangement that has been proposed by the board under Section 177(2) but will assess it critically.

\begin{footnotesize}
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\item It is possible for a company in voluntary liquidation to enter into a plan of arrangement: in such a case, the liquidator completes the necessary procedural formalities; however, if a company is in insolvent liquidation, the liquidator is required to authorise the directors to take the procedural steps set out in the BCA.
\item In the event that ‘fair value’ cannot be agreed upon between the shareholders, there is a mechanism under Section 179 BCA to resolve the matter by reference to independent but party-appointed appraisers.
\item BVIHC (COM) 132 of 2012, unreported (22 January 2013).
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Secondly, Section 177 does not provide an automatic right to dissent. Under Section 177(4)(c), the Court has a discretion to allow any holder of shares, debt obligations or other securities to dissent under Section 179. In *Rio Verde* the judge considered that warrant holders would be within the ambit of Section 179 as holders of ‘other securities’ under Section 177(4)(c).

Once a final order approving a plan of arrangement is made, it cannot be appealed except on a point of law. If a party does wish to appeal on a question of law, the notice of appeal must be filed within 20 days immediately following the date of the order.

**Creditors’ arrangements**

Part II of the IA prescribes the procedure for creditors’ arrangements. The objective of the legislation is to make it relatively simple for the majority of the unsecured creditors of a company that is insolvent to reach an arrangement with the company for compromising the company’s debts and bind all the other unsecured creditors. A company may enter into a creditors’ arrangement even where it is in liquidation.24

A creditors’ arrangement may be proposed by any person, but a majority of 75 per cent of the company’s unsecured creditors by value must vote in favour of the arrangement in order to approve it and bind dissenters.25 A supervisor must be appointed to oversee the arrangement, and the supervisor must be a licensed insolvency practitioner. A disgruntled creditor or member may apply to the court for relief on the basis that their interests have been unfairly prejudiced.

An arrangement may compromise all or part of the debtor’s liabilities, and may affect the rights of creditors to recover all or part of their debts; however, it may not (without written consent) affect the rights of secured creditors or cause a preferential creditor to receive less than it would have received in the liquidation of the debtor, had such a liquidation commenced at the time the arrangement was approved.26

The procedure can be invoked even when a company is in liquidation. The most striking difference between this type of compromise and comparable regimes in other jurisdictions is that in the BVI the court is not involved, thereby (theoretically) making a binding compromise arrangement easier to bring about; similarly, there is no requirement to register the arrangement with the Registrar of Corporate Affairs. However, notwithstanding these refinements, the use of creditors’ arrangements has not yet proved popular in the BVI.

As in relation to other arrangement regimes in the BVI, no moratorium arises to protect the company from creditors’ claims during the period in which a creditors’ arrangement is being prepared and approved; however, as stated above, once the majority of creditors approve the arrangement, any creditors who dissented or did not vote are bound by the majority decision, even where they did not receive notice of the meeting at which the arrangement was proposed.27

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24 Section 17(4) IA.
26 Section 15 IA.
27 However, in certain circumstances creditors, members and other persons may apply to the court for relief on the basis that their interests have been unfairly prejudiced by the arrangement: Section 43 IA.
If a company is unable to reorganise itself using one of the procedures outlined above there are broadly two winding-up procedures in the BVI: liquidation by order of the court and liquidation at the instigation of the company or its members.28

**Liquidation by order of the court**

The company, a creditor, a member, a supervisor of a creditors’ arrangement in respect of the company, the Financial Services Commission (FSC) or the Attorney General may apply to the court for the appointment of a liquidator on the basis that the company is insolvent, that it is just and equitable to appoint a liquidator, or that liquidation is in the public’s interest. The court will appoint the liquidator, though the company’s creditors may vote to replace the court-appointed liquidator at the first creditors’ meeting. Directors’ powers, functions, and duties cease on the appointment of a liquidator, save to the extent they are permitted by the IA or authorised by the liquidator.

**Liquidation at the instigation of the company or its members**

A company may put itself into voluntary liquidation on either a solvent or an insolvent basis. In a voluntary solvent liquidation, under the BCA the directors resolve to place the company into liquidation, but must also determine that the company is both able to pay its debts as they fall due and that its assets exceed its liabilities. Normally, the shareholders must resolve to appoint a liquidator; however, if the company’s memorandum and articles of association permit, the directors can resolve to appoint a liquidator, though in such cases it is still necessary for the shareholders to approve the liquidation plan. Liquidation commences at the time the notice of the liquidator’s appointment is filed with the BVI Registry of Corporate Affairs. Once the voluntary liquidator is appointed, the directors remain in office, but their powers cease. The liquidator is required to consider the company’s solvency on an ongoing basis. If the liquidator forms the view that the company is insolvent, he or she must convert the liquidation to an insolvent liquidation. When the company’s affairs have been wound up, any creditors’ claims satisfied, and any surplus assets distributed among the company’s members, the company is struck off the register of companies and dissolved.

For a company to voluntarily enter insolvent liquidation, its members must resolve to appoint a liquidator by passing a special resolution.29 They must then notify the liquidator of his or her appointment. Once a liquidator has been appointed in this manner, the liquidation proceeds in much the same way as in the case of a liquidation by order of the court.30 The status of a liquidator appointed by way of a qualifying resolution pursuant to Section 159(2) of the Insolvency Act has also been considered by the High Court in Citco Global Custody NV v. Y2K Finance Inc,31 where Justice Bannister held:

> If they do that [i.e. pass a qualifying resolution under section 159(2) of the Insolvency Act 2003], the result will be a liquidation governed by the provisions of sections 175 to 232 of the 2993 Act and the liquidator account will be an officer of the Court (see section 184(1) of the 2003 Act). The

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28 It is important to note that the BVI legislation does not use the sometimes-arcane language of the UK legislation: it refers to ‘applications for the appointment of a liquidator’ rather than ‘winding-up petitions’.
29 Section 159(2) IA. Voluntary insolvent liquidation may also be used by companies where the directors are not comfortable signing a declaration of solvency.
30 Section 175 et seq IA.
31 BVIHCV 2009/0020A.
result would be no different from that which obtained when the Court appointed a liquidator under section 162 of the 2003 Act – in other words, both parties would be contending for an identical outcome. I suspect that Y2K may have formed the erroneous view that simply because section 159(2) permits the appointment of a liquidator to be made by the members, it results, as would a liquidation commenced by a similar route in England, in a voluntary liquidation. A voluntary liquidation of broadly similar effect to be commenced under Chapters II and III of the UK Insolvency Act 1986 can be carried out in the BVI only by making use of Division 1 of Part XII of the Business Companies Act 2004 (‘the 2004 Act’). 52

ii Enforcement of security

There are broadly seven types of security interest that can arise under BVI law: legal mortgage, equitable mortgage, equitable charge (fixed or floating), pledge, legal lien, equitable lien, and hypothecation or trust receipt. BVI companies are often used as holding vehicles either on a stand-alone basis or as part of a wider group structure when seeking to raise capital through debt financing, and there are a number of features of BVI law that make it particularly attractive to lenders to structure such transactions through a BVI entity or to use such a company as a security provider.

The enforcement of security interests is normally conducted in the jurisdiction where the relevant collateral is located. In most cases concerning the enforcement of security in assets located within the BVI, the assets in question are shares in BVI companies. As such, most of the legal issues that arise in this context are in relation to security over shares. In practice, the common-law remedies available in the BVI are similar to those remedies available under the laws of other common-law jurisdictions.

There are several other arrangements that parties can put in place that have the effect of conferring a type of security but that do not actually create a proprietary security interest in the subject matter. For example, it is possible to grant a power of attorney or conditional option in favour of the secured party relating to shares, to enter into a retention-of-title agreement, or to execute undated transfer instruments. While these methods may provide protection for the secured party, they do not confer a proprietary interest in the assets to which they relate, and for this reason they are not subject to the same legal considerations the courts have developed in the context of conventional proprietary security interests.

The range of remedies that is available to the security holder depends to a degree upon the type of security interest. Generally, the main types of security interest that can arise in relation to shares in a BVI company are a perfected legal mortgage, an equitable mortgage, an equitable charge (which may be fixed or floating) or a possessory pledge.

In the event that there is a default on the secured obligations, the holder of a security interest over shares may have up to four primary remedies (depending upon the type of security interest which they hold): foreclosure, power of sale, receivership or taking possession.

In addition, the holder of the security can usually sue upon the covenant to pay that appears in most security documents. There are other remedies available, in particular to the holder of a mortgage, but they relate predominantly to land and are rarely exercised in relation to shares, and so are not considered further here. The holder of a security interest is entitled to pursue all of its remedies concurrently or consecutively.

32 Ibid at [17].
Registration of security interests granted by companies is optional and not mandatory; however, unregistered security rights will be subordinated to registered charges and unregistered charges created before the BCA’s commencement date, and may encounter difficulties as against a liquidator.33

If a company goes into liquidation, the rights of secured creditors remain unaffected, unless there is a dispute over the validity of the security. After the commencement of the liquidation, the secured creditor can either value the assets subject to the security interest and, if there is a shortfall, prove for the balance as an unsecured creditor in the liquidation, or surrender his or her security interest to the liquidator and prove as a wholly unsecured creditor.

If the liquidator does not agree with the value placed on the asset by the secured creditor, he or she can require that the asset be offered for sale. The secured creditor will be paid his or her debt out of the proceeds of sale, and any surplus funds will be paid to the liquidator for the benefit of the general body of unsecured creditors.

A liquidator of a company in insolvent liquidation has the power to borrow money in the company’s name, if doing so is likely to be in the interests of the company’s creditors. In such circumstances the liquidator can grant post-commencement lenders security or higher priority than other creditors.34 A liquidator of a company in solvent liquidation also has the power to grant lenders security over the company’s assets; however, as stated above, the liquidator is required to keep the question of the company’s solvency under review and take care that borrowing does not cause the company to become insolvent. Unlike in some other jurisdictions, however, there is no provision in BVI legislation for the grant of super-priority status in respect of post-commencement finance, or for the grant of security over already-secured assets.

### iii Duties of directors of companies in financial difficulty

In the BVI, there is no express duty on the directors of a company to commence insolvency proceedings at any particular time; however, there is a substantial body of case law from a variety of common-law jurisdictions that suggests that in certain circumstances the directors’ duty to act in the best interests of the company as a whole (and not to any individual person or class of persons)35 will require them to take account of the interests of the company’s creditors:36 the directors are expected to regard the creditors’ interests as paramount, on the basis that the interests of the company are in fact perfectly aligned with the interests of

33 Section 166 BCA. See also Re Bond Worth Ltd [1980] Ch 228.
34 Section 186 and Schedule II, Paragraph 11 IA.
36 Walker v. Wimbourne and others (1976) 137 CLR 1 (HCA) at 6 to 7 (Mason J). Whether or not the directors or the company owe a duty to creditors in such circumstances does not appear to be settled: the preponderance of the academic authorities asserts that directors have a duty to consider creditors’ interests but not a duty to creditors to act in their best interests; however, some authorities argue that there is a duty owed to creditors as a whole.

Arguing for a duty: Nicholson v. Permakraft (NZ) Ltd [1985] NZLR 242 at 249 to 250 (Cooke J) (but this view was not concurred in by Richardson or Somers JJ); Hinnant, W. ‘Fiduciary Duties of Directors: How Far Do They Go?’ (1988) 23 Wake Forest Law Review 163; and Sappideen, R. ‘Fiduciary Obligations to
the creditors.\textsuperscript{37} In such circumstances, the directors must take those interests into account when deciding how to act until such time as solvency is restored, the company’s debts are restructured, or the company goes into liquidation.\textsuperscript{38}

As to the circumstances in which this shift in the focus of the company’s interests takes place, it has variously been said that it happens when the company is insolvent or of doubtful solvency, near to or in the vicinity of insolvency, or if a contemplated payment would jeopardise the company’s solvency or cause a loss to creditors.\textsuperscript{39} On balance, we take the view that for the directors’ duty to act in the best interests of the company to be aligned with creditors’ interests instead of shareholders’, the company must actually be insolvent or very close to it.

The term ‘director’ is defined as a person occupying or acting in the position of director by whatever name he or she is called, and can include former directors in certain circumstances. ‘De facto’ directors\textsuperscript{40} would be considered directors with all rights and liabilities attached

\textsuperscript{37} Colin Gwyer \& Associates Ltd and another v. London Wharf (Limehouse) Ltd and others [2003] BCC 885 (Ch) at 906, [74] (Leslie Kosmin QC sitting as a deputy High Court judge).

\textsuperscript{38} Kinsela and another v. Russell Kinsela Pty Ltd (in liquidation) (1986) 4 NSWLR 722 at 730 (Street CJ).

\textsuperscript{39} Nicholas v. Permakraft (NZ) Ltd [1985] NZLR 242 at 249 (Cooke J) and 256 (Somers J); Kinsela v. Russell Kinsela Pty Ltd (1986) 4 NSWLR 722 at 730 (Street CJ); Brady v. Brady (1987) 3 BCC 535 (CA) at 552 (Nourse LJ); Liquidator of West Mercia Safetyware Ltd v. Dodd and another (1988) 4 BCC 30 (CA) at 33 (Dillon LJ); Facia Footwear (in administration) v. Hinchcliffe [1998] 1 BCLC 218 (Ch) at 228b to c (Sir Richard Scott VC); and Dynasty Line Ltd (in liquidation) v. Sia Sukamto and another [2014] SGCA 21 at [34] to [35] (Sundaresh Menon CJ).

\textsuperscript{40} Persons acting as directors and carrying out their functions but without formal appointment as directors.
to them; however, the BCA’s definition of the term ‘director’ does not include ‘shadow directors’.41 In the BVI, it is common for a company to appoint a sole director, whether that be a natural person or a corporate person.42

Part IX of the IA deals with malpractice and the principal ways in which a director may be ordered to contribute assets to an insolvent company, including liability for misfeasance, fraudulent trading and insolvent trading. An application pursuant to Part IX can only be brought by a liquidator, but the provisions are not limited territorially.

**Misfeasance**

In the event that a director or officer of the company has misapplied or retained or become accountable for any money of the company, or if the director could be described as being ‘guilty of any misfeasance or breach of any fiduciary or other duty in relation to the company’,43 then the court has broad powers to make an order that such director or officer repays, restores or accounts for money or assets or any part of it to the company as compensation for the misfeasance or breach of duty. The IA misfeasance action merely puts on a statutory footing the powers at common law, but this statutory provision does not preclude any parallel liability arising under general directors’ duties at common law or otherwise.

**Fraudulent trading**

The court can make an order against a company’s directors if it is satisfied that, at any time before the commencement of the liquidation of the company, any of its business has been carried on ‘with the intent to defraud creditors of the company or creditors of any other person; or for any fraudulent purpose’.44 In such cases, the court can declare that the director is liable to make a contribution that the court considers proper towards the company’s assets. This is not limited to directors and officers, but applies to anyone who has been involved in carrying on the business in a fraudulent manner. There is no statutory defence to fraudulent trading, but it is necessary that actual dishonesty be proved.

**Insolvent trading**

If the court is satisfied that a director ‘at any time before the commencement of the liquidation of the company, knew or ought to have concluded that there was no reasonable prospect that

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41 The term ‘shadow director’ is given a statutory footing in the UK, and is defined by Companies Act 2006, Section 251, as ‘a person in accordance with whose directions or instructions the directors of a company are accustomed to act’; see also Revenue and Customs Commissioners v. Holland and another; In re Paycheck Services 3 Ltd and others [2010] UKSC 51, [2010] 1 WLR 2793. Although the BCA definition of ‘director’ does not extend to shadow directors, the IA definition does, save in the context of Parts IX and X of the IA, which relate to malpractice and disqualification respectively: Section 6 IA. The IA definition is in almost identical terms to the UK legislation, with the insertion of the words ‘may be required or’ before ‘are accustomed to act’. The consequence is that while shadow directors may not be subject to claims for breaches of duties owed under the BCA, they may find themselves defending IA claims by liquidators or other entitled persons.

42 In Revenue and Customs Commissioners v. Holland and others (op cit), the UK Supreme Court held that where a corporate person is a sole director (in that case of an English company), the directors of the corporate person will not be regarded as shadow directors or de facto directors of the company. This is likely to be persuasive in BVI law.

43 Section 254 IA.

44 Section 255(1) IA.
the company could avoid going into liquidation’, then the court can order any director to make such contribution to the assets of the company as it considers proper. The court cannot make an order against a director if it is satisfied that the director knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation, and that the director ‘took every step reasonably open to him to minimise the loss to the company’s creditors’. Any contribution that the court orders will be compensatory rather than penal, and the money recovered will be pooled with the general assets of the company for distribution by the liquidator. The court has broad powers to order such person to repay, restore or account for the money or assets, or pay compensation for such misfeasance.

iv Clawback actions

Part VIII of the IA provides a number of voidable-transaction claims by which a subsequently appointed liquidator may seek to recover company funds and property, thereby swelling the assets of the insolvent estate for the benefit of its creditors.

There are four types of voidable transaction that a liquidator may consider upon a company going into insolvent liquidation: unfair preferences, undervalue transactions, voidable floating charges and extortionate credit transactions. In relation to most of these, several defined terms are used: ‘insolvency transaction’, ‘vulnerability period’ and ‘connected person’.

In relation to unfair preferences, undervalue transactions, and voidable floating charges, the liquidator must show that the transaction was an ‘insolvency transaction’: the transaction in question must either have been made at a time when the company was insolvent, or have caused the company to become insolvent. For these purposes, ‘insolvency’ excludes balance-sheet insolvency: only cash-flow insolvency and technical insolvency are sufficient. The liquidator is not required to prove that an extortionate credit transaction is an insolvency transaction, and in relation to other types of voidable transactions, the court will sometimes presume that the transaction was an insolvency transaction, as explained below.

In relation to unfair preferences, undervalue transactions, and voidable floating charges, the ‘vulnerability period’ is the period beginning six months before the onset of insolvency and ending on the date on which the liquidator was appointed. If the transaction was with a person connected to the company, this period is extended to two years. In the case of extortionate credit transactions, the vulnerability period begins five years before the onset of insolvency and ends with the appointment of the liquidator. In relation to clawback actions brought in the context of liquidations, the term ‘onset of insolvency’ is defined as the date on which the application for the appointment of a liquidator was filed (in the case of insolvent liquidations by order of the court), or the date on which the liquidator was appointed (in the case of insolvent liquidations commenced by the members).

45 Section 256(1) IA.
46 Section 256(2) IA.
47 Section 256(3) IA.
48 Whether or not a transaction caused a company to become insolvent is a question of fact to be determined by applying the ordinary rules of causation, which in some cases concerning financially distressed companies can be very complex.
49 Section 244(3) IA.
A person is treated as being ‘connected’ to a company if they fall within the list of persons set out in Section 5 IA. This list includes directors or members of a company or of a related company, a different company that has a common director with the company, a company that is a subsidiary or holding company of the company, and relatives of directors.

A company gives an unfair preference if it enters into a transaction that would have the effect of putting a creditor in a better position in the event of the company’s liquidation than the position in which he or she would have been if the transaction had not occurred. The transaction will not be an unfair preference if it was entered into in the ordinary course of business. As stated above, the liquidator must show that the transaction was an insolvency transaction and that it took place within the vulnerability period. If the transaction took place between the company and a connected person, it will be presumed that the transaction was an insolvency transaction and that it did not take place in the ordinary course of business, unless the contrary is proved.

A company enters into a transaction at an undervalue if it transfers an asset to another for no consideration, or sells an asset for consideration that is worth significantly less than the asset’s market value. Again, and as stated above, the transaction must be an insolvency transaction and it must have taken place within the vulnerability period. The transaction will not be an undervalue transaction if it can be shown that the company acted in good faith and for the purposes of its business, and if at the time of the transaction there were reasonable grounds for believing the transaction would benefit the company. If the transaction is entered into between the company and a connected person, the court will presume that the transaction was an insolvency transaction and that the company did not act in good faith or have reasonable grounds for believing the transaction would benefit the company.

If the grant of a floating charge took place within the vulnerability period and was either made at a time when the company was insolvent or caused the company to become insolvent (ie, was an insolvency transaction), it will be voidable. If, however, the charge was not created in order to secure an existing debt, but secured new borrowing or liabilities, it will not be voidable. If a charge was created in favour of a connected person, it is presumed that the charge was an insolvency transaction.

Finally, a transaction is an extortionate credit transaction if it is concerned with the provision of credit to the company and either the terms of the credit arrangement require grossly exorbitant payments to be made in respect of the provision of credit (whether unconditionally or on the occurrence of certain contingencies) or otherwise grossly contravenes ordinary principles of fair trading. It is not necessary to show that the extortionate credit transaction was an insolvency transaction.

Despite this group of liquidator claims coming within the Part of the IA that is headed ‘voidable transactions’, a successful claim by the liquidator does not necessarily result in the

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50 Section 245 IA. Note that in the BVI (unlike in many other common-law jurisdictions) it is not necessary that the liquidator show that the transferor had any intention or desire to achieve this result for the recipient.
51 Section 252(2) IA.
52 In such cases it is still necessary to show that the transaction took place in the vulnerability period.
53 Section 246 IA.
54 Section 246(2) IA.
55 Section 247 IA.
56 Section 247(4) IA.
57 Section 248 IA. It is not sufficient that the transaction is merely unfair; it must be oppressive.
transaction being voided or becoming voidable at the liquidator’s election: the court has a very broad discretion as to what relief to grant, and may make any order it deems appropriate.\textsuperscript{58} It may order that the transaction be set aside in whole or in part, but it is not required to do so; alternatively or additionally, it may make such orders as appropriate to restore the parties to their original positions or otherwise.\textsuperscript{59}

### III RECENT LEGAL DEVELOPMENTS

#### i Amendments to the BCA: compulsory filing of companies’ registers of directors

The BCA has undergone some significant changes at the end of 2015 and the beginning of 2016, the most important of which relate to companies’ registers of directors. Formerly, Section 231 permitted a company to file copies of its register of members and its register of directors with the Registrar of Corporate Affairs. The position has now changed dramatically: the BVI Business Companies (Amendment) Act 2015 repealed Section 231, replaced Section 118 with a new version, and introduced Sections 118A and 118B, which make it compulsory for every company to maintain a register of directors containing specified information and file copies with the Registrar. These new provisions were further adjusted by the BVI Business Companies (Amendment) Act 2016.

Section 118 of the BCA contains the requirement that companies maintain a register of directors. Section 118A sets out the matters that must be recorded in the register of directors: as regards individual directors, the register must include their full name, any former name, their date of appointment or nomination as a director or reserve director, the date on which they ceased to be a director or reserve director, their usual residential address, their date and place of birth, and their nationality. If the director is a corporate entity, the register must include its corporate name, its corporate or registration number, its registered or principal office address, its postal address (unless it is a BVI company, in which case its registration number suffices), the date on which it was appointed as a corporate director, the date on which it ceased to be a corporate director, and its place and date of incorporation or registration.

Section 118B requires that a company’s register of directors be filed with the Registrar. A copy is required to be filed within 21 days after the appointment of the company’s first directors. The Registrar must be notified of changes to the register within 30 days of their taking place. Failure to file the initial copy of the register of directors, and failure to file notice of changes to the register within the relevant periods each attract a penalty of US$100.

Existing companies have until 31 March 2017 to bring themselves into compliance with these provisions. If they fail to do so, they will charged a penalty of US$300 for the first month of non-compliance, US$500 for the next period of three months (or part thereof), and US$750 for the following three months. If they still have not brought themselves into compliance within seven months of 31 March 2017, they face a penalty of US$1,000 for each month that their failure continues thereafter;\textsuperscript{60} it is possible, however, to apply for an extension of this deadline by up to six months.

Despite this new requirement that the Registrar have details of all companies’ directors, these registers are not publicly available. Any person wishing to inspect the copy of a company’s register of directors must apply to the court for an order. In addition, certain

\textsuperscript{58} Section 249 IA.

\textsuperscript{59} See also Section 250 IA.

\textsuperscript{60} Section 118B(9) and Schedule I, Part II, BCA.
‘competent authorities’ may be entitled to request to inspect the registers. Section 118B does not set out the basis on which the court may make an order permitting an applicant to inspect the copy of a company’s register of members filed with the Registrar, nor does it state who has standing to make such an application or what must be proved; nevertheless, it seems likely that Section 118B provides a route by which a person may seek to obtain disclosure of a company’s register of directors, and the court’s jurisdiction to allow inspection is likely to be the subject of development in the coming years.

The option to file a register of members with the Registrar is contained in the new Section 43A of the BCA. Where a company elects to file a register of members, it is bound by the copy of the register that is filed with the Registrar until such time as it files a change or notice that it intends to cease registration of the register. It should be noted that Section 43A, unlike Section 118B, does not suggest that registers of members filed with the Registrar may be disclosed by order of the court or to ‘competent authorities’.

**ii The test to be applied on an application to confirm, reverse or modify an act of an office holder**

In *Busch and another v. Russell Crumpler and another*,62 two unsecured creditors of a company in liquidation applied under Section 273 of the BCA for an order reversing the joint liquidators’ decision to reject proofs in the liquidation. The question before the court was what test should be applied when determining whether or not relief should be granted under that section. The first creditor complained that his claim had been rejected from proof when other analogous claims had been admitted. The second creditor asserted that the liquidators had been wrong to reject its claim to payment under the terms of a contract.

The judge was referred to the English authorities of *Re Edenno*note 63 and *Mohomed v. Morris*,64 as well as the BVI case of *Iceberg Transport and others v. Malone*,64 all of which approved the ‘perversity test’. Pursuant to that test, the court will only interfere with the act of a liquidator if he or she has done something so utterly unreasonable and absurd that no reasonable person would have done it. However, the judge also noted the exception to the rule in *Mitchell v. Buckingham International PLC*,65 namely that where the office-holder’s decision is concerned not with admitting or rejecting claims simpliciter or with valuing assets, but with managing competing creditors’ interests, the perversity test does not apply, and the court has a freer hand in reviewing the office-holder’s exercise of discretion.

The judge held that the first creditor’s application was to be determined by reference to the perversity test, and found that there had been no reasonable basis for the liquidators’ decision. He therefore set it aside and directed that the claim be admitted in the liquidation. The second creditor’s claim in the liquidation, however, turned on a question of contract law and was entirely unsuitable for determination under the Section 273 process. The judge held that while it was arguable that the perversity test was not engaged, in reality there was no basis on which to set aside the joint liquidators’ decision, and the second creditor would need to establish the contractual right to be paid before the liquidators’ decision not to admit the claim could be challenged.

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61 Section 118B(4) BCA.
62 BVIHC (COM) 30 of 2014, unreported (26 January 2016).
64 BVIHCV 130 of 2004, unreported.
iii Need to investigate the company's affairs as grounds for a just-and-equitable winding up

In *Parkmond Group Limited v. Richtown Development Limited*, the liquidators of Parkmond applied for an order putting Richtown into liquidation. Parkmond and Richtown were both companies within the same group, and the liquidators said that Richtown owed Parkmond US$12.549 million. The liquidators asserted that Richtown was unable to pay its debts and was, therefore, insolvent. In addition, the liquidators argued that Richtown had been so mixed up in intra-group fraud that it was necessary to wind the company up on the just and equitable ground.

The judge found that Richtown was insolvent, but in addition said that even if he was incorrect in that regard, it was just and equitable to wind the company up in any event. He noted that it was sufficient to grant an application on the just and equitable ground to find that the company's affairs were being conducted in an improper manner. He did not feel that he was able to make a finding of fraud; however, the directors of Richtown had failed to comply with repeated requests from the liquidators for information regarding group finances and had failed to comply with orders for the production of specific documents. He found that the directors had not complied with their duty to maintain records sufficient to show and explain the company’s transactions and enable them to determine the financial position of the company. It was this failure that had given rise to the suspicion of fraud, and this constituted sufficiently serious misconduct on the directors’ parts to make it just and equitable to liquidate the company.

IV INTERNATIONAL

When framing the final scope of the IA, the drafters were cognisant of the BVI’s position as a premier offshore jurisdiction and the numerous cross-border issues this brings. Part XIX of the IA provides the basic statutory framework for judicial assistance in insolvency proceedings. It allows foreign representatives in certain types of insolvency proceedings (i.e., collective judicial or administrative proceedings in which the property and affairs of the debtor are subject to control or supervision by a foreign court taking place in designated territories) to apply to the BVI court for assistance.

The BVI court, when faced with such an application, is required to do what will best ensure the economic and expeditious administration of the foreign proceedings, to the extent that is consistent with certain guiding principles. The orders that the court can make in aid of the foreign proceedings are wide, and include orders:

- a restraining the commencement or continuation of proceedings against a debtor or in relation to the debtor’s property;
- b restraining the creation, exercise or enforcement of any rights against the debtor’s property;
- c requiring a person to deliver up the property of the company to the foreign representative;
- d making any order or granting any relief the court considers appropriate to facilitate, approve or implement arrangements that will result in the coordination of BVI insolvency proceedings with foreign insolvency proceedings;

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66 BVIHC (COM) 55 of 2017, unreported (2 June 2017).
appointing an interim receiver of any property of the debtor; and

making such other order or granting such other relief as it considers appropriate.\(^\text{67}\)

The provisions appear to be wide enough for the BVI court not only to provide procedural assistance but also to apply substantive principles of BVI insolvency law, and the BVI court has discretion whether to apply the law of the BVI or the law applicable to the foreign proceedings.

The BVI courts have had a number of opportunities to consider the scope of Part XIX. In *Irving H Picard v. Bernard L Madoff Investment Securities LLC*,\(^\text{68}\) Mr Picard, the trustee appointed in the US liquidation of Bernard L Madoff Investment Securities LLC, sought: (1) recognition in the BVI as a foreign representative; (2) permission to apply to the BVI court for orders in aid of the foreign proceedings; and (3) permission to require any person to deliver up to him or her any property belonging to the company. Deciding the case against Mr Picard, Bannister J held that foreign representatives are confined to relying upon Part XIX, because the legislature had decided not to bring the alternative provisions in Part XVIII into force. The key difference between the two Parts was that whereas Part XVIII conferred status on foreign representatives through recognition of the foreign proceedings, Part XIX merely gave the foreign representative express rights to apply to the court for orders in aid, but without conferring status. The codification of rules on recognition of foreign office holders in Part XVIII had resulted in the implied repeal of the common-law rules of recognition, so Mr Picard could only rely on the support afforded by Part XIX. The court then held that because Part XIX operated on an ‘application-by-application basis it could not give Mr Picard any general authority or special status, but would have to hear individual applications for specific orders.

In *Re FuturesOne Diversified Fund SPC Ltd*,\(^\text{69}\) the court had to consider the position of a receiver appointed by the United States District Court for the Northern District of Illinois on the application of the United States Commodity Futures Trading Commission. An application had been made by the joint liquidators of certain funds incorporated in the BVI for a declaration that they had been validly appointed. The receiver applied to be added to the proceedings, either under the court’s inherent jurisdiction or under Section 273 of the IA as a person ‘aggrieved by an act, omission or decision’ of a company liquidator so that he could oppose the liquidators’ application and seek orders reversing everything that had been done, on the basis that it was done to avoid the effect of the order by which the receiver had been appointed. He also sought an order under Section 467 of the IA in support of the Illinois proceedings staying the BVI liquidations.

This case was also heard by Bannister J. In relation to the latter application, his Lordship held that the ability to make orders in aid of foreign proceedings was limited to foreign proceedings for the purpose of ‘reorganisation, liquidation or bankruptcy’, and that on the evidence before the court it appeared that the purpose of the US receivership was to protect investors rather than for any of the specified purposes. Accordingly, Bannister J held that the US-court-appointed receiver had no standing to make any application under Section 467 of the IA. In relation to the receiver’s application to reverse the acts of the liquidators, the court held that the liquidators’ claim that they had been appointed was not an ‘act, omission or
In the Matter of C (a bankrupt) concerned an application brought by trustees in bankruptcy who had been appointed under the laws of Hong Kong for recognition in the BVI of the Hong Kong proceedings and the trustees’ appointment. Bannister J reviewed his earlier decision in Picard v. Bernard Madoff Investment Securities LLC (supra) and stated that Part XIX was not an exhaustive code in relation to the court’s jurisdiction to assist foreign insolvency officials: the effect of Section 470 of the IA was to preserve the common-law jurisdiction to assist foreign representatives as defined in Section 466 IA.70 If the foreign office-holder came within that definition, the powers of the court in Part XIX would be available in addition to the common-law powers that had existed prior to the enactment of the IA. His Lordship also clarified the scope of that jurisdiction, stating that it was effectively limited to making orders for the purposes of preserving the integrity of the foreign bankruptcy procedures. He rejected submissions that if a foreign insolvency official were recognised by the BVI courts, they should be treated as having all the powers of an equivalent insolvency official under BVI law.

i UNCITRAL Model Law

Part XVIII of the IA adopts the UNCITRAL Model Law on Cross-Border Insolvency for giving and seeking assistance in insolvency proceedings; however, this Part has not been brought into force, and the generally held view is that it is unlikely to come into force; as with administration orders, however, this may be reconsidered in the future.

ii Liquidation of foreign companies

It should be stressed that the BVI courts will exercise insolvency jurisdiction over all companies registered in the BVI as of right, even if such a company does not have any assets in the BVI or has the its centre of main interests in another jurisdiction. The various insolvency regimes provided for in the IA and discussed in more detail above in this chapter are all available in relation to BVI companies, notwithstanding that they may not conduct business in the jurisdiction or indeed have any connection with the BVI other than the fact of their incorporation there.

The position with respect to companies that are not incorporated or registered in the BVI (defined as ‘foreign companies’ under the IA) is different. Foreign companies can enter into liquidation (through a court-appointed liquidator) provided that they have a sufficient connection with the BVI. For these purposes, ‘connection’ has a statutory definition and means the presence of assets in the BVI, the carrying on of business in the BVI, or the reasonable prospect that the appointment of a liquidator in the BVI will otherwise benefit

70 This Section requires that the foreign office holder be a person acting as an office holder in insolvency proceedings in a relevant foreign country designated as such by the Financial Services Commission of the BVI. If the jurisdiction in which the foreign office holder was appointed has not been designated by the FSC, Section 470 is of no assistance. This does however conflict with an earlier unreported decision where assistance pursuant to the common law was granted to a foreign insolvency professional from Curacao, a jurisdiction lying outside FSC designation.
the creditors of the company. Even if such a connection is established, the BVI court retains discretion regarding whether or not to appoint a liquidator. Administration and creditors’ arrangements are not available to foreign companies.71

iii Concurrent proceedings

If a BVI company has been wound up or is in the process of being wound up by a foreign court, it can nevertheless be placed in liquidation in the BVI by either of the two routes available (i.e., the appointment of a liquidator by the court or by the members of a company). A foreign company that is in liquidation abroad may also be placed in liquidation, but only through the mechanism of a court-appointed liquidator.

In such situations, the liquidation of the company in its place of incorporation will generally be regarded as the primary liquidation and, in common-law countries at least, all others will be treated as ‘ancillary’ or secondary liquidations in which the liquidator’s powers will be confined to collecting and distributing the assets in that jurisdiction.

If a liquidator is appointed over a BVI company, he or she becomes the appropriate person to deal with the company’s assets in place of the directors. The liquidator will be recognised as having the authority to administer the assets of the company worldwide, but the recognition of his or her authority abroad is effectively a matter for the foreign courts in the relevant jurisdiction. Most common-law jurisdictions will generally recognise a liquidator of a foreign company appointed by the court of the place of incorporation.

iv Judicial Insolvency Network guidelines

On 11 May 2017 the BVI’s Commercial Court formally adopted new guidelines for communication and cooperation between courts in cross-border insolvency matters. The initiative, which was the fruits of the Judicial Insolvency Network’s activities (JIN), has proved very popular among offshore practitioners and judges alike. The BVI is the latest key commercial jurisdiction to adopt the JIN guidelines this year, joining New York, Delaware, Singapore, and Bermuda. The guidelines are designed primarily to enhance communication between courts, insolvency representatives, and other parties as they deal with the vicissitudes of global restructurings and insolvency. With the increase in efficiency, it is hoped that stakeholders will see a reduction in delay and cost.

V FUTURE DEVELOPMENTS

There may be some movement in the jurisdiction towards the enactment of administration or an alternative regime that would be accompanied by at least a short-term moratorium on creditor enforcement.

The administration process is an alternative to liquidation for financially distressed companies; however, whereas the objective of liquidation is to realise the company’s assets for the benefit of its unsecured creditors, administration seeks to preserve the company as a going concern.

An application is made to the BVI court for an administration order. If the order is granted, then an administrator (who must be a licensed insolvency practitioner) is appointed

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71 It is possible to migrate a foreign company to the BVI for the purpose of making use of the BVI’s restructuring options under Part X BCA.
to administer the company’s assets; however, once the order is made, there is a moratorium on the exercise of creditors’ rights. None of the company’s creditors – including its secured creditors – may enforce their rights against the company while the order is in effect.

Under English law it is only necessary to show that an administration order is ‘likely to’ achieve one of the statutory purposes; however, in the BVI the requirement is to show that it ‘will’. Another important difference is that in the BVI an administration order can be made if it will facilitate the rehabilitation of a group of companies of which the company in question is a member, whereas under the UK legislation the order must be for the benefit of that specific company.

While it would appear unlikely at this stage that Part XVIII will be enacted to introduce the Model Law on cross-border insolvency, an extension of the countries designated by the FSC to which assistance will be extended would appear likely.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

Nine years after the financial crisis, the global economic recovery is somewhat more optimistic than last year, with global GDP growth projected to be 3.5 per cent by 2017, slightly up from last year.2 Fears of another international recession continue as global trade growth remains depressed and emerging market economies lose momentum, with sharp downturns in some emerging economies, especially those that are heavily reliant on commodity producers. The developments in China’s economy cloud the stability of the overall global upturn as economic growth is set to head further south, from 6.6 per cent in 2017 to 6.4 per cent by the end of 2018.

While the petitions being filed in the Cayman Islands during 2016 remained identical to the previous year, there were 13 fewer insolvency petitions. There were 46 insolvency petitions in 2016, making up two-thirds of the total petitions filed over the year. This is down from 2015 when insolvency petitions made up a remarkable 84 per cent of the annual total of petitions.3 Nevertheless, the Cayman Islands Monetary Authority (CIMA) continues to combat these uncertain times by introducing robust but market-flexible regulatory, monetary and cooperative initiatives to enhance market confidence and to maintain its reputation as a leading international financial centre.

The US is the largest source of foreign direct investment (US$260 billion, equal to 47 per cent) followed by Hong Kong (US$56 billion), the Netherlands (US$53 billion) and Brazil (US$52 billion). Outward direct investment from the Cayman Islands goes to Luxembourg, the US, Hong Kong, Singapore, the Netherlands and China. The Cayman Islands is the largest holder of US securities in the world (excluding long-term debt held by Chinese and Japanese central banks). Recently, there has been a massive increase in Japanese portfolio investment in the Cayman Islands, from US$574 to US$713 billion over the past year. This is double the portfolio investment from Hong Kong, which stands at US$337 billion and is largely due to special legislation enacted to attract investment funds specifically targeted at Japanese investors.4

The Cayman Islands’ banking sector continues to play a major part in the Cayman financial services sector, with 158 banks licensed as of the end of March 2017, with total international (cross-border positions in all currency and domestic positions in foreign currency) assets and liabilities of US$1.15 trillion and US$1.21 trillion, respectively, in

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1 Ian Mann, Chai Ridgers and Madeleine Heal are partners at Harney Westwood & Riegels.
2 OECD Economic Outlook June 2017, page 2.
4 Fichtner, J. Explaining Cayman’s success through its role in the Anglo-American triangle, 26 April 2017.

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June 2016.5 While the majority of these banks are subsidiaries, affiliates and branches of global financial institutions conducting business in the international markets, it is testament to the islands’ recognised and robust banking sector that 40 of the world’s top 50 banks hold licences in the Cayman Islands.

The 158 banks licensed in the Cayman Islands are categorised into A and B classes, with the former licensed to carry out local as well as international business. There are presently 11 Class A licensed banks in the Cayman Islands, six of which carry out retail services. The remaining banks hold Class B licences and are broadly restricted to offshore transactions with non-residents. We submit that the robustness and relatively regulator-friendly nature of the Cayman banking sector will see an increase in the use of Class B banks. Its flexibility will likely prove to be an attractive, alternative structure to sophisticated high net worth individuals as well as global corporations looking for a tax-efficient method to structure their intra-group financing.

Of the 158 banks licensed in the Cayman Islands, 36 are from Europe, 25 are from the US, 21 are from the Caribbean and Central America, 20 are from Asia and Australia, 16 are from Canada and Mexico, 35 are from South America, and five are from the Middle East and Africa. The volume of cross-border assets and liabilities held by Cayman banks has seen a gradual decline since June 2009, despite a slight increase in 2013. The decline is considered to be attributable to the hangover from the financial crisis impacting on international credit markets, and the contraction of the global economy, in particular in the eurozone, and most notably the emerging European markets that conduct transactions through the UK and the US, who in turn make up the rump of the international banking sector in the Cayman Islands. There has also been a healthy shift from the banking sector to the debt securities and investment funds market because of the relatively high performance of stocks and bonds.

Other parts of the Cayman Islands financial services industry are demonstrating resilience in the face of the new global order of international standards, transparency and heightened regulation. The Cayman Islands continues to be a leading jurisdiction for the incorporation of special purpose vehicles (SPVs) for the global structured finance market, given its tax-neutral status; buyers of debt issued by the SPVs can participate in the knowledge that they will only be taxed in their home jurisdictions. The vast majority of these SPVs are used to purchase loans issued by Wall Street and the European banks that are subsequently traded to other institutional investors.

The success of the Cayman Islands financial services industry is, therefore, the result of a number of factors, including its freedom of investment decisions for hedge fund managers, its tax-neutral status and the knowledge of experienced professional service providers in the Islands. The Cayman Islands’ globally renowned legal system has also provided a robust framework to effectively address restructuring or liquidity issues arising from the lingering effects of the credit crisis. The Cayman Islands has a globally recognised and comprehensive, creditor-friendly regime to facilitate domestic and cross-border insolvencies and restructurings, with effective procedural rules in place both for insolvency practitioners and the courts.

‘Light-touch’ restructurings by way of the appointment of provisional liquidators in the Cayman Islands continues to be a prominent feature for consideration by interested stakeholders, and we see no immediate signs of this trend abating given the preference by Asian clients to use companies incorporated in the Cayman Islands as their listing vehicle.

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5 Ibid.
In this regard, investors and opportunistic funds continue to keenly examine the Chinese debt burden and the far-reaching impact any market correction is likely to have on the global economy. Chinese regulators and banks have been on the offensive in reining in credit creation in light of the trend seen in 2016 of deteriorating credit quality. With overdue and non-performing loans rising as economic growth moderates, it remains to be seen if China can rein in credit creation without jeopardising its goal of sustaining GDP growth rates at above 6 per cent. Chinese banks are still by far the largest source of funding, facilitating massive lending for investment projects that are driven by the need to generate economic activity and employment.6

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Formal insolvency and restructuring procedures

The Cayman Islands legislative framework does not contain an equivalent regime to the United States Chapter 11 Bankruptcy Code or the United Kingdom’s administration restructuring tools to facilitate the rescue of an insolvent company (however, see Section IV as to proposed reforms). As a result, and in order to obtain the benefit of a moratorium against any proceedings continuing or being commenced against a company without leave of the Grand Court, companies tend to utilise the light-touch restructuring tool by seeking to appoint provisional liquidators pursuant to Part V of the Companies Law (2016 Revision) (the Companies Law), specifically Section 104(3), to assist the company in promoting a compromise or arrangement with its creditors. An application under Section 104(3) is usually made by the company on an ex parte basis on the grounds that the company is or is likely to become unable to pay its debts as they fall due and, as mentioned above, the company intends to present a compromise or arrangement to its creditors, most commonly by the promotion of a scheme of arrangement pursuant to Section 86 of the Companies Law. On the appointment of provisional liquidators, the Grand Court will determine which corporate powers will remain with the directors and which will be vested in the provisional liquidators.

The benefit of the light-touch restructuring process is that the appointment of provisional liquidators invokes the statutory moratorium on any proceedings, including winding-up proceedings by a creditor, being brought against the company.

Somewhat surprisingly, the Companies Law in its current state does not specifically provide for a creditor, a contributory or CIMA (in the case of regulated entities) to seek the appointment of provisional liquidators to promote a light-touch restructuring similar to Section 104(3). Instead, to have provisional liquidators appointed, these parties must first demonstrate that there are prima facie grounds to wind up the company, and that the appointment of provisional liquidators is necessary to prevent the actual or threatened dissipation of assets or mismanagement by the company’s directors.7 Such an application will ordinarily be inter partes; however, it can be made ex parte if exceptional circumstances can be shown. Given that there is no statutory fetter on the Grand Court’s discretion in respect of the functions and powers that may be given to the provisional liquidators, in appropriate circumstances, a ‘traditional’ dissipation of assets provisional liquidator should be able to

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6 Bloomberg, ‘Can China Really Rein in Credit?’ 15 June 2017.
7 Section 104(2) of the Companies Law.
promote a scheme of arrangement or other compromise or arrangement with the company’s creditors or members by virtue of the powers extended to official liquidators (which includes provisional liquidators, pursuant to Section 89 of the Companies Law) under Section 110(2) of the Companies Law. This proposition is supported by a number of recent Hong Kong decisions, most notably by the Hong Kong Court of Appeal in the case of Re Legend International Resorts Ltd, where it was held:

_The law on the appointment of provisional liquidators at present is contained in section 192 [equivalent to s.104(1) of the Companies Law] and the following sections and it is clear in the wording of those sections that the appointment of a provisional liquidator must be for the purposes of the winding up. Provided that those purposes exist there is no objection to extra powers being given to the provisional liquidator(s), for example those that would enable the presentation of an application under section 166 [equivalent to s.86 of the Companies Law dealing with schemes of arrangement]._

The decision in Re Legend International Resorts Ltd was followed in the subsequent Hong Kong decision in Re Plus Holdings Ltd,9 where the court empowered the provisional liquidators to promote a scheme of arrangement when the company had failed to find a ‘white knight’ for a period of two years and it was considered not to be futile for independent professionals to explore viable methods of restructuring.

Given that the primary purpose of a scheme or compromise between a company and its creditors is to return the company to solvency and allow it to carry on business for the benefit of its stakeholders, it is counter-intuitive for those stakeholders to have no entitlement to appoint provisional liquidators to achieve that purpose. When the question comes before the Grand Court for adjudication, it is expected that the Court will take a pragmatic approach consistent with the Hong Kong position and allow stakeholders to utilise a light-touch restructuring remedy.

The area of light-touch restructuring is still developing in the Cayman Islands, as evidenced in the ruling in Re Grant T G Gold Holdings Limited. Justice Segal released an Outline Ruling in the case, where the Court considered a creditor’s winding-up petition and application for the appointment of provisional liquidators. The company sought an adjournment of the petition in order to allow it to progress an early stage restructuring. Justice Segal found that in light of all the circumstances it would not be appropriate to order a winding up and he declined to appointed light-touch provisional liquidators to supervise any restructuring. In declining the winding-up order, Justice Segal seemed to rely on the principles espoused in Re Demaglass Holdings Ltd,10 in particular that in the absence of a good reason (such as the opposition of a majority of creditors or lack of prospective benefit from the appointment of a liquidator), a company’s unpaid creditor is entitled to a winding-up order virtually as of right. In the present case, the restructuring had the support of a significant group of creditors who also opposed the winding-up order and there was evidence that the appointment of provisional liquidators might negatively impact the proposed restructuring.

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8 [2006] 2 HKLRD 192 per Hon Rogers VP at Section 35; see also Re Luen Cheong Tai International Holdings Ltd [2003] 2 HKLRD 719.
9 [2007] 2 HKLRD 725 per Kwan J at Section 18.4
Instead, Justice Segal granted a short adjournment that would allow the company to progress its proposed restructuring, while ensuring the court could review the position in a timely manner to ensure that the position of all creditors was protected.

In a similar case before Chief Justice Ian Kawaley in the Bermuda Commercial Court, Up Energy Development Group Limited, Justice Segal’s ruling was relied upon by the company in an attempt to resist a creditor’s application for the appointment of provisional liquidators on the basis that it had appointed its own restructuring advisers and that deference should be given to the position of the majority of creditors, who also opposed appointment of the provisional liquidators. Chief Justice Kawaley did not appear to place much weight on Justice Segal’s ruling, and instead held that the role of provisional liquidators in insolvency restructurings was so deeply entrenched in Bermudian insolvency law practice that it was now a legitimate expectation of stakeholders. The Chief Justice went on to state there was a strong starting assumption in favour of the appointment of provisional liquidators and it would be a heavy burden to displace. Chief Justice Kawaley appeared to distinguish the position in respect of the weight to be given to the view of the majority creditors when deciding: (1) whether or not to adjourn for restructuring purposes rather than immediately order a winding up – which would ordinarily be considerable (consistent with Re Demaglass Holdings); and (2) whether to appointment provisional liquidators to monitor a restructuring process – which the court was not obliged to blindly follow.

As of publication, Justice Segal’s full judgment has yet to be released and it will be curious to see whether he delves deeper into the relevant legal principles and considers the wider impact that the appointment of provisional liquidators can have beyond simply preventing a winding up. At the least, these decisions are interesting to the extent that they appear to evidence a dichotomy between the Cayman and Bermuda positions regarding the appointment of light-touch provisional liquidators where a restructuring is proposed.

In continuing with Bermuda position to inform us on the possible path the Cayman Islands may take with regards to light-touch provisional liquidators and restructuring, Chief Justice Kawaley in Z-Obee Holdings Limited appointed Hong Kong restructuring provisional liquidators as joint provisional liquidators over a Bermuda-incorporated company for the express purpose of initiating a restructuring. Z-Obee applied to appoint Hong Kong provisional liquidators as Bermuda provisional liquidators for the explicit purpose of restructuring the company. It was explained to the Bermuda Court that an important reason for the application was the inability of the Hong Kong court to use provisional liquidators for restructuring purposes under Hong Kong law. Once the Bermuda provisional liquidators were appointed, they would ask the Bermuda court to issue a letter of request to the Hong Kong court for recognition and assistance in the standard form acceptable to the Hong Kong court.

In a remarkable piece of judicial cooperation, Mr Justice Jonathan Harris of the Companies Court of the High Court of Hong Kong had earlier adjourned a winding-up petition in relation to the company in Hong Kong precisely so that an application to appoint restructuring provisional liquidators in Bermuda could be made, thereby making modern restructuring law available to an offshore incorporated, Hong Kong listed company. Parallel schemes of arrangement in both Hong Kong and Bermuda would likely be the restructuring

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11 In the matter of Up Energy Development Group Limited [2016] SC (Bda) 83 Com (20 September 2016).
13 Re Z-Obee Holdings Ltd HCCW 85/2014 (27 June 2016).
tools of choice. To progress the restructuring, Hong Kong provisional liquidators were later discharged so that the joint provisional liquidators appointed in Bermuda could seek recognition of their appointment in Hong Kong. At that point, the joint provisional liquidators may introduce parallel schemes to ultimately effect the restructuring of the company in Hong Kong and Bermuda.

The decisions by Chief Justice Kawaley in the Bermuda Supreme Court and Mr Justice Harris in the High Court of Hong Kong demonstrate the common law recognition and assistance techniques available to the courts and practitioners in attempting to solve problems encountered in cross-border insolvency. Furthermore, the case of Z-Obee goes to mitigate the effects of the Legend case that held that the statutory power to appoint provisional liquidators under the Companies Ordinance in Hong Kong to restructure a company's debt, as opposed to preserve assets, is impermissible.

With the judicious use of these staged applications in the offshore and onshore courts, Z-Obee has successfully ‘slingshotted’ modern offshore restructuring law into an onshore jurisdiction. It will be very interesting to see how the decision of Z-Obee will affect cross-border insolvency in the future, particular for the Cayman Islands since it has a similar ‘light-touch restructuring’ regime to Bermuda. There is no reason, in principal, why the procedure used in Z-Obee could not be used for the restructuring of a Cayman Islands company.

The full extent and effect of the Cayman Islands’ light-touch restructuring regime was demonstrated in the restructuring of Mongolian Mining Corporation in the first half of 2017. Mongolian Mining was a Cayman incorporated, Hong Kong Stock Exchange listed, coking coal producer and exporter operating in Mongolia. The company struggled with declining coal prices, caused by oversupply and a weakening demand for China’s steel industry, leading to the need to restructure more than US$760 million in offshore domiciled debt. The restructuring was executed by way of a Cayman Islands provisional liquidation of Mongolian Mining, parallel schemes of arrangement under the laws of the Cayman Islands and Hong Kong, bespoke out-of-court consensual arrangements with certain creditors and recognition of the Cayman Islands provisional liquidation proceedings and schemes of arrangement in the United States under Chapter 15 of the US Bankruptcy Code. This successful restructuring was a favourable outcome for Mongolian Mining and its stakeholders and has reinforced the Cayman Islands as a leading restructuring jurisdiction, thanks to the Cayman Island courts, legislative framework and insolvency practitioners.

A company may seek to promote a scheme of arrangement outside of provisional liquidation to make a compromise or arrangement with its members or creditors (or any class of them). An application may be brought by the company itself, any creditor or member of the company or, where the company is being wound up, by the liquidator, and the Grand Court may order a meeting of the company’s creditors or members. If a majority in number representing 75 per cent in value of creditors or members present, either in person or by proxy and entitled to vote at the meeting, agree to the terms of the proposed compromise or arrangement, then, subject to the Grand Court’s sanction, the scheme will be binding on all of the creditors or members of the company and against the company itself and, if the company is in liquidation, against the liquidator and contributories of the company. The scheme becomes effective only once a copy has been delivered to the Registrar of Companies for filing.

Where a scheme is being promoted outside of provisional liquidation, the directors of the company will remain in control of the company and will formulate the terms of the proposed compromise to be put to its creditors or members (in practice, this will almost
always be done with the assistance of qualified insolvency practitioners who will become the scheme supervisors upon the company’s creditors or members and the Grand Court approving the scheme. The promotion of a scheme of arrangement outside of provisional liquidation therefore does not afford the company the benefit of the moratorium. The company remains at risk of aggressive creditor action unless it can persuade the Grand Court to use its extensive discretionary powers to stay any proceedings or suspend the enforcement of any judgment order for a period of time. Although untested in the Cayman Islands, it is to be hoped that the English case of Bluecrest Mercantile BV and another v. Vietnam Shipbuilding Industry Group and others\textsuperscript{14} will be followed. In that case Mr Justice Blair held that his discretion to grant a stay could be exercised in order to protect a proposed scheme of arrangement. Materially, he held that:

\textit{It is clear that a vast amount of work has gone into this restructuring and, now that the requisite majority of lenders are agreed and 25 June 2013 is provisionally booked for the hearing, there is at least a reasonable prospect of the scheme finally going ahead. I agreed with [the Applicant] that matters have now reached a delicate stage. I am satisfied that unless I grant a stay now, there is a risk of exactly the kind of free-for-all that Thomas J feared in the Garuda Airlines case. The balance, in my view, is in favour of the proceedings.}\textsuperscript{15}

There are broadly two winding-up procedures in the Cayman Islands: compulsory liquidations by order of the Grand Court and voluntary liquidations. The Grand Court has jurisdiction to make a winding-up order in respect of any company incorporated or registered in the Cayman Islands or a foreign company that:
\begin{itemize}
\item[a] has property located in the Islands;
\item[b] is carrying on business in the Islands;
\item[c] is the general partner of a limited partnership; or
\item[d] is registered under Part IX of the Companies Law (overseas companies).
\end{itemize}

\textbf{Compulsory liquidation}

An application to the Grand Court to wind up a company is by petition and made either by the company itself, any creditor (including any contingent or prospective creditor), any contributory of the company, or the CIMA in the case of regulated entities. The most common grounds upon which the Grand Court will order the winding up of a company is on the basis that it is unable to pay its debts as they fall due, or that it is just and equitable to do so.\textsuperscript{16} In respect of a winding up on the insolvency ground, the test for solvency is a cash-flow test.

At any time after the presentation of a winding-up petition but before the making of a winding-up order, upon an application by the company, a creditor or contributory, the Grand Court may stay or restrain any proceedings against the company on such terms as it deems fit.\textsuperscript{17} Once a winding-up order is made or a provisional liquidator is appointed, the statutory moratorium is invoked and no suit, action or other proceedings, including criminal proceedings, may be proceeded with or commenced against the company except with the

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\textsuperscript{14} [2013] EWHC 1146 (Comm) (22 April 2013).
\textsuperscript{15} Ibid at [41].
\textsuperscript{16} Sections 92(d) and 92(e) of the Companies Law.
\textsuperscript{17} Section 96 of the Companies Law.
leave of the Grand Court. Section 99 of the Companies Law also provides that once a winding-up order has been made, any disposition of the company’s property and any transfer of shares made after the commencement of the winding up is, unless the Court otherwise orders, void.

Once a winding-up order has been made and official liquidators are appointed, the powers of the directors are automatically terminated. Where the liquidation is of a cross-border nature, it is now common for there to be more than one liquidator appointed over the undertaking, assets and property of the company, with an overseas qualified liquidator dealing with the assets and investigations outside of the Cayman Islands. The Insolvency Practitioner’s Regulations 2008 require that, in such circumstances, there must be at least one qualified insolvency practitioner resident in the Cayman Islands appointed over the company.

In The matter of Primeo Fund (in Official Liquidation), the Court of Appeal distinguished between liquidators’ statutory obligations under the Companies Law and their obligation as litigants before the court. In these proceedings, the joint official liquidators of Primeo sought damages against the Bank of Bermuda and HSBC. The bank defendants claimed the liquidators had not complied with their discovery obligations and sought to compel the liquidators to issue a letter of request under section 103 and the collecting of books and records of the company under Section 138 (both of the Companies Law) against a bank in Austria.

At first instance, Justice Jones ordered that the joint official liquidators issue the letter of request under Sections 103 and 138. However, this decision was overturned by the Court of Appeal on the basis that: (1) the defendants were attempting to use the liquidators’ statutory powers to seek documents from a third party in circumstances where Grand Court Rules did not provide for third party discovery; (2) the first instance judge had conflated the liquidators’ statutory duties with the obligation to give discovery under civil procedural law and had wrongly suggested liquidators have to go so far as to assist adversaries to obtain documents in the course of litigation; (3) the court should not interfere with the conduct of the liquidator other than in exception circumstances and the rationale for making the order came ‘nowhere near’ meeting the exceptional circumstances test set out in Eden; (4) the liquidators’ statutory powers are not for the benefit of a party in the liquidation, where the exercising of those powers does not serve the liquidation; and (5) it is an abuse of power if statutory powers conferred for a certain purpose are deliberately used to obtain a result outside the contemplation of the law creating the power.

The official liquidators will take control of the company’s affairs and will seek to realise its assets for the benefit of its stakeholders (which in the case of an insolvent company will be its creditors) as a whole and make a distribution in accordance with the statutory priorities under the Companies Law, having first paid all the costs and expenses in the liquidation. The appointment of official liquidators does not prohibit secured creditors from enforcing their security; however, the secured creditor may request the liquidator to realise the assets

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18 Section 97 of the Companies Law.
19 A winding up is deemed to commence at the time of the presentation of the petition (Section 100(2) of the Companies Law).
subject to its security. If the liquidator does so, he or she will be entitled to deduct his or her reasonable costs of realising the assets before distributing the balance of the proceeds to the secured creditor.

After considering secured creditors and paying all costs and expenses in the liquidation, realisations will first be applied to pay all preferential debts, which broadly comprise certain debts due to employees and the Cayman Islands government, subject to a maximum amount prescribed by the Companies Law. Any remaining unsecured creditors will receive a distribution according to the level of their debt, with any surplus after satisfying all creditor claims being paid to the members of the company. In the event that there are insufficient assets in the liquidation to satisfy the claims of all unsecured creditors, then debts and liabilities of the company (other than any due to members in their character as such) will be paid on a pari passu basis. Member claims rank lower in priority than claims of ordinary creditors.22

Voluntary liquidation

A voluntary liquidation is commenced by passing a members’ resolution, upon the expiry of a fixed period or upon the occurrence of a specified event stated in the company’s memorandum and articles of association. A company resolves by special resolution that it be wound up voluntarily or if the company, in general meeting, resolves by ordinary resolution that it be wound up voluntarily because it is unable to pay its debts as they fall due.23 The voluntary liquidation of the company commences upon the passing of the resolution, the expiry of the fixed period or the occurrence of the specified event.24

A liquidator appointed to conduct a voluntary liquidation does not require the Grand Court’s authorisation to exercise his or her powers; however, the liquidator can apply to the Court to determine any question that arises during the winding-up process. A voluntary liquidator is required to apply to the Grand Court for an order that the liquidation continues under the Grand Court’s supervision unless, within 28 days of the liquidation commencing, the directors sign a declaration that the company will be able to pay its debts in full (with interest) within a period not exceeding 12 months after the commencement of the liquidation. The making of a supervision order effectively converts a voluntary liquidation to an official liquidation, and the provisions of Part V of the Companies Law will apply.

Even after the directors make such a declaration, the liquidators or any creditor or member can apply to bring the liquidation under the Grand Court’s supervision if the company is or is likely to become insolvent, or court supervision will facilitate a more effective, less expensive or quicker liquidation of the company in the interests of the creditors and members. The liquidation will then continue as a compulsory liquidation.

In certain circumstances where directors of the company determine that the company is insolvent and cannot trade out of its difficulties or find new funding, it might be appropriate to pass an ordinary resolution of its members to place the company into voluntary liquidation followed by confirmation that the directors are not able to sign the declaration of solvency. The voluntary liquidator can then apply to the Grand Court for a supervision order and seek appointment as official liquidator.

The appointment of liquidators in these circumstances may help circumvent any challenges or concerns as to whether directors are entitled to present a winding-up petition

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22 Section 37(7) of the Companies Law.
23 Section 116 of the Companies Law.
24 Section 117 of the Companies Law.
in the company's name. In the recent case of CHC Group Ltd Justice McMillan considered both the decisions of Justice Jones in Re China Milk Products Group Limited,25 where it was held that directors of an insolvent company would be allowed to present winding-up petitions on behalf of their companies without approval by the shareholders, and the decision in Re China Shanshui Cement Group Limited26 where Justice Mangatal reached a different conclusion in deciding that directors of a company do not have standing or authority to present a winding-up petition nor the power or authority to apply for the appointment of joint provisional liquidators unless they are expressly authorised to do so by the company's articles of association or a valid shareholder resolution has been passed.27

Justice McMillan distinguished both China Milk and China Shanshui on the basis that they had no bearing on the present situation where there was a separate creditor winding-up petition in existence, which was then followed by an application by the company, acting by its directors, for the appointment of joint provisional liquidators for the purpose of restructuring. It was held that where a creditor has already filed a winding-up petition in respect of a company, not only may the directors of the company apply for the appointment of joint provisional liquidators, but also that they may take that step without a shareholders resolution or express provision in the company's articles of association. This interpretation appears to contradict the English common law position in Re Emmadart Ltd28 as well as the Cayman Islands' common law position in China Shanshui. The case of CHC Group confirms the workaround of having a creditor, not the company, file the petition underpinning the proceedings for provisional liquidation for the purposes of restructuring.

ii Taking of enforcement of security

The most common forms of security in the Cayman Islands are mortgages and fixed and floating charges over a company’s property, undertaking and assets. Secured creditors can therefore appoint receivers over charged assets to enforce their security interests; the security instrument will ordinarily detail the assets that the receiver will be appointed over and the extent of the receiver's powers. Receivers are not supervised by the court, and usually owe their duties to the secured creditor appointing them and not the company.

The security instrument may detail enforcement provisions other than the appointment of receivers, and may include the right for the secured creditor to take possession of and vote in relation to the charged assets, sell the charged assets to a third party, or effect any contractual right of set-off or otherwise.

iii Duties of directors of companies in financial difficulty

While there is no statutory obligation on a company or its directors to commence winding-up proceedings, the Companies Law and the common law do impose various duties and responsibilities on directors to the company. If a company is insolvent or it is likely to become insolvent, the duties and responsibilities of its directors also extend to the interests of the company's creditors. Directors and officers of a company also include shadow directors.

A shadow director is defined as any person in accordance with whose directions or instructions the directors of a company are accustomed to act, provided that a person is

25 Re China Milk Products Group Limited [2011 (2) CILR 61].
28 Re Emmadart Ltd [1979] Ch. 540.
not deemed to be a shadow director by reason only that the directors act on advice given by him or her in a professional capacity. Therefore, an investment manager of a company making recommendations as to the purchase or sale of investments should not, for example, ordinarily constitute a shadow director. Importantly, however, unlike in other common law jurisdictions, the Companies Law does not expressly subject shadow directors to the common law or equitable duties imposed on de jure directors. Rather, shadow directors are only subject to penalties for fraudulent trading, misconduct in the course of a winding up and making a material omission in any statement relating to the company’s affairs.

The Companies Law contains numerous provisions relating to the duties of directors and prescribes penalties for any breach. The most serious of these involve dishonesty or the authorising of illegal payments and carry both criminal and civil penalties. The insolvency provisions of the Companies Law also include certain offences against directors, such as fraud in anticipation of winding up, transactions in fraud of creditors, misconduct in the winding up and fraudulent trading. These proceedings are commenced by the official liquidator and, if proven, the Grand Court will order the director to contribute to the losses suffered by the company as a result of his or her actions.

The memorandum and articles of association will also detail the general duties that directors owe to the company. In addition, given that there is no statutory codification of the general duties and liabilities owed by directors to its company in the Cayman Islands, principles have developed that derive from English common law. At common law, a director owes two types of duty to the company: fiduciary duties, and duties of skill, care and diligence. Directors’ fiduciary duties to their company can broadly be described as their duty to act in good faith in their dealings with or on behalf of the company, and to exercise the powers and fulfil the duties of the office honestly. In recent years, English and Commonwealth authorities have moved from the traditional purely subjective test referencing the individual director whose conduct is being judged, towards an objective test for the applicable standard of skill and care that a director will be required to have. Following these cases, it is likely that the applicable skill and care test will be that of:

\[
A \text{ reasonable diligent person having both – (a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the same functions as are carried out by that director in relation to the company, and (b) the general knowledge, skill and experience that that director has.}^{34}
\]

Therefore, there is a minimum objective standard based upon the functions given to the director in question, but the standard can be raised where the director in question has more knowledge, skill and experience than would normally be expected (e.g., if he or she has been recruited as an expert in a particular business of the company). Breaches of these duties may

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29 Section 134 of the Companies Law.
30 Section 135 of the Companies Law.
31 Section 136 of the Companies Law.
32 Section 147 of the Companies Law.
33 Fiduciary duties covered by the general obligation include duties to act in good faith; to exercise powers in the company’s interests; to exercise unfettered discretion; not to make a secret profit; to avoid any conflict of interests; and to make disclosure where appropriate.
result in the director being held personally liable, and a subsequently appointed liquidator can bring an action to recover losses on behalf of the company that derived from the director’s breach of duty.

iv Clawback actions
The Companies Law provides for a number of clawback actions to enable a subsequently appointed liquidator to recover assets belonging to the company and thereby maximise returns for stakeholders. For example, when a company is being wound up or falls under the supervision of the Grand Court, all dispositions of the company’s property and any transfer of shares of the company made between the date of the presentation of the petition and the making of the winding-up order are void, unless the Grand Court orders otherwise.35

Clawback claims can be divided into claims against members of the company to recover redemption payments, and claims against other third parties to recover company assets.

A payment out of capital to a member made at a time when the company is insolvent, or that has the effect of rendering the company insolvent, is void.36 In the event of such an unlawful payment, it is arguable that the effect of the illegality is to render the payment subject to a claim in restitution by the liquidators.

A clawback of redemption payments may also be available where members have been overpaid as a result of a misstated net asset value attributed to the company’s property. In the case of a solvent company that has issued redeemable shares at prices based upon its net asset value from time to time, the liquidator shall have power to settle and, if necessary, rectify the company’s register of members.37 This power of rectification may be exercised where the misstated net asset value is not binding upon the company and its members by reason of fraud or default.38 This statutory restatement procedure does not expressly provide for repayment by former investors of any sums that they have been overpaid; nor does it provide for any procedure to be invoked by the liquidators to make such recoveries. It would, therefore, seem to logically follow that on a restatement of the net asset value of the company, and consequent rectification of the register of members, economic consequences, should follow.

Although the existence of this power must be considered in light of the Privy Council decisions in *Fairfield Sentry Ltd v. Migani* [2014] UKPC 9 and *Pearson v. Primeo Fund* [2017] UKPC 19, the effect of which was to allow former members or redemption creditors to retain redemption payments or enforce redemption claims against a BVI and Cayman company respectively, despite the fact that the net asset value of the shares in question were calculated by reference to fictitious assets and profits. It should be noted that neither the scope nor application of Section 112(2) of the Companies Law was considered by the Board in *Pearson v. Primeo Fund* so this may yet be the subject of litigation in future.

In relation to third-party recipients of company assets, any transactions in which property of the company is disposed of at an undervalue with the intention of defrauding

35 Section 99 of the Companies Law.
36 Section 37(6)(a) of the Companies Law: ‘A payment out of capital by a company for the redemption or purchase of its own shares is not lawful unless immediately following the date on which the payment out of capital is proposed to be made the company shall be able to pay its debts as they fall due in the ordinary course of business.’
37 Section 112(2) of the Companies Law.
38 Order 12, Rule 2(1) of the Companies Winding-Up Rules 2008.
the company’s creditors are void upon an application by the official liquidator.\(^{39}\) The official liquidator must commence such proceedings within six years of the disposition, and the burden of proof will be upon the liquidator to demonstrate that there was an intention to defraud.

A transaction can also be set aside on the basis that it constitutes a voidable preference.\(^{40}\) The Companies Law does not specify who can bring proceedings to set aside a transaction as a voidable preference; however, it is widely considered that only an official liquidator would have the capacity to do so. A transaction with a creditor will constitute a voidable preference if it can be shown that the company executed the transaction in the six months prior to commencement of the company’s liquidation, and at a time when it is unable to pay its debts as they fall due; and the principal or dominant intention of the company’s directors in executing the transaction is to give that creditor a preference over other creditors.\(^{41}\) If the party that receives the benefit of the payment, transfer or charge is a related party, such that it has the ability to control the company or exercise significant influence over it in making financial and operational decisions, such payment will have been deemed to have been made with a view to giving a preference.\(^{42}\) Where a transaction is set aside as being a preference, it is void, and the creditor will be required to return the payment or asset and claim in the liquidation for the amount of its claim.

In the matter of\(^{43}\) Re Weavering Macro Fixed Income Fund Ltd (in Liquidation), the Court of Appeal considered in substantial detail each stage of the test to be applied in identifying voidable preferences under Section 145(1) of the Companies Law. Weavering concerned an appeal against an Order of Justice Clifford declaring certain payments were invalid preference payments. In considering the solvency test under Section 145(1), the Court of Appeal confirmed the applicability of the cash flow test in the Cayman Islands and clarified that this test was not confined to debts that are immediately due and payable, but also extends to debts that ‘will become due in the reasonably near future’ and that any other conclusion would lead to artificiality.

On the question of establishing an intention to prefer on the part of the company in liquidation, the Court of Appeal dismissed the suggestion that a ‘taint of dishonesty’\(^{44}\) is required in order for a payment or transfer to be deemed preferential. The Court of Appeal explained that the ‘preference’ referred to in the section refers to one creditor receiving more than the amount to which they would be entitled on a pari passu basis, not necessarily a preference of a fraudulent nature. It is also irrelevant to the question of identifying a preference that the recipient of the payment was paid by mistake. The liquidator need only prove that the company intended to prefer a creditor (not that particular creditor necessarily) over others.

The Court of Appeal also confirmed that common law defences, such as change of position, are not available to statutory claims under section 145(1) and as such, where the elements of Section 145(1) are made out, the payment is automatically avoided and must be returned.

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39 Section 146 of the Companies Law.
40 Section 145 of the Companies Law.
41 See RMF Market Neutral Strategies (Master) Limited v. DD Growth Premium 2X Fund [2014 (2) CILR 316].
42 Section 145(2) of the Companies Law.
44 Re Kushler Ltd [1943] 1 Ch 248.
III RECENT LEGAL DEVELOPMENTS

The provision of services of independent directors to funds and companies alike is a growing facet of the Cayman Islands’ financial services industry. It became apparent during the credit crisis that independent directors played a key role when hedge funds were faced with difficult decisions, as they ensured compliance with the fund documents and that shareholders were treated fairly as far as possible. Institutional investors are now, in the majority of cases, requesting that all new hedge funds have a majority of independent directors appointed to the board as part of their investment criteria.

To provide statutory weight and robustness to this growing sector, the government approved the Directors Registration and Licensing Law 2014, which came into effect on 4 June 2014. The new legislation requires all directors of mutual funds regulated by the Mutual Funds Law (2013 Revision) and directors of companies who are registered as ‘excluded persons’ under the Securities and Investment Business Law (2011 Revision) to register with the CIMA. The new Law provides for the registration and licensing of individuals or companies that are appointed as directors of mutual funds and entities carrying on securities investment business in the Cayman Islands. The new regime also requires individuals acting as a director in 20 or more companies to apply for a professional director’s licence unless they meet the limited exceptions. Professional directors are now required to have professional insurance coverage with a minimum aggregate cover of US$1 million, including a minimum cover of US$1 million for each and every claim.

Furthermore, the highly anticipated Limited Liability Companies Law, 2016 (LLC Law) was published in the Cayman Islands on 28 June 2016 and came into force on 8 July 2016. The introduction of the new Cayman Islands limited liability company (an LLC) satisfies the demands of stakeholders, in particular in North America and Asia, for a more flexible corporate offshore structure, and provides a welcome addition to the existing range of corporate vehicles available in the Cayman Islands. The LLC is closely aligned with the Delaware limited liability company and is expected to be popular as a vehicle of choice for investment fund and private equity structures, as well as corporate transactions, including joint ventures, special purpose vehicles and holding companies, where the LLC structure can be tailored to suit the particular transaction.

The LLC Law provides for the formation and operation of an LLC in the Cayman Islands, as a body corporate with limited liability and separate legal personality from its members. The LLC Law also provides for the conversion or merger of existing Cayman Islands exempted companies into LLCs and the continuation into the Cayman Islands as an LLC of entities established in another jurisdiction. In relation to the insolvency or restructuring of an LLC, the LLC Law incorporates by reference, and largely reflects Part V of the Companies Law, containing provisions which mirror those in the Companies Law dealing with arrangements and reconstructions. As such, to all intents and purposes, the insolvency or reconstruction of an LLC will be subject to the same rules as are applicable to exempted limited companies.
IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

In the recent case of Natural Dairy (NZ) Holdings Limited, the Grand Court confirmed that the court may substitute a contributory petitioner on a contributory’s winding-up petition, even though there is no express power to do so under the Companies Winding-Up Rules. Following the presentation of the petition, the Petitioner discovered it was the beneficial – not the registered – owner of its shares, and, therefore, did not have standing to petition for winding up under the Companies Law. The company argued that substitution was not possible and sought to strike out the petition as a nullity. It was argued successfully that the court should allow substitution and pointed to the practice of Cayman court prior to the introduction of the Companies Winding-Up Rules, and the modern practice of the English High Court, to permit substitution on a contributory’s petition, notwithstanding the absence of an express power to do so under the Insolvency Rules 1986, which applied in the jurisdiction prior to the introduction of the Companies Winding-Up Rules. The Petitioner relied on a series of decisions starting with HSH Cayman I GP Limited in which the Cayman courts confirmed their inherent jurisdiction to deal with irregularities in Companies Winding-Up Rules proceedings. This was necessitated by the lack of an equivalent in the Companies Winding-Up Rules to Order 2, Rule 1 of the Grand Court Rules, which enabled the court to relieve a party from noncompliance with procedural requirements. Justice Segal permitted substitution, pointing out that the lack of an express power to substitute on contributories’ petitions – in contrast with the position regarding creditors’ petitions – was probably because the rule was intended to prevent companies paying off petitioning creditors one by one, and there was less need for such a rule regarding contributories’ petitions as contributories are not so easily bought off.

In another decision in Primeo Fund (in Official Liquidation) v. Bank of Bermuda and HSBC Securities Services (Luxembourg), the Court of Appeal considered the scope of legal professional privilege in the context of witness statements. The Court of Appeal reaffirmed the view that claims for privilege should be viewed narrowly and weigh against the importance of transparency and openness in civil proceedings. In considering when privilege is lost in respect of witness statements filed on other or related proceedings, the Court of Appeal confirmed that: (1) witness statements are prima facie discoverable; (2) privilege does not apply to witness statements that have been finalised and unconditionally served (even if they were not relied on at trial); and (3) when privilege in a witness statement is lost, it is as against the whole world. The Court of Appeal declined to go so far to say witness statements lose their privilege before they are served.

The court in Uni-Asia Holdings Limited recently sanctioned a members’ meeting of a company for the purpose of considering a ‘migration’ scheme of arrangement. The arrangement proposed by the Cayman company was that its members exchange their shares

48 FSD 34 of 2017.
for shares in a Singaporean company. The intended objective – an internal restructuring – was for the Singaporean company to become the new holdings company for the group and the Cayman company to become its subsidiary.

Shareholders may hold their shares through a central depository, with the result that a single shareholder (the depository) may hold shares on behalf of several owners beneficiary. This poses a unique problem in a members’ scheme of arrangement because the scheme is passed on a ‘head count’ (and ‘value’) test.

In the Cayman Islands, the approved approach is to look through the register and treat the registered shareholders as having a head for each beneficial owner, rather than a single head, for the head count test. The challenge then becomes how to incorporate a mechanism into the scheme documents that enfranchises those beneficial owners to vote on the scheme when that right otherwise rests with the registered shareholder.

In this instance, the court approved a mechanism by which the nominee gave voting proxies to each beneficial owner (or someone else appointed by the owner) in respect of that owner’s shares. The court rolled up its sleeves when it came to the drafting of the scheme documents on that issue (and others) requiring that: (1) the mechanism be hard-wired into the scheme documents – it was not sufficient to rely on a provision in the articles of association by which the registered shareholder was ‘deemed’ to authorise a beneficial owner to act even without a formal proxy; and (2) the order specify that the registered shareholder be able to split its vote.

V INTERNATIONAL

The Cayman Islands has elected not to adopt the UNCITRAL Model Law on Cross-Border Insolvency per se. However, in 2009 the Cayman Islands comprehensively revamped its cross-border insolvency legislation, inserting international cooperation provisions, in the form of Part XVII of the Companies Law,\(^{49}\) that are not dissimilar to the provisions of the Model Law. In addition, the Cayman Islands Grand Court applies Model Law principles in a manner that means the Model Law is strictly unnecessary.\(^{50}\)

In some ways, Part XVII is more liberal (or universalist) than the Model Law:

*By implementing through its Courts a public policy model on a par with international codes of conduct, the territory has vouchsafed its ability to render the kind of international judicial assistance that is critical to the fulfilment of the tenets of the UNCITRAL Model Law and to the principles of universality of bankruptcy that the Law embraces.\(^{51}\)*

Part XVII of the Companies Law codifies the Grand Court’s powers to make orders in aid of foreign insolvency proceedings, and does so in terms substantially similar to the key tenets of the Model Law.

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50 Save that, of course, the certainty of having the same Model Law apply in Cayman as it does in other places creates a common currency (see Guide to the Enactment of the UNCITRAL Model Law on Public Procurement (Guide to the Enactment of the Model Law)).

Section 240 of the Companies Law provides definitions for the international cooperation provisions of Part XVII. ‘Debtor’ means a foreign corporation or other foreign legal entity subject to a foreign bankruptcy proceeding in the country in which it is incorporated or established. The definition of ‘debtor’ in Section 240 draws upon the Model Law language of ‘non-main proceedings’ by use of the word ‘established’, but also confers jurisdiction on an application under Part XVII based merely on the debtor’s incorporation in the country of the foreign bankruptcy proceeding court.52 The reference to incorporation as a qualifying test for a foreign representative’s standing to apply for ancillary relief under Part XVII is a lower (more universalist) threshold than that which applies in the Model Law.

Consistent with this liberal approach, Part XVII does not require a determination of a debtor’s centre of main interest53 or any determination as to whether particular foreign proceedings are main or non-main. Further, in order to seek ancillary orders pursuant to Section 241, there is no requirement for a foreign bankruptcy proceeding to be subject to the control of or supervision by the foreign court.54

Foreign office holders or representatives (meaning a trustee, liquidator or other official appointed for the purposes of a foreign bankruptcy proceeding) have been recognised in the Cayman Islands in two noteworthy decisions in Re Bernard L Madoff Investment Securities LLC (BLMIS) (5 February 2010) and Re Reserve International Liquidity Fund (16 April 2010) in reliance upon the dicta in Cambridge Gas Transport Corporation v. The Official Committee of Unsecured Creditors55 holding that the purpose of common law (i.e., non-Model Law) recognition is to give a foreign office holder or creditors the remedies to which they would have been entitled if the equivalent proceedings had taken place locally, without the need to commence parallel insolvency proceedings locally.

Article 13 of the Model Law (parity of treatment for foreign and local creditors) is enshrined in Section 242(1)(a) of Part XVII of the Companies Law, which provides that all creditors should be treated equally and fairly, regardless of their domicile.

Articles 15 and 16 of the Model Law set out the procedure for the recognition of foreign insolvency proceedings. ‘In the Cayman Islands, as a matter of established practice, it is likely that a foreign representative of a company will be recognised where it is appointed by a court in the country of the company’s incorporation.’56 The criteria for the Grand Court in deciding whether to make an ancillary order for recognition pursuant to Part XVII of the Companies Law are ‘[…] matters which will best assure an economic and expeditious administration of the debtor’s estate’, consistent with the principles of the Model Law. Article 21 of the Model Law provides for the relief that may be granted to a foreign representative upon recognition. Both Article 21 and Section 241(1) provide for the recognition of foreign representatives, stays of proceedings and enforcement against the debtor’s property, examination of parties with relevant information and assumption of control of assets by the foreign representative.

In Re Trident Microsystems (Far East) Limited57 is another example of the purposive approach towards international cooperation taken by the Grand Court. Trident was a

53 Look Chan Ho, A Commentary on the UNCITRAL Model Law, Third Edition, 2012 (see in particular the chapter written by Tony Heaver-Wren and Jeremy Walton on the Cayman Islands, at page 105).
54 Consistent with the Model Law, Article 2(a) and (e), and the Guide to the Enactment of the Model Law.
56 Look Chan Ho, A Commentary on the UNCITRAL Model Law, Third Edition, 2012 (see in particular the chapter written by Tony Heaver-Wren and Jeremy Walton on the Cayman Islands, at page 110).
57 In the matter of Trident Microsystems (Far East) Limited [2012] (1) CILR 424.
company incorporated in the Cayman Islands, and its parent company was incorporated in Delaware. Both entities applied to the Delaware Bankruptcy Court for relief seeking, *inter alia*, the Court’s sanction for the sale of certain assets. In the Grand Court, pending the determination of Trident’s winding-up petition, joint provisional liquidators were appointed, and it was ordered that any sale of the company’s assets be subject to court approval. The Grand Court subsequently adjourned the winding-up petition to allow for a consideration of a potential restructuring of the companies’ TV business after the proposed sale of its set-top box business. The Delaware Court and the Grand Court approved a cross-border insolvency protocol agreement entered into between the parties that provided a framework for the Courts’ cooperation; in particular, it provided that the liquidators would seek approval of the procedures for the sale of material assets and authority to sell first from the Delaware Court, and thereafter from the Grand Court, and would not complete any sales unless the necessary approvals were received from both Courts.

In October 2016, judges from 10 different jurisdictions, including the Cayman Islands, met in Singapore for the inaugural Judicial Insolvency Network (JIN) Conference. The result of the conference was the JIN Guidelines for Cooperation in Cross-Border Insolvency Matters. The Guidelines were designed primarily to enhance communication between courts, insolvency representatives and other parties in the context of global restructurings and insolvency. As a result of the increased efficiency, it is hoped that stakeholders will see a reduction in delay and cost. As of the date of publication of this chapter, Bermuda and the BVI have both adopted the Guidelines. It will be interesting to see if and when the Cayman Islands follows suit.

**VI  FUTURE DEVELOPMENTS**

The Companies Law in the Cayman Islands is substantially derived from the UK Companies Act 1948, and although Part V was revised considerably in 2009, it has not enjoyed the same developments as its English counterpart and those of many other offshore jurisdictions. For example, Part V contains 67 sections, whereas the BVI Insolvency Act comprehensively comprises 505 sections. To fill the various lacunae in the Companies Law, the Grand Court has adopted a purposive approach to its interpretation and developed a cohesive set of principles that largely complement the contemporary common law position.

Notwithstanding the status of the Companies Law, the Cayman Islands Law Reform Commission can and does make recommendations on a regular basis in respect of proposed changes to the Companies Law. In 2014, the Commission circulated a consultation paper examining the position of directors in the Cayman Islands and discussing whether there is a need for codification of directors’ duties. Underpinning the role of the Law Reform Commission is the Insolvency Rules Committee, which is constantly reviewing the Companies Winding-Up Rules. It is expected that the monitoring of the Companies Law by the Law Reform Commission and the Insolvency Rules Committee will be a continuing venture to ensure that the legislation meets the needs of the Cayman Islands financial services industry.

Nevertheless, Cayman Islands insolvency and restructuring professionals are currently discussing revisions of the Companies Law, which would have the effect of introducing ‘restructuring officers’. It is hoped, however, that any amendments will maintain the present balance in Cayman Islands restructuring provisions of the rights of all interested parties.

The ‘just and equitable’ winding-up petition is the remedy of choice for aggrieved shareholders in Cayman Islands companies. Not only is a petition the gateway to winding up a company, but once the court is satisfied that it is just and equitable to do so, it may grant
alternative relief such as order regulating the conduct of the company’s affairs, or an order that a shareholder be bought out. However, the Companies Law expressly limits the right to petition a shareholder who is either the original allottee of shares, or has been the registered shareholder for at least six months prior to presentation of the petition. This provision reinforces and extends the common law principles that a company need not recognise trusts of its shares, which has also been recognised by the Cayman Islands courts in *Svanstrom v. Jonasson* and *Schultz v. Reynolds*, both of which held that the beneficial owner of shares was not able to pursue a derivative action in the name of the company. The expressed legislative intent behind this provision was to prevent vulture funds from buying shares purely for the purpose of petitioning. However, the effect is to exclude the large number of investors who hold their shares through custodians or clearinghouses from the remedy of just and equitable winding up.

The vast majority of such investors are unaware that this is the effect of using a custodian, and many custodians are unwilling to petition. Even if a custodian is willing to transfer the shares to the beneficial owner to allow it to petition in its own name, in most cases relief is required urgently and the requirement to wait six months before petitioning will be fatal. The law is ripe for review, as the effect of the current provisions, combined with the widespread use of nominees, is that many investors are left without an effective remedy for wrongdoing by the company.

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I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

i Banking and finance

According to the annual report from the Danish central bank, Danmarks Nationalbank, their stress test of the credit institutions showed that even in a severe recession the systemic institutions would have positive excess capital adequacy in relation to the minimum requirements. For most of the institutions, the capital base has been increased over the last year or so.2

Finansiel Stabilitet A/S

Finansiel Stabilitet A/S was established in October 2008 as part of an agreement between the government and the Danish banks. The company is state-owned through the Danish Ministry of Economic and Business Affairs. The purpose thereof was to establish confidence, which was lacking in the Danish financial sector due to the international financial crisis.

Currently, the following companies belong under Finansiel Stabilitet: FS Property Finance, FS Finans I A/S (the former Sparbank Østjylland), FS Finans II A/S (the former Max Bank), FS Finans III A/S (the former Amagerbanken), FS Finans IV A/S (Fjordbank Mors) and FS Finans V A/S (Andelskassen J.A.K. Slagelse).

ii Corporate

According to Statistics Denmark, there was an increase in the number of bankruptcies in 2016. The number of bankruptcies was 5,468 in 2011, 5,634 in 2012, 4,993 in 2013, 4,049 in 2014, 4,029 in 2015 and 6,674 in 2016. Between January to May 2017, 2,134 bankruptcies were filed, which was 901 less than the same period last year.

The number of bankruptcies in Denmark reached a record high number in 2016 with 6,674 bankruptcies, which is an increase with more than 60 per cent compared to 2015. A large part of this increase is a result of the zero-company, which is a company with no employees and a turnover below 1 million kroner. The number of jobs lost as a result of companies going bankrupt has been in decline since 2010, and the number is now half the size it was in 2010.3

1 Kristian Gustav Andersson is a partner at Lundgrens.
2 Danmarks Nationalbank’s Annual Report 2016.
II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Restructuring process
If a company is unable to pay its creditors at maturity, the company may file a petition for restructuring proceedings with the Danish bankruptcy court for the purpose of completing a compulsory composition or a (partial) business transfer.

The bankruptcy court appoints a restructuring administrator as well as a restructuring accountant. The administrator is an attorney, whose duties as administrator are to take care of and protect the creditors’ interests in the company. The reorganiser must be independent and meet the Bankruptcy Act’s requirements with respect to impartiality, and accordingly the administrator may not, for example, have been the company’s attorney. The accountant may not have been the company’s auditor for a period of two years prior to the restructuring proceedings.

The Danish rules on restructuring proceedings ensure that all creditors are treated equally, notwithstanding their size and nationality. However, under a compulsory composition, some creditors are entitled to full recovery, while other creditors may accept a dividend and some creditors’ claims lapse, depending on the type of the claim.

The day of filing a petition for restructuring proceedings to the bankruptcy court establishes a reference date (the commencement date of the proceedings), and after the reference date until completion of the restructuring proceedings, debts may only be paid in accordance with the order of priority of creditors or if the payment is necessary to avert loss. The company may be restructured by means of a compulsory arrangement with the creditors for an extension of payments or payment of compulsory dividend, or both, or an arrangement with the creditors concerning a (partial) business transfer of the company.

The management of a company in restructuring will continue to have management powers in accordance with the Companies Act, but any significant decisions must be pre-approved by the administrator. However, upon request by the debtor or the creditor, the bankruptcy court may decide that the administrator is to take over management and control of the company. Furthermore, the administrator automatically takes over the management of the company, if the restructuring proceedings are initiated without consent from the management of the company.

In the restructuring period, the company is protected against individual debt proceedings and other rights to seek satisfaction in the company’s assets. However, some specific types of debt proceedings are not affected by the restructuring proceedings.

After the restructuring proceedings are initiated, the process of restructuring starts with restructuring plan that is subject to a vote at a creditor meeting, which shall be held no later than four weeks after the initiation of the restructuring. After the approval of the restructuring plan, the administrator shall – within six to 10 months – present a restructuring proposal to the creditors for their approval. If either the restructuring plan or proposal is not approved then the company will pass on to bankruptcy proceedings.

A restructuring plan will be considered approved unless a majority of the creditors present votes against the plan and they represent a minimum of 25 per cent of the known amounts entitled to vote. Accordingly, both the number of creditors and the amounts entitled to vote are important to the voting. There are no voting rights attached to debts of full or no coverage and to related parties’ debts.

With respect to the compulsory composition, voting rights are only attached to debts to the extent that the debts are effected by the composition but do not lapse as a result thereof.
A restructuring proposal is considered approved unless a majority of the creditors present votes against the restructuring proposal. The voting procedure is arranged according to the amounts of the creditor’s claims, but there are no voting rights attached to debts of full or no coverage and related parties’ debts. Accordingly, the number of creditors voting against a restructuring proposal is irrelevant at the voting regarding adoption of the restructuring proposal – contrary to what applies with respect to the adoption of the restructuring plan.

The restructuring can only result in a compulsory composition or a business transfer or part thereof. If the only outcome of the restructuring is a business transfer, bankruptcy proceedings against the company in restructuring are commenced immediately.

The steps of a restructuring in terms of time are as follows. After the opening of the restructuring:

- the initial meeting in the bankruptcy court takes place four weeks later;
- the initial meeting may be adjourned for four weeks, if there are specific reasons to do so;
- within three months after the initial meeting, the administrator shall send a statement of all material aspects regarding the restructuring proceedings to the creditors;
- a meeting in the bankruptcy court for the purpose of reviewing the proposals for the restructuring is held six months later;
- the meeting may be adjourned for two months for the purpose of reviewing the proposals for restructuring; and
- the meeting may be further adjourned for two months for the purpose of reviewing the proposals for restructuring.

This means that the maximum duration of restructuring proceedings is 12 months.

**Bankruptcy**

A petition for bankruptcy may be filed by a creditor or by the debtor itself to the bankruptcy court. If the bankruptcy court finds that the debtor is insolvent and that the insolvency is not considered to be of a temporary nature, the bankruptcy court will decide to commence bankruptcy proceedings against the debtor.

If a creditor is to file for bankruptcy against a company, the proceedings are conditional upon said creditor’s payment of a security of 30,000 kroner for the costs incidental to preliminary administration of the estate. In the event, a creditor has floating charge over the debtor, this creditor is required to pay a security of 50,000 kroner. Under certain circumstances, the bankruptcy court may disregard the condition of a security, but this is a rare exception.

If the petition is filed by the debtor (in practice only companies), security is also a prerequisite for the bankruptcy court to initiate the proceedings, but the claim for security can be disregarded by the court, if the debtor does not have the required 30,000 kroner in cash.

*Bankruptcy orders*

When a bankruptcy order is issued by the bankruptcy court, the debtor loses its right to dispose of its assets, rights and obligations. Thus, an estate will be established and, the bankruptcy court appoints a trustee of the estate in bankruptcy. The trustee in bankruptcy is appointed at the same time as the bankruptcy notice is issued.

The trustee in bankruptcy will manage all affairs on behalf of the bankruptcy estate, including ensuring that all property of the debtor vests in the estate and that the assets are sold for the purpose of paying dividends to the creditors.
Accordingly, the trustee in bankruptcy will act as the management and, consequently, is granted full right of disposal of the bankruptcy estate, and is, therefore, authorised to act on behalf of the bankruptcy estate in all matters, including pending court cases and other disputes, and neither the bankruptcy court nor the creditors are to approve the transactions or arrangements made by the trustee in bankruptcy. However, in the event the estate’s assets are pledged, a sale of that asset requires consent from the pledgee as a starting point.

**Objective of the bankruptcy proceedings**

The main objective of the trustee is to wind up the business in favour of the creditors. The trustee has to monetise the assets of the estate. The trustee is obligated to review the company’s records, accounts and transaction history for the purpose of clarifying whether the creditors have been pursued for any unlawful conduct or any unusual business transactions and in this case the trustee can set aside these avoidable transactions.

After the records and accounts have been reviewed by the trustee and all assets have been monetised, the estate’s cash holdings after payment of the estate’s administrative costs are distributed to the creditors.

**Claims settlement**

The creditors of a bankrupt entity will receive dividends, if any, according to the priority order set out by the Danish Bankruptcy Act. The creditors are ranked into six groups as outlined below. Accordingly, a creditor in a subordinated group will not receive any dividend unless the creditors in the previous group have received full payment of their claims. If a group of creditors only receives partial payment of their claims, the dividend will be distributed proportionally among the creditors.

The ranking of the creditors is governed by Sections 93 and 98 of the Danish Bankruptcy Act that provides the following order of priority:

**Section 93 claims: Costs related to the bankruptcy estate**

This group covers (1) the costs of bankruptcy entry, (2) the administrative costs of the estate, and (3) the debt incurred under its care.

**Section 94 claims: Reasonable costs related to attempt to achieve a comprehensive composition.**

This group covers (1) costs for attempting to achieve a comprehensive settlement of the debtor’s financial situation by restructuring, (2) costs related to liquidation, (3) costs related to compulsory or voluntary composition, and (4) other debt that the debtor has contracted after the reference date with the consent of the restructuring administrator.

**Section 95 claims: Employee claims**

This group covers (1) claims for wages, (2) damages for claims for wages, (3) holiday allowances, and (4) miscellaneous fees and other requirements.

**Section 96 claims: Suppliers’ claims for duty on products specific claims**

This group covers suppliers’ claims for duty on products that are liable to duty according to certain Danish acts, and that are delivered to the debtor duty paid for the purpose of resale within a period of 12 months prior to the reference date.
Section 97 claims: Other claims, except for Section 98 claims
This group covers among others tax claims and claims from the debtor’s suppliers.

Section 98 claims: Subordinated claims
This group covers (1) interest accrued after the date of the bankruptcy order, (2) certain claims under lease agreements, (3) subordinated loans to the debtor, (4) claims for fines, and (5) claims for gratuitous promises.

Conclusion of proceedings
Normally, the trustee in bankruptcy will conclude the bankruptcy proceedings with a statement of affairs and accounts for the estate, including a proposal for distribution to the creditors, and the creditors will receive dividends of their claims, provided that the estate pays dividends to the specific group of claim.

iii  Compulsory liquidation
A company is generally wound up by compulsory liquidation at the request of the Danish Business Authority.

   The following situations may result in the Danish Business Authority requesting that the bankruptcy court initiate compulsory liquidation:
   a  the company has not filed its annual report in a timely manner and has not responded to the reminder from the Danish Business Authority;
   b  the company does not have the management or the registered office required by law;
   c  the company has not registered an auditor required by law;
   d  the company has not registered an auditor, even if the general meeting has decided that the company’s annual report must be audited; or
   e  the company’s management has not taken appropriate measures by, for example, capital decrease in relation to requests for payment of unpaid share capital that cannot be paid by shareholders.

Before the company is sent into compulsory liquidation, the Danish Business Authority will forward a warning letter to the management of the company with a deadline for compliance.

   The bankruptcy court may appoint one or several liquidators to be in charge of proceedings. The rules for voluntary liquidation will mutatis mutandis apply to the liquidators’ work in relation to the compulsory liquidation. The former members of the management of the company in compulsory liquidation are committed to the extent necessary to assist the liquidators with information about the company.

   When the proceedings are completed, the bankruptcy court will notify the Danish Business Authority and request the company to be deleted from the Danish business register.
III RECENT LEGAL DEVELOPMENTS

i The Bankruptcy Act

Bankruptcy quarantine

On 1 January 2014, provisions on bankruptcy quarantine came into effect. The bankruptcy quarantine is imposed on a member of management or a member of the board of directors by the bankruptcy court if that member has acted with gross negligence in managing a company that is later adjudged as bankrupt.

A bankruptcy quarantine prohibits the person from managing a limited company for a period of three years as a starting point, however, this may be for a shorter period in case of mitigating circumstances. The court may impose upon a person subject to bankruptcy quarantine a new bankruptcy quarantine from another bankrupt company (which may be in the same group as the bankrupt company related to the first bankruptcy quarantine). In this case, the two (or more) quarantine periods are added together, though then cannot exceed 10 years from the first bankruptcy quarantine.

Any person subject to bankruptcy quarantine must be recorded in a register kept by the Danish Business Authority.

After the provisions came into effect there have been a large number of judgments, and the bankruptcy courts are considered to have taken a strict approach to the provisions. 4

ii The Companies Act

Public Register of Shareholders

On 15 June 2015, the new Danish Public Register of Shareholders came into force.

According to the 2015 act, all Danish companies (A/S, ApS, IVS and P/S) are required to register their direct shareholders (ownership of 5 per cent or more of capital or shares).

On 1 March 2016, the provisions on the Danish Public Register of Shareholders's provisions were updated.

According to the 2016 Act, all Danish companies are required to register their beneficial owners holding more than 25 per cent of the shares or voting rights. The update is in accordance with EU’s Fourth Directive on preventing money laundering.

The register is publicly available. The registration duty is imposed on all Danish companies, and if not complied with, the Danish Business Authority may impose a fine on the company (fine levels are still unknown).

IV INTERNATIONAL

The EU Insolvency Regulation came into force throughout the European Union, with the exception of Denmark, on 31 May 2002. Because of Denmark’s opt-out relating to judicial cooperation, which effectively dates back to the Danish referendum on the Maastricht Treaty in 1992, the EU Insolvency Regulation does not apply in Denmark. Therefore, the general national Danish rules apply to international insolvency.

In principle, bankruptcy proceedings initiated in another jurisdiction do not exclude a creditor from the attachment of the debtor's assets in Denmark.

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4 Bo Vadt Christensen, the Danish weekly law reports (Ugeskrift for Retsvæsen), 2015, page 186.
If the Danish rules on jurisdiction are met, there should be nothing to prevent an implementation of independent bankruptcy of a debtor’s assets in Denmark, regardless of whether the bankruptcy has already started in another jurisdiction.

The Nordic countries (Denmark, Norway, Sweden, Finland and Iceland) have all joined the Nordic Bankruptcy Convention. The Bankruptcy Convention only applies in rare cases. The Convention includes all assets and liabilities belonging to the debtor in the other Nordic countries.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

i State of the economy and the finance industry

In the early summer of 2016, the United Kingdom (UK) experienced considerable political upheaval as a result of the unexpected and momentous decision of the British people to leave the European Union (EU) (Brexit). Decades of foundational assumptions in public policy and the making and administration of laws were thus overturned. Prior to the vote economic forecasts concerning the potential impact of Brexit ranged from a slide into a deep and immediate recession to robust economic growth in the medium to long term. One year on from the referendum, it is clear that the apocalyptic predictions of economic meltdown following a Brexit vote have not occurred. Despite an air of instability and concern in some quarters about the UK’s prospects, the UK’s economic growth has continued, although at a slower pace. Following the referendum, gross domestic product (GDP) grew by 0.5 per cent in Q3 2016, 0.7 per cent in Q4 2016 and 0.2 per cent in Q1 2017 (the lowest quarter for a year). At the same time the rate of unemployment decreased to 4.6 per cent, the lowest level since 1975. Economists consider the main reason for this development to be the sharp fall in the value of the pound sterling (sterling) since the EU referendum. In March 2017, the sterling exchange rate index (ERI) fell a further 1.5 per cent from the end of February 2017 and was 10.5 per cent lower compared with the end of March 2016. This decline in value meant British goods became considerably cheaper especially for countries from the European Union and the United States (US). As a result, the UK’s export rate increased by almost 10 per cent to March 2017. However, the weakness of sterling has resulted in increased import costs that have resulted in some price rises and contributed to a reduction in consumption.

One important topic raised before the referendum for the City of London was the impact of Brexit for the role of London as the foremost European financial centre. Despite predictions that a multitude of firms and businesses would leave the UK for other European financial centres immediately following a vote to leave the EU, this has not come to fruition. In terms of contingency planning, a few banks based in London have rented new offices outside of the UK, primarily in Frankfurt. Three Japanese banks, namely Sumitomo Mitsui, Daiwa Securities and Nomura have announced plans to relocate their business seats from London to Frankfurt. However, as at the time of writing, none of these banks has disclosed...
how many employees will be transferred and the actions that have been taken to date seem to be more part of preparation for a range of scenarios concerning the outcome of the withdrawal negotiations rather than specific definitive measures to leave the UK.

It is too early to draw any conclusions as to the medium or long-term impact of Brexit on the economy and the finance industry. There are a number of complex considerations that will form part of the negotiations between the UK and the EU. Indeed, it also remains to be seen whether the UK’s economic fate will depend solely on the outcome of these negotiations given the range of external global macro-economic factors that could affect global financial markets in the next decades as well as the British economy and financial sector. Much of the discussion relating to withdrawal negotiations has centred on the ‘model’ that the UK will try to pursue. A so-called ‘hard’ Brexit envisages the UK withdrawing from both the customs union and the single market, whereas a so-called ‘soft’ Brexit envisages the UK remaining in either or both. Perhaps more significant for the UK’s economic fortunes, certainly in the short to medium term, will be the extent and duration of the transitional arrangements adopted by the UK in order to cushion the impact of the UK’s eventual withdrawal from the EU. In the event that the economy sours and business stagnates, the UK’s restructuring and insolvency sector (as explained in more detail in this chapter) stands well prepared to respond to any negative economic consequences.

ii Market trends in restructuring procedures and techniques employed during this period

As explained below, most large restructurings in the UK continue to be effected on an informal, out-of-court basis. Insolvency Service statistics for activity in Q1 2017 show that company insolvencies rose for the third successive quarter and suggest that the trend of reduced insolvency activity observed over recent years might be reversing. After a historic decrease in the liquidation rate up to Q3 2016, where it was at its lowest rate since records began in 1984, the rate has increased to 0.47 per cent of all active registered companies a level last seen in mid-2015. However, compared to the long term average of 1.2 per cent over the past 25 years, the liquidation rate remains low.

There were 3,967 company insolvencies in England and Wales in the Q1 2017. This was an increase of 4.5 per cent compared to the underlying number in Q4 2016 and an increase of 5.3 per cent compared to Q1 2016. This figure comprised 2,693 creditors’ voluntary liquidations (CVLs) (68 per cent of all insolvencies), 836 compulsory liquidations (21 per cent of all insolvencies), representing an increase of 3.3 per cent on the previous quarter and an increase of 2.8 per cent on Q1 2016. Further, there were 357 administrations and 81 company voluntary arrangements. These figures represent an increase of 13 per cent and a decrease of 3.6 per cent, respectively, on the equivalent figures for Q1 2016. The Insolvency Service recorded no administrative receiverships in the period.

Despite the slight increase in the liquidation rate, it should be noted that the number of active companies has grown over this period as well. The number of active companies has reached more than 3.6 million, an increase of approximately 200,000 compared to May 2016. Compared to fewer than 800,000 active companies in 1986, the number of active companies is currently more than three times higher. The low liquidation rate by historic standards reflects the change of emphasis in the UK’s insolvency legislation towards the rescue and rehabilitation of financially distressed companies and the rise in popularity of pre-pack administrations (trends that are discussed further below). Further, market practice in the recent past has tended to favour amending and extending the terms of corporate
debt rather than forcing financially distressed companies into insolvency, and this trend has been particularly pronounced since the onset of the financial crisis due to the persistence of historic lows in interest rates.

Much discussion in recent years has concerned the impact of possible rises in interest rates on business failures. An increase of base rates to a level closer to historic averages would expose many distressed businesses to the risk of failure. Research conducted by the Association of Business Recovery Professionals (R3) suggests that a rise in interest rates would have a major impact on highly geared businesses, typically hotels, catering and retail. However, for as long as interest rates and hence borrowing costs remain at the historic lows that have been seen in recent years, many distressed companies that, in any other period, would likely have been forced into insolvency procedures have been able to amend and extend their debt and therefore avoid insolvency. The uncertainties in relation to the UK’s departure from the EU make it appear likely, however, that UK interest rates will remain at very low levels for some time to come.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Secured creditors and the balance of power

The approach of the UK’s legal system to the insolvency of troubled businesses is, in part, a product of the secured credit markets in which it developed. The comprehensive security available to lenders in the UK and the rights afforded to them in the event of insolvency go some way to explaining the conventional categorisation of the UK as a ‘creditor-friendly’ jurisdiction, as opposed to one generally regarded as favouring debtors, such as the US.

A bank lending money to a UK corporate enterprise will typically take fixed and floating charges over the company’s assets and undertaking as security for repayment of the debt. Until relatively recently, the holder of a floating charge over the whole (or substantially the whole) of an English company’s property was able to appoint an ‘administrative receiver’ to enforce its security in the event of a default under its credit agreement (or other specified event). Once appointed, an administrative receiver had wide powers to manage and dispose of the assets of the company and owed his or her principal duty to the secured creditor to seek repayment of the secured debt, typically by selling the assets or business as a going concern. Reforms in the UK have now restricted administrative receivership as a remedy for secured creditors, as explained in more detail below.

The holder of a valid floating charge is generally entitled to be repaid in priority to unsecured creditors, but ranks behind fixed charge holders and certain categories of

2 While a fixed charge attaches to a particular asset and allows its disposal only with consent of the secured creditor or on repayment of the debt, a floating charge is created over a class of assets, present and future, and allows the debtor to carry on its business and deal with such assets until a default under the relevant loan agreement (or other defined event), upon which the charge ‘crystallises’ and attaches to the secured assets, preventing the debtor dealing with the assets without repayment of the debt or consent of the creditor.

3 However, where assets are subject to a floating charge created on or after 15 September 2003, a liquidator, receiver or administrator must in general make a ‘prescribed part’ of the floating charge realisations (currently 50 per cent of the first £10,000 and 20 per cent of the remainder, capped at £600,000) available for the satisfaction of unsecured debts in priority to the claim of the floating charge holder.
preferential creditors in respect of its claim. The holder of a valid fixed charge is generally entitled to be repaid out of the proceeds of the realisation of its security in priority to all other claims on the company’s assets. The holder of a qualifying floating charge has the right to appoint its own administrator to enforce its security where the debtor is in default. Further, while a company may also be put into administration by court order or by an out-of-court procedure by another creditor, a floating charge holder will in most cases have the right to choose which administrator is appointed.

ii Statutory insolvency regimes

Corporate insolvency law in the UK has well-developed rules governing the collection and distribution of the assets of an insolvent company on a winding up. The main statutory sources of corporate insolvency law are the Insolvency Act 1986 (IA86) and the Insolvency Rules 2016 (IR 2016), which replaced the Insolvency Rules 1986, and supplement the IA86 by providing the procedural framework for the insolvency regime. Part IV of the IA86 sets out the circumstances in which a company may be wound up on a compulsory or voluntary basis.

Compulsory liquidation involves the company being wound up by an order of the court following the petition of an interested party. There are a number of grounds on which a court may make a winding-up order, with the most usual being an ‘inability to pay debts’. The company is ‘unable to pay its debts’ for these purposes under certain statutory criteria, including under the ‘cash-flow’ test (i.e., where the company is unable to pay its debts as and when they fall due) and the ‘balance sheet’ test (i.e., where the company’s assets are less than its liabilities, taking into account contingent and prospective liabilities). There is no stay or moratorium on the enforcement of security, but it is not possible to commence or continue proceedings against the company without the leave of the court.

Voluntary liquidation is commenced by a resolution of the company and does not generally involve the court. The procedure will be a members’ voluntary liquidation where the directors are prepared to make a statutory declaration that the company will be able to pay its debts in full, together with interest at the official rate, within a period of 12 months from the commencement of the liquidation. Where the directors are not prepared to make such a declaration, the liquidation will proceed as a creditors’ voluntary liquidation. In a members’ voluntary liquidation, the members of the company appoint the liquidator, whereas in a creditors’ voluntary liquidation, both the members of the company and its creditors nominate their choice of liquidator, with the creditors’ choice prevailing in cases of disagreement.

Introduced by the IA86 in response to a recommendation that insolvency law should provide mechanisms to rescue potentially viable businesses, administration is the principal corporate recovery procedure in the UK.

As described in more detail below, administration is a mechanism to enable external management, the administrator, to take control of the company for the benefit of all creditors, while steps are taken under the protection of a statutory moratorium to formulate a strategy to address the company’s insolvency. An administrator may propose an arrangement under Part 1 of the IA86 (a company voluntary arrangement or CVA) or Section 895 of the Companies Act 2006 (a scheme of arrangement or scheme), under which a reorganisation or compromise may be effected; these procedures also exist independently of administration. A scheme or a CVA may be invoked whether or not the company is in fact insolvent, and can be used in conjunction with or to avoid administration or liquidation. In each case, the
arrangement will be binding on the company’s relevant creditors if the requisite majorities of the appropriate classes vote in favour of the proposals at duly convened meetings and, in the case of a scheme, it is sanctioned by the court.

The Small Business Enterprise and Employment Act 2015 (SBEEA 2015) and the Deregulation Act 2015 (DA 2015) have introduced a number of amendments to the IA86 that have been brought into effect, with further contemplated amendments partially in force purely for the purpose of enabling subordinate legislation to be passed. The IR 2016, which came into force on 6 April 2017 replaced the IR86 in its entirety with the express purposes of consolidating the IR86 with the 28 amending instruments made since the IR86 came into force, restructuring and updating the language of the IR86 and giving effect to the policy changes and changes to the IA 86 made by the SBEEA 2015 and the DA 2015. The revised rules provide, among other things, for: the abolition of creditors’ meetings as the default method for decision making in insolvency procedures; the ability to communicate and file forms electronically; split voting rights; and a reduction in the burden of reporting and record keeping requirements for insolvency practitioners. Further minor clarifications to the IR 2016 have been made by the IR Amendment Rules (SI 2017/366) and the IR Consequential Amendments Rules (SI 2017/369).

iii The ‘rescue culture’ and the demise of administrative receivership

Although the statutory framework does not yet provide a single comprehensive procedure under which a distressed company can seek to reorganise its obligations or capital structure, a ‘rescue culture’ has nevertheless developed in recent decades in the UK.

The introduction of the administration and CVA procedures in 1986 provided impetus for a culture of supporting financially distressed companies pending a reorganisation. Banks in the 1990s began to recognise enterprise value in distressed businesses, which, with much-needed influence from the Bank of England, led to the development of established principles for multicreditor workouts (London Approach). These principles were based on consensual contractual out-of-court arrangements, and developed as much as a result of the shortcomings of the CVA and administration regimes as of their introduction. Recognition that the employment of both procedures was disappointingly low led to significant reforms under the Insolvency Act 2000 and a reshaping of corporate rescue law under the Enterprise Act 2002 (EA02).

Designed to facilitate company rescue and to produce better returns for creditors as a whole, the EA02, inter alia, restricted the ability of secured creditors to appoint administrative receivers to a limited number of circumstances. It was widely acknowledged that the administrative receivership remedy gave too much power to secured parties who, as a result of their security, lacked sufficient incentive to rescue failing companies. Administrative receivership was, therefore, effectively replaced by a substantially revised administration regime, under which the administrator is now required to act in the interests of creditors as a whole. Following the EA02, an administrator may be appointed to manage the company with a view to achieving one of three statutory purposes, arranged hierarchically as follows:

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4 CVA proposals must be approved by a simple majority in value of the members and three-quarters in value of the company's creditors present and voting. A scheme requires approval by a majority in number representing three-quarters in value of the members or creditors (or of each class of members or creditors) who vote at a meeting convened by the court for the purpose of considering the scheme. The scheme must subsequently be approved by the court.
a rescuing the company as a going concern;
b achieving a better result for the company’s creditors as a whole than would be likely if the company were wound up (without first being in administration); or
c realising property in order to make a distribution to one or more secured or preferential creditors.5

The administrator may only perform his or her functions in pursuit of the objective stated in (b) above if he or she believes that it is not reasonably practicable to achieve the objective stated in (b), and to do so would achieve a better result for the creditors as a whole.6 The administrator may only, in turn, perform his or her functions in pursuit of the objective stated in (c) above if he or she believes that it is not reasonably practicable to achieve the objectives stated in (a) or (b), and to do so would not unnecessarily harm the interests of the creditors of the company as a whole. Therefore, the administrator’s primary objective is now the rescue of the company as a going concern.7

In recent years, however, the increasing popularity of pre-pack administrations (discussed in more detail below) has to some extent undermined the aims of the revised administration regime and shifted the focus back to the protection of secured and major creditors that was such a feature of administrative receivership. Concerns continue to be expressed that the policy aims behind the reforms to administration made in the EA02 are being frustrated. The pre-pack debate is summarised in more detail below, but it is worth noting here that the market appears to demand a restructuring remedy that allows key creditors to play a central role and that, despite the government’s attempts to enforce equality between creditors, the market is likely to continue to find a way to meet this demand.

The EA02 also made a number of other amendments to the corporate recovery laws of the UK. In particular, the Crown’s preferential status in insolvency proceedings has been abolished, and in its place a proportion of floating charge recoveries are ‘ring-fenced’ for the general unsecured creditors.

iv Role of directors

Modern insolvency law in the UK is founded on the premise that the function of corporate insolvency law is not merely to distribute the estate to creditors, but to encourage debt recovery and scrutinise the actions of the directors in order to ‘meet the demands of commercial morality’. Although administration was introduced by the IA86 to facilitate the rescue of viable businesses, it was done at a time when corporate failure was generally associated with mismanagement and concerns over director misconduct led Parliament to take a strict approach with regard to errant directors. Accordingly, it was decided that the powers of the directors should effectively cease on the appointment of an administrator, who in turn would be given wide powers to carry on the company’s business. Although the directors may remain in control of the company during proposals for a scheme or CVA if those proposals are made outside of administration, the company will not benefit from a statutory moratorium on debt enforcement, unless the company is a ‘small’ company (as defined in the IA86), in which case it may benefit from a limited CVA moratorium.

5 Paragraph 3(1), Schedule B1 to the IA86.
6 Paragraph 3(3), Schedule B1 to the IA86.
7 Paragraph 3(4), Schedule B1 to the IA86.
As a result of reforms introduced at the same time as the CVA and administration procedures, directors of insolvent companies may also face disqualification from holding office in future and find themselves personally liable for ‘wrongful trading’ in circumstances where they continued to trade their business despite it being in the twilight of insolvency. This test is set out in Section 214 of the IA86, and provides that a director may be held personally liable for a company’s debts where, knowing there was no reasonable prospect of the company avoiding insolvent liquidation, he or she failed to take every step that he or she ought to have taken with a view to minimising losses to creditors. Directors may also face personal liability in circumstances where they have been found guilty of fraudulent trading under Section 213 of the IA86 or misfeasance under Section 212. In addition, although the codification of directors’ duties under the Companies Act 2006 did not include a specific duty to creditors, directors of a UK company owe common law duties to creditors where the company is insolvent or nearly insolvent, and can also be held personally liable where a breach of those duties is established.

v Clawback actions

In addition to taking action against errant directors, the liquidator or administrator of a UK company may apply to the court to unwind certain transactions entered into by the company prior to the commencement of formal insolvency proceedings. A transaction entered into within a particular time frame before the onset of insolvency could be unwound, for example, if it constituted a ‘transaction at an undervalue’ or a ‘preference’.

A transaction at an undervalue involves a gift by a company, or a company entering into a transaction where it receives no consideration or consideration of significantly less value than the consideration given by the company. A preference involves putting a creditor (or a surety or guarantor for any of the company’s debts or liabilities) in a better position than the creditor would otherwise have enjoyed on an insolvent winding-up. A court will not generally intervene, however, in the case of a transaction at an undervalue, if the company entered into the transaction in good faith for the purpose of carrying on its business and at the time it did so there were reasonable grounds for believing the transaction would benefit the company. In the same manner, in the case of a preference, the court will not generally intervene if the company was not influenced by a desire to prefer the creditor, surety or guarantor in question. In the absence of fraud, a transaction will also not normally be unwound if the company was not insolvent at the time of the transaction and did not become so as a result of it.

The court also has the ability to make an order to unwind a transaction if it is satisfied that the transaction was entered into to defraud creditors by putting assets beyond the reach of claimants against the company or otherwise prejudicing their interests. No time limit applies for unwinding such a transaction.

Floating charges created by an insolvent company in the year before the insolvency are invalid, except to the extent of any fresh consideration, namely the value of the consideration given to the company by the lender when the charge was created. This period is extended to two years where the charge was created in favour of a connected person.
III RECENT LEGAL DEVELOPMENTS

i Modified universalism

A significant trend in English restructuring law in recent years has been the concept of ‘modified universalism’, which holds that, in cross-border insolvency matters, it is inherently desirable for all claims against the insolvent entity to be dealt with in the same process and in one jurisdiction, and hence that under the common law (i.e., where statute law is silent on the subject), courts should be ready to assist foreign insolvency officeholders where appropriate in the conduct of the insolvency. Modified universalism is, therefore, both a consequence of the increasingly international nature of insolvency law and a facilitator of the trend for cross-border restructurings.

In the case of Rubin and Another v. Eurofinance SA and others, the Supreme Court held that no special common-law rules apply permitting judgments in respect of avoidance actions in foreign insolvency proceedings to be recognised where foreign judgments would not be recognised or enforced outside of an insolvency context. It was decided that the English courts and many Commonwealth courts applying English common law will enforce a foreign judgment in personam only if at least one of the conditions summarised in Dicey, Morris & Collins, Conflict of Laws, 15th ed., 2012 (Dicey), as R 43, is satisfied. One of those conditions is described in Dicey as follows:

\[\text{a court of a foreign country outside the UK has jurisdiction to give a judgment in personam capable of enforcement or recognition as against the person against whom it was given [...] if the person against whom the judgment was given had before the commencement of the proceedings agreed, in respect of the subject matter of the proceedings, to submit to the jurisdiction of the court or of the courts of that country.}\]

The question of whether submission to a jurisdiction under the common law can be implied was examined in the recent case of Vizcaya Partners Limited (Appellant) v. Picard and another (Respondent) (Gibraltar). In Vizcaya, the contract before the court was a customer agreement in a standard form entered into between a company owned by the convicted fraudster Bernard Madoff and a genuine investor, Vizcaya Partners Limited. Madoff’s trustee in bankruptcy had obtained a judgment in default in the New York Bankruptcy Court against the investor that the partial repayment of an investment to Vizcaya had been a statutory fraudulent preference. It was argued that because the agreement specified that it should be construed, and the rights and liabilities of the parties determined, in accordance with New York law, then the parties had impliedly agreed to submit to the jurisdiction of the New York courts, as according to the laws of the State of New York, the New York court had jurisdiction.

The Privy Council decided that submission to a jurisdiction could, in certain circumstances, be implied; however, it was not implied in the instant case. The court stated that whether there had been a submission to the jurisdiction of the foreign court for the purposes of enforcement of foreign judgments depended on English law and that, if that agreement is to arise through implication, then under English law it can be a matter of fact or be implied by law. On the expert evidence on which the trustee relied, Lord Collins noted that, even as a matter of New York law, the evidence did not state that the choice of New York

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law carried with it an agreement to the jurisdiction of the New York court. For a term to be implied as a matter of fact, the liquidation trustee would have to adduce evidence to the effect that in New York law there is a rule of contractual interpretation or construction, on the basis of which the Gibraltar court could conclude that the agreement, in the context of the choice of law and the deemed place of contracting, amounted to a choice of jurisdiction (in addition to the main contractual obligations). For a term to be implied as a matter of law, the expert would have had to show what relevant terms are implied under New York law. There was no relevant evidence under either head.

The decision clarifies the previous uncertainty on the scope of Dicey’s fourth case. An agreement to submit to the jurisdiction of a foreign court can be implied. Implying such a term in a foreign law governed contract in any given case will be assessed by reference to common-law principles, informed by expert evidence. The decision also confirmed that in the field of insolvency-related judgments, specifically those in avoidance actions, the increasingly applicable principle of ‘modified universalism’ does not mean that insolvency proceedings are exempt from the application of general principles.

ii Cross-border protocols
The Judicial Insolvency Network (JIN) is a collaboration between judges from approximately 10 jurisdictions established at the initiative of the Chief Justice of Singapore, Sundaresh Menon. The JIN held its first meeting in October 2016, attended by judges from the US (Delaware and the Southern District of New York), Canada (Ontario), Australia (Federal Court and New South Wales), the British Virgin Islands, the Cayman Islands and England. Hong Kong sent an observer and the judiciaries of Bermuda, South Korea and Japan requested to be kept apprised of the discussions and the outcome. The meeting produced the Judicial Insolvency Network guidelines for judicial communication and co-operation on cross-border insolvency matters (the JIN Guidelines). The guidelines have been adopted by several important jurisdictions, including the Supreme Court of Singapore (via Registrar’s Circular No. 1 of 2017), the US Bankruptcy Court for the District of Delaware (via Local Bankruptcy Rule 9029-2), the US Bankruptcy Court for the Southern District of New York (via General Order M-511), the Supreme Court of Bermuda (via Practice Direction, Circular No. 6 OF 2017), and the Eastern Caribbean Supreme Court for the British Virgin Islands (via Practice Direction 8 of the BVI’s Insolvency Rules 2005). The English High Court adopted the guidelines on 5 May 2017 by adding a reference to the JIN Guidelines in Chapter 25 of the Chancery Guide.

The JIN Guidelines intend to improve communication and cooperation between courts involved in cross-border insolvency proceedings, including on substantive matters, and to make provision for joint hearings. The JIN Guidelines encourage courts to permit parties to be present when court-to-court communication takes place, although any court involved in the communication may direct otherwise. The court may also authorise a party to appear before and be heard by a foreign court, even if it is not a party to the foreign proceeding, and such an appearance will not render the party subject to the foreign jurisdiction. The guidelines require the mutual recognition of statutory law, regulations and rules of court applicable to the proceedings in other jurisdictions without further proof. Further, under the guidelines a court must generally recognise that orders made in the other proceedings were duly made for the purposes of the proceedings without further proof.

Courts are permitted to communicate in advance of joint hearings to establish procedures for the making of submissions and the rendering of decisions and to resolve any
procedural, administrative or preparatory matters. During a joint hearing, each court retains sole and exclusive jurisdiction over its own proceedings but each court should be able to hear the other proceeding simultaneously. After the hearing, courts may communicate with or without counsel present, including on substantive matters. It is noted that, regardless of the legal framework, the scope for joint hearings between courts in different jurisdictions may be limited where the time zones, language or legal culture are significantly different.

IV KEY RESTRUCTURING TOOLS, SIGNIFICANT DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

i The importance of the ‘pre-pack’

The term ‘pre-pack’ is typically used in UK insolvencies to describe the sale of a distressed business where all the arrangements of the sale are negotiated, and agreed before the company enters a formal insolvency procedure and concluded by the insolvency practitioner very shortly thereafter. This allows the business to survive relatively intact while allowing it to jettison a proportion of its debts. Pre-packs emerged in the 1980s in the context of administrative receivership but, following the reforms of the IA 1986 by the EA02, and in particular the possibility of a company being placed into administration without a court order, the practice is now prevalent in administrations. The increase in popularity of pre-packs, despite the government’s attempts to enforce equality between creditors by means of legislation such as the EA02, appears to reflect a market demand for a restructuring remedy that allows key creditors to play a central role.

On the one hand, the pre-pack can be seen as an effective way of preserving the business of an insolvent company and realising value for creditors in situations where time is of critical importance. Pre-pack sales provide for a relatively rapid and straightforward business transfer without the damaging publicity and consequent harm to reputation caused by a standard insolvency process. They can also be used as an effective restructuring tool, giving effect to an agreed deal between stakeholders. On the other hand, critics argue that the process lacks transparency, is controlled by senior lenders, sidesteps procedural safeguards inherent in the administration process and offers no guarantees that the interests of all creditors will be properly taken into account; the Insolvency Service recently estimated that approximately 85 per cent of all pre-packs result in sales to connected parties such as management (known as ‘phoenix’ sales). The fact that the insolvent company may often move straight to dissolution following the sale (without a separate liquidator being appointed) has also attracted suggestions that the actions of the administrator and senior creditors are not subject to adequate checks and balances.

The most important consideration is, however, that in many cases, particularly when a company has no cash available, there is simply no third way between an insolvent liquidation, with the loss of all the company’s goodwill and employees, and a quick pre-pack asset sale from administration, which will probably save most of the business and allow employees to keep working. It is for this reason that the use of pre-packs is likely to continue to grow. Knowledge and use of pre-packs are now widespread. Dozens of high street names have been resurrected under pre-pack deals in the past few years, including MFI (the furniture chain), Karen Millen and Oasis (both fashion retailers), the Laurel Pub Company and Cobra Beer.

In an attempt to address some of the concerns surrounding the use of pre-packs, the Insolvency Service published Statement of Insolvency Practice 16 (SIP 16) in January 2009. A revised version was in effect between October 2012 and November 2015.
Following the publication of the government-commissioned Graham Review into Pre-pack Administration in June 2014, an independent report by Teresa Graham that made a number of recommendations for the better regulation of pre-pack sales, the latest version of SIP 16 was published with effect from 1 November 2015. The revised SIP 16 is designed to improve the transparency and proprietary of pre-packs, introducing six principles for good marketing with which administrators must comply. Administrators must give a full account in their SIP 16 statement of all steps that were taken and all alternatives to the pre-pack that were considered, to show that it was appropriate to implement the restructuring by means of a pre-pack. Any deviation from the specific essential steps must be explained in the statement. The key principle of the revised SIP 16 is that the SIP 16 statement must contain sufficient information for the company’s creditors, such that a reasonable and informed third party would conclude that the pre-pack is appropriate and that the administrator has acted with due regard for the creditors’ interests.

Pre-pack sales to connected parties of the company are accorded greater scrutiny, with the administrator required to refer the potential purchaser to the pre-pack pool, a body of experienced independent business practitioners, to review the proposed deal and issue a statement on its reasonableness, and request a viability review statement of the SIP 16 statement, explaining what operational and financing changes the purchasing entity will make so that the acquired business will be viable.

Further to SIP 16, the licensing bodies for insolvency practitioners have jointly adopted an Insolvency Code of Ethics for England and Wales, which is intended to help insolvency practitioners meet the standards of conduct expected of them by providing professional and ethical guidance. The government has no current proposals to legislate for the regulation or reform of the pre-pack process but does have a backstop power to do so under the IA86, as amended by the SBEEA 2015, if the voluntary self-regulatory regulation does not alleviate concerns.

In terms of the case law treatment of pre-packs, the use of a pre-pack was explicitly approved in the case of *Re Hellas Telecommunications (Luxembourg) II SCA*,¹⁰ where the High Court granted an administration order in respect of the Greek telecommunications company Wind Hellas (which was incorporated in Luxembourg) and expressly granted the company’s administrators liberty to complete a pre-pack sale of the company’s assets. The judgment is significant as it was the first case where the court expressly supported a pre-pack sale. It is clear from *Wind Hellas* and subsequent judgments that pre-packs have become an established and accepted feature of the English insolvency landscape, and that the English courts will continue to consider the merits of such a sale where an administration order is sought, on the proviso that the SIP 16 guidelines are followed when negotiating and agreeing the terms of such a sale. Pre-packs have been implicitly approved by the courts in other recent decisions. In the case of *DKLL Solicitors*,¹¹ despite the fact that HM Revenue & Customs (in its position as a major creditor of the company) opposed the proposed sale of assets to existing management, the court nevertheless decided to make the order in light of all the circumstances, including the interests of other stakeholders. The use of a pre-pack sale prior to the creditors’ meeting was again approved in *Re Kayley*,¹² thereby further entrenching the position of pre-packs in the UK insolvency landscape. In that case, it is also interesting to

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¹⁰ [2009] EWHC 3199 (Ch).
¹¹ [2007] EWHC 2067 (Ch).
¹² [2009] EWHC 904 (Ch).
note that HHJ David Cooke ruled that the administrators’ pre-appointment costs were to be treated as an expense of the administration. In so doing, he followed the approaches of HHJ Norris QC in *Re SE Services Ltd*,¹³ and HHJ Purle QC in *Aldersley Battery Chairs Limited* (unreported).

In the more recent case of *Capital for Enterprise Fund a LP and another v. Bibby Financial Services Ltd*,¹⁴ the High Court considered whether the circumstances of a pre-pack sale showed that the insolvent company’s director had conspired by unlawful means to transfer the company’s business and assets to another company in which the director was interested, in breach of his fiduciary duties. Though the High Court ordered, in the circumstances, that the claimants had not established that the unlawful conduct had caused them the loss and damage that they alleged, it was nevertheless held that the director, in not informing the other directors of the proposed pre-pack sale, had breached his duties to the company by putting the preservation of the company’s business above the interests of the company and its creditors. The case thus serves as a useful reminder of the need for a director of a company in financial difficulties to distinguish between the interests of the business of the company and that of the company and its creditors.

**ii Schemes and debt-equity swaps**

Schemes have become the restructuring tool of choice for UK practitioners and are increasingly competitive on an international scale for restructuring foreign as well as domestic companies, standing alongside the US Chapter 11 procedure as the pre-eminent tool for implementing complex international restructurings of multinational companies.

A scheme can be used to achieve anything that a company and its creditors or members may agree among themselves. Examples include,*inter alia*: a moratorium; the transfer of assets from the debtor to a new company; a release or compromise of secured debts; and a debt-to-equity swap. In recent cases, the most common arrangement or compromise for schemes has been a debt-to-equity swap. The main objective of a debt-to-equity swap is to provide a struggling company with a strengthened balance sheet and improved liquidity. This in turn improves cash flow and relieves pressure from creditors, thereby addressing concerns that directors may have about their duties and potential personal liability issues. Creditors benefit from the greater chance of their debt being repaid, preserved enterprise value and a potential for equity upside if the company returns to profitability or is sold. Key customers and suppliers are placed on a sounder footing, encouraging suppliers to provide or restore essential credit terms and credit issuers to keep lines in place, while reassuring customers that long-term or further orders will be fulfilled.

Debt-to-equity swaps can be used both in consensual circumstances and in non-consensual circumstances as dissenting creditors can be ‘crammed down’ by a scheme provided the requisite percentage and number have approved the scheme and it has been sanctioned by court. There will often be ‘out of the money’ creditors when debt-to-equity swaps are being implemented by schemes, and in such situations it may be necessary to use a transfer scheme. In these circumstances a scheme is used to cram down any ‘in the money’ creditors and a pre-pack is used to transfer the scheme company’s assets to a new company, thereby leaving ‘out of the money’ creditors with claims against the scheme.

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¹³ 9 August 2006 (unreported).
¹⁴ [2015] EWHC 2593 (Ch).
company with no assets. This was the case with the 2009 IMO Carwash Group scheme,\textsuperscript{15} where the junior lenders were excluded from the scheme on the basis that the value broke in the senior debt on a going-concern valuation and that they consequently had no economic interest in the company. It was therefore equitable to exclude them from the restructuring. The court followed the approach adopted in the earlier Countrywide and McCarthy & Stone schemes, noting in particular that the courts should be slow to reject a scheme that, in the absence of any manifest error or irregularity, the participants generally regarded as being in their commercial interests, especially where the scheme properly constituted the classes of participant creditors, complied with the requirements of company law and did not display any other manifest irregularity.

The implementation of debt-to-equity swaps in more complex, and high-profile transactions has become more apparent. The use of a court-sanctioned scheme to effect a debt-to-equity swap was a key part of the process in the Uniq restructuring,\textsuperscript{16} as was the acquiescence of the UK’s Pensions Regulator and Pension Protection Fund, which was achieved only after protracted negotiations.

Schemes have become a popular tool in large restructurings, and are increasingly being considered by foreign companies that can establish a connection to the UK due to the lack of a local equivalent that would enable them successfully to restructure their debts without the unanimous consent of their creditors.\textsuperscript{17} Foreign companies have been allowed to avail themselves of English law schemes where they can demonstrate both a ‘sufficient connection’ with England and Wales, and that the scheme order would be effective in the jurisdiction in which the company would otherwise be wound up. Following schemes in relation to TeleColumbus,\textsuperscript{18} Rodenstock\textsuperscript{19} and Primacom,\textsuperscript{20} it has become a well-trodden path for the English courts to exercise their scheme jurisdiction over foreign companies on the basis that there is a sufficient connection resulting from the subject matter of the scheme compromise involving English law-governed finance documents that provide for submission to the jurisdiction of the English court. For foreign companies that do not have English law-governed debt, it may be possible to use the amendment provisions in the financing documents to amend the governing law to English law (often this type of amendment will require the support of two-thirds of the lenders) and thereby establish a sufficient connection (see the case summary below for further information about this approach). Another means of establishing jurisdiction is to shift the centre of main interests (COMI) of the company to

\textsuperscript{15} In the matter of IMO (UK) Ltd [2009] EWHC 2114 (Ch) (reported as Re Bluebrook Ltd [2010] 1 BCLC 338).
\textsuperscript{16} Re Uniq plc [2011] EWHC 749 (Ch).
\textsuperscript{17} Following the success of schemes of arrangement in the UK, a number of jurisdictions (such as the Netherlands and Singapore) have recently implemented reforms to their restructuring frameworks. Such reforms have included the adoption of a procedure similar or identical to the UK’s scheme of arrangement in part or in full in order to benefit from the increasing global demand by companies for this popular and flexible restructuring tool. However, the UK remains the most popular forum to effect a scheme as it has been well-tested in the English courts and the case-law continues to evolve to meet the practical and commercial needs of distressed companies.
\textsuperscript{18} Re Tele Columbus GmbH [2014] EWHC 249 (Ch).
\textsuperscript{19} Re Rodenstock GmbH [2011] EWHC 1104 (Ch).
\textsuperscript{20} Primacom Holding GmbH v. A Group of the Senior Lenders & Credit Agricole [2012] EWHC 164 (Ch).
the UK, as was done successfully in the restructuring of Wind Hellas and more recently in the restructuring of Magyar Telecom,\(^{21}\) which successfully implemented the restructuring of New York law-governed bonds through a scheme supported by US Chapter 15 recognition.

The jurisdictional reach of the scheme to implement complex international restructurings is an area of continued development as it increasingly becomes the restructuring tool of choice for balance sheet restructurings of both domestic and foreign companies. The development of schemes of arrangement as a tool for international restructurings has come about through judicial decision-making, and it is anticipated that the English law scheme jurisdiction will continue to thrive in the coming years. The judiciary has generally expressed strong support for the use of schemes for international restructurings, and there has been a trend in recent years for decisions to add further flexibility to the scheme process, which is expected generally to continue; courts have, however, begun to apply greater scrutiny to jurisdictional requirements and information supplied to creditors during the scheme process to ensure that creditors are able to reach a fully informed decision. Some of the recent judicial decisions of note in this area are summarised below.

**Establishing ‘sufficient connection’ with England and Wales**

In *Privatbank*\(^{22}\) the court was satisfied that there was a sufficient connection with England in relation to two subordinated loan notes (the 2016 notes and the 2021 notes) which contained English governing law and jurisdiction clauses, providing jurisdiction to the English courts and which submitted disputes to arbitration with a seat in London. The bank also had a representative office, albeit of an administrative nature, and assets in England.

In *Re Codere*\(^{23}\), the court was satisfied that, despite the Spanish group’s relatively recent acquisition of an English company for the purpose of assuming the group’s liabilities in respect of loan notes in order to enter an English scheme, a number of factors existed to demonstrate a sufficient connection: the intercreditor agreement was governed by English law; 97 per cent of the creditors by value had submitted to the jurisdiction by virtue of signing a lock-up agreement; a significant percentage of noteholders were domiciled in England; and the note trustee and security trustee performed their functions from offices in London. Further, as the English company acquired was incorporated in England, its COMI was in England.

**Amendment of the governing law and the test to establish ‘sufficient connection’**

In order to benefit from the UK’s scheme of arrangement, foreign companies have in recent years sought to amend their foreign-law governed finance and security documents to be governed by English law. The English courts have considered whether such a change in governing law provides jurisdiction to the English courts to sanction a scheme of arrangement. In *Re Apcoa Parking Holdings GmbH and others*\(^{24}\) (the second of two related schemes relating to nine companies incorporated in England, Germany, Austria, Belgium, Norway and Denmark) the proponents of the scheme sought to demonstrate a sufficient connection with England following the amendment of governing law and jurisdiction clauses of the relevant facility agreements to English law and jurisdiction.

\(^{21}\) *Re Magyar Telecom BV* [2013] EWHC 3800 (Ch).
\(^{23}\) *Re Codere Finance (UK) Limited* [2015] EWHC 3778 (Ch).
\(^{24}\) [2014] EWHC 3849 (Ch).
One of the group’s creditors who had not consented to, but was bound by, the change in governing law and jurisdiction clauses strongly contested the schemes arguing that the changes in the governing law and jurisdiction clauses were only made to allow the scheme companies to avail themselves of the English courts’ jurisdiction. The court held that there was a sufficient connection with England for a number of reasons including that creditors had been made aware at the outset that the change in governing law and jurisdiction clauses would be used to persuade an English court to exercise its jurisdiction to sanction a scheme and that the amendment to the governing law was not arbitrary and that it had been provided for in the original debt documentation. Furthermore, a majority of creditors who did not gain from the change in law and jurisdiction consented to the amendment. The court cautioned, however, that in some circumstances a change of governing law to English law in relevant documents would not give rise to a sufficient connection. This might be the case, for example, if there were no connection between the new governing law and the parties’ previous arrangements or if the change in law had been solely to advantage the proponents at the expense of the dissenting parties.

Similarly, in Re DTEK Finance BV, a Dutch company amended the governing law clause of its high-yield bonds to English law in order to implement a restructuring by way of an English scheme of arrangement. The question for the court was whether the connection was truly sufficient given that the amendment had occurred a mere two weeks prior to the scheme sanction hearing. The court held that a change in governing law should by itself establish sufficient connection, and followed the judgment in Apcoa that the original documentation had provided for a change in governing law and was therefore a prospect of which the noteholders should have been aware when purchasing the notes.

Greater judicial scrutiny of the jurisdictional requirements under the EU Judgments Regulation (1215/2012)

Addressing jurisdictional issues is particularly important for schemes involving overseas companies that have a limited jurisdictional nexus with England and given that recognition of the scheme in other countries is a precondition of such scheme becoming effective. The jurisdiction of the English court to sanction a scheme of arrangement under Part 26 of the Companies Act 2006 extends to any company that is liable to be wound up under the IA86. This provides a very broad extraterritorial jurisdiction that covers foreign companies by virtue of Sections 220 and 221(1) of the IA86. However, when considering its scheme jurisdiction, the court must consider any restrictions imposed by the EU Judgments Regulation, which, broadly speaking, provides for jurisdiction based on the defendant’s domicile, which in the case of a scheme is arguably the domicile of the company’s creditors. Whilst the courts are yet to resolve whether or not EU Judgments Regulation applies in scheme cases, on the assumption that it does, foreign scheme companies have relied on two routes to establish jurisdiction under this regulation: Articles 8 and 25.

Article 8 provides that a defendant may be sued in a Member State where at least one ‘defendant’ (treating scheme creditors as defendants) is domiciled, provided that ‘the claims are so closely connected that it is expedient to hear and determine them together’. Two different approaches to the question of how many creditors must be domiciled in England and Wales to satisfy the ‘expediency’ test have emerged in recent cases. On the one hand, the

25 [2015] EWHC 1164 (Ch).
judgments in *Metinvest*,26 *Hibu*27 and *DTEK* suggest that only one scheme creditor must be domiciled in England and Wales for it to be expedient to bring the claim in England because of the desirability of binding all scheme creditors to the same restructuring. On the other hand, in the *Van Gansewinkel* case28 and in *Re Global Garden Products Italy SpA*29 (*GGP*), Snowden J has emphasised that although technically only one scheme creditor is required to be domiciled in England, the ‘expediency’ test may require consideration of the number and value of the creditors domiciled in the UK.

Article 25 is potentially engaged where the relevant documents contain an exclusive jurisdiction clause pursuant to which parties have agreed that the courts of a particular Member State are to have jurisdiction to settle disputes. In *Hibu*, Warren J found that Article 25 can apply to asymmetric jurisdiction clauses despite such jurisdiction clauses only binding one of the parties to a particular jurisdiction rather than both parties. However, in *GGP*, Snowden J found that Article 25 did not confer jurisdiction in respect of ‘asymmetric’ jurisdiction clauses. In *CBR Fashion*,30 the conflicting views in *Hibu* and *GGP* were noted but the position was not resolved as the judge found that the court had jurisdiction to sanction the scheme under Article 8, in any event.

It is expected that future scheme judgments will provide greater clarity on the jurisdictional requirements under the EU Judgments Regulation, specifically in relation to the jurisdiction of the English courts under Articles 8 and 25.

**Greater judicial scrutiny of notice requirements and the scheme company’s evidence and its proposed disclosure to scheme creditors**

The *Indah Kiat*31 judgment reiterates the importance of providing scheme creditors with sufficient notice of the first scheme court hearing (the convening hearing). This should include appropriate disclosure and give sufficient time to enable scheme creditors to consider the matter, take advice and, if desired, participate at the hearing. What constitutes sufficient notice will depend upon the complexity and urgency of the scheme. In this instance, Snowden J found that 14 days’ notice of the convening hearing for a bond scheme that was distributed to creditors via the clearing system was inadequate notice given the lack of justification for its urgency. Snowden J therefore adjourned the hearing for six weeks. In doing so, he cautioned that the court must be astute to detect any attempt to ‘bounce’ creditors into a convening hearing in relation to a complex or novel scheme with inadequate notice.

Snowden J also found that the scheme company’s application did not adduce evidence of sufficient quality and credibility to persuade the court to convene scheme meetings. In doing so, he also cautioned that whether or not there is any opposition, a scheme company has a duty to make full and frank disclosure to the court of all material facts and matters that may be relevant to any decision that the court is asked to make particularly when the court is considering a scheme for an overseas company where recognition of the scheme in other countries will be important.

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26 [2016] EWHC 79 (Ch).
27 [2014] EWHC 370 (Ch).
28 *Re Van Gansewinkel Groep BV and others* [2015] EWHC 2151 (Ch), [2015] All ER (D) 241 (July).
29 [2016] EWHC 1884 (Ch).
30 [2016] EWHC 2808 (Ch).
31 *Re Indah Kiat International Finance Company BV* [2016] EWHC 246 (Ch).
Snowden J has also emphasised, in Van Gansewinkel and more recently, in Indah Kiat, the importance of scheme companies providing sufficient detail of the most likely alternative or ‘comparator’ to the scheme in the explanatory statement and in other evidence. The comparator will most often be a formal insolvency or liquidation but the court needs to be satisfied that the evidence provided is sufficient to justify the comparator chosen and any evidence to substantiate it, such as financial analysis and valuations. The provision of this information is likely to be essential if the scheme is challenged by dissenting creditors. In Indah Kiat, the court criticised the scheme company on the grounds that the draft explanatory statement and the fairness opinion relied on by the company did not contain a full analysis of all of the alternatives to the scheme, such as the discharge of the debts by the parent, which appeared, in fact, to be in a strong financial position.

**Class issues: an unwillingness to fracture classes despite challenges**

The comparator analysis has also played a role in recent cases in relation to the constitution of classes. The English courts have shown an unwillingness to fracture classes where creditors who have different rights prior to the scheme would rank *pari passu* in an insolvent liquidation, where liquidation is the relevant comparator to a scheme. In Privatbank, although creditors held notes maturing at different dates, the relevant comparator to the scheme was insolvency in which noteholders of both the 2016 notes and 2021 notes would rank *pari passu*. Similarly, in Indah Kiat, although the point was not decided, Snowden J’s provisional view was that the dissenting creditor, APPIO, should not be in a separate class from other scheme creditors by virtue of it having taken an assignment of rights under a US judgment that it argued it was entitled to directly enforce against the scheme company.

Another issue relating to the constitution of classes which has featured in recent cases is lock-up fees, (also known as ‘consent fees’ or ‘work fees’). Such fees are often offered to consenting creditors who enter into a binding agreement to support the restructuring. The courts have considered the question whether such fees, which are not paid to creditors who do not consent or consent later, fracture the class. In Privatbank, the consent fee of 2 per cent of the principal amount outstanding on the notes, did not give rise to any fairness or class issues given that it had been offered to all noteholders and was available until five days before the meeting. Richards J proposed that the test that may be applied in relation to consent fees is whether it will have a material effect on the decision of a creditor to support the scheme. In this instance, the 2 per cent fee was not considered to breach the ‘materiality’ threshold.

### iii Hot industries

The retail industry experienced continued restructuring activity in the second half of 2016 and first half of 2017. Several factors affected British retail companies in an unfavourable manner. The changes in the political landscape following the Brexit referendum result in June 2016 and the election result in June 2017, when the Conservative Party retained its position as the largest party in Parliament but failed to achieve a working majority in its own right, has generated uncertainty that, combined with surging consumer debt levels, contributed to the weakening of the value of sterling. This depreciation has subsequently increased operating and importing costs for UK retailers. The political uncertainty may also have reduced consumer confidence, which, in turn, has further increased economic uncertainty and caused discretionary consumer spending to shift away from retail. This was evidenced by a decline
in retail sales by 1.4 per cent in the first quarter of 2017, the largest quarterly fall since 2010. These factors will likely continue to impact British retail stores in the third quarter of 2017 and beyond.

The shipping industry also saw continued restructuring activity in 2016, and such activity is expected to continue through the end of 2017. Sluggish demand for shipping has caused industry capacity to far outweigh demand, resulting in downward price pressures. Shipping companies are now experiencing increased operating costs, low freight rates and deteriorating asset values. These factors, coupled with diminished returns for investors, have caused lenders to tighten access to new finance, resulting in liquidity issues for shipping companies. In the absence of positive market indicators in the short to medium term, it is likely that such liquidity issues will persist. Even top performing companies may experience financial hardship due to depleting cash reserves and may need to restructure. The global shipping industry continues to face a bleak environment, as evidenced by Hanjin Shipping entering into insolvency proceedings and ultimately being liquidated in February 2017. This was one of the largest insolvencies in the history of the shipping industry, and has caused severe disruptions to many of the UK’s businesses that operate within, or are reliant upon, the worldwide shipping industry.

The oil and gas sector experienced significant restructuring activity throughout 2016. Despite the recent upsurge in commodity prices, the reduced oil prices this past year resulted in a slowdown in offshore capital expenditure and negatively affected the financial health of several businesses in the oil and gas sector. The weakened oil price environment, dropping to as low as US$45/bbl in June, and increasing field costs associated with drilling, production and transportation have exacerbated the financial difficulties experienced by industry incumbents. Corporates with restricted access to production and transportation infrastructure remain particularly vulnerable to restructuring pressure, as revenues have dropped below the break-even point. These market challenges have also added additional pressure on oil servicing companies that are expected to continue to suffer as a result of the slowdown in offshore capital expenditure.

The construction and industrials sector has been significantly affected by Brexit-driven uncertainty. Although 2017 will see the completion of a number of large infrastructure projects, restructuring activity is predicted to remain widespread throughout the sector. This can be attributed in part to subdued business confidence and mounting costs across the supply chain, which is likely to contribute to project delays and ongoing challenges for construction companies. In accordance with the trend seen in previous years, the construction industry was the sector responsible for the most administration appointments in 2016, totalling 277 appointments across all four quarters. Ongoing difficulties indicate that restructuring activity will remain rife in the short to medium-term.

V INTERNATIONAL

The main sources of cross-border insolvency law in the UK are the Regulation on Insolvency Proceedings (recast) (Recast Insolvency Regulation),32 the Cross-Border Insolvency Regulations 2006,33 which implement the UNCITRAL Model Law on Cross-Border

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33 SI 2006/1030.
Insolvency (Model Law), Section 426 of the IA86 and the underlying common law. As discussed elsewhere in this chapter, the framework applicable to cross-border insolvencies may be subject to significant change in the coming years as a result of the UK’s decision to leave the EU.

i Recast Regulation

After a lengthy process of negotiation, on 20 May 2015, the European Parliament and the Council of the EU officially adopted the Recast Regulation, replacing the EU Regulation on Insolvency Proceedings (Insolvency Regulation).34 The Recast Insolvency Regulation entered into force on 25 June 2015, although the majority of its provisions came into effect from 26 June 2017.35

Under the former Insolvency Regulation, any main proceedings opened in a Member State of the EU were required to be generally recognised without any further formality in all other Member States from the time of the opening of such proceedings. The Insolvency Regulation stipulated that main proceedings could only be opened in the jurisdiction where the company has its COMI; a rebuttable presumption was included that the location of the company’s COMI would be the jurisdiction in which the company is incorporated.

The fundamental premise that insolvency law is a matter for each EU Member State has remained embedded within the Recast Regulation, which seeks to strengthen the framework of recognition and cooperation that the Insolvency Regulation introduced upon its entry to force in 2002. The amendments in the Recast Regulation extend the scope of the Insolvency Regulation to cover ‘preventative’ insolvency proceedings, clarify the criteria for jurisdiction and establish a system to increase transparency for debtors, thereby bringing it into line with developments in national insolvency laws. The Recast Regulation introduces the following measures:

a Measures have been introduced to discourage abusive forum shopping, namely by changing the presumptions applied in relation to the location of COMI. The Recast Regulation introduces a formal definition of the term ‘COMI’ that allows courts to investigate and identify if a debtor’s move to a new jurisdiction before filing for insolvency is genuine and not abusive. The period of investigation has been set at three months for business professionals and six months for individuals.36

b A new procedure, to be known as a ‘group coordination proceeding’, will allow for coordination on insolvencies of groups of companies, in which group members can choose to participate. The Recast Regulation further provides for a flexible framework for cooperation between officeholders and courts dealing with the insolvency of a group of companies.37

c Pre-insolvency rescue proceedings will be included in the definition of main proceedings, as the scope of proceedings is broadened. Secondary proceedings will no longer be limited to winding-up proceedings. For the UK, however, schemes of arrangement under Part 26 of the Companies Act 2006 will remain outside the scope of the Recast Insolvency Regulation.38

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36 Ibid, Article 3.
37 Ibid, Chapter V.
38 Ibid, Articles 1 and 3.
Provision is made for a court to be able to postpone or refuse a request to open secondary proceedings. In certain situations, an officeholder of the main proceedings may, with the support of local creditors, give an undertaking as to the treatment of creditors in other Member States in order to avoid secondary proceedings in those jurisdictions. Various other mechanisms have been introduced to minimise the need to open secondary proceedings.

EU-wide insolvency registers will be established so that they are searchable in all official languages of the EU (although these provisions will not come into force at the same time as the majority of the new provisions).

In relation to the determination of a company’s COMI, the leading authorities under the Insolvency Regulation are the rulings of the European Court of Justice in Re Eurofood IFSC and Interedil Srl (in liquidation) v. Fallimento Interedil Srl and another. In Eurofood, it was held that in the case of a company whose registered office and that of its parent company are situated in two different Member States, the presumption that its COMI is in the jurisdiction in which it is incorporated can be rebutted only if there are factors, objective and ascertainable by third parties, which enable this to be established to the contrary. The mere fact, however, that a parent company controls, or can control, the economic choices of its subsidiary, where the subsidiary has a registered office and carries on its business in another jurisdiction, is not enough to rebut this presumption. The Eurofood test was subsequently applied by the English High Court in Re Stanford International Bank Limited and others.

Interedil established the principle that, in determining a company’s COMI under the Insolvency Regulation, more weight must be given to the location of the company’s central administration in accordance with Recital 13 of the Insolvency Regulation (which states that a debtor’s COMI must correspond to the place where it regularly conducts the administration of its interests). If the company’s management and supervision take place in the location of the company’s registered office, this will be the location of the company’s COMI. If the company’s central administration takes place elsewhere, the presumption regarding the jurisdiction of incorporation will be rebutted. Consistent with Interedil, in Olympic Airlines SA Pension and Life Assurance Scheme v. Olympic Airlines SA, the English Court of Appeal held that a company not conducting economic activity has no establishment in the UK, and hence the Court has no jurisdiction to commence secondary proceedings in such cases.

In the context of European cross-border insolvencies involving proceedings in multiple jurisdictions, and given the focus on group coordination proceedings in the Recast Regulation, the English High Court’s decision in Re Nortel Networks SA & Ors is of interest. In this case, an application was made by the UK administrators of certain companies in the distressed Nortel Networks group to send letters of request to the courts in a number of other European jurisdictions, asking those courts to notify the administrators of any application to open secondary insolvency proceedings in respect of any companies in the Nortel Networks group.

39 Ibid, Article 36.
40 Ibid, Articles 25-30.
41 Case C-341/04.
42 Case C-396/09.
43 [2009] EWHC 1441 (Ch).
45 [2009] EWHC 206 (Ch).
The High Court made it clear that a duty of cooperation between insolvency officeholders existed and that it extended to the courts that exercised control of secondary insolvency proceedings in their respective jurisdictions, particularly in cases where foreign insolvency proceedings could potentially impede a successful restructuring of the group as a whole. On this basis, the High Court ruled in favour of the administrators, stating that it was highly desirable that the requested assistance from the foreign courts be sought. The Court authorised the sending of the letters of request. This decision is important for insolvency practitioners as the ability of courts to cooperate with each other has been a critical factor in recent European cross-border insolvency reform, as evidenced by the Recast Regulation.

ii Cross-Border Regulations

The Cross-Border Regulations enacted the Model Law in the law of Great Britain (i.e., England, Wales and Scotland) in April 2006. The Cross-Border Regulations provide, inter alia, for the recognition of a foreign proceeding commenced or officeholder appointed in any foreign jurisdiction, regardless of whether that foreign jurisdiction has enacted a version of the Model Law.

The High Court heard its first reported case for recognition and relief under the Cross-Border Regulations in November 2006 in the case of Re Rajapakse.46 The Registrar heard an application for recognition by a US Chapter 7 trustee. In granting a recognition order, the Registrar also produced a note of helpful observations for practitioners when making such applications (including what documents must be filed, process for doing so, how to effect service).

Earlier in 2009, the High Court heard the case of Samsun Logix Corporation v. DEF47 under the Cross-Border Regulations, in which it recognised the primacy of the rehabilitation proceedings commenced by Samsun in its home jurisdiction of Korea, together with the order that the Korean court granted, imposing a moratorium on the commencement and continuation of creditor actions and proceedings against Samsun in the UK.

In subsequent cases, the Cross-Border Regulations have been successfully used to obtain recognition from the English courts of insolvency proceedings in the BVI,48 Denmark,49 Switzerland50 and Antigua.51 In light of the introduction of the Cross-Border Regulations and the above cases, it is expected that there will be an increased number of overseas office holders who will seek recognition of overseas proceedings and their domestic powers in the UK.

The Cross-Border Regulations provide that, on the recognition of a foreign proceeding, the court may order ‘the delivery of information concerning the debtor’s assets, affairs, rights, obligations or liabilities’,52 and may grant ‘any additional relief that may be available to a British insolvency office holder under the law of Great Britain, including any relief provided

48 Akers and McDonald v. Deutsche Bank AG (Re Chesterfield United Inc. and Partridge Management Group SA) [2012] EWHC 244 (Ch).
49 Larsen and others v. Navios International Inc. (Re Atlas Bulk Shipping A/S) [2011] EWHC (Ch) 878.
50 Cosco Bulk Carrier Co Ltd v. Armada Shipping SA and another [2011] EWHC 216 (Ch).
52 Article 21(1)(d), Schedule 1 of the Cross-Border Regulations.
under Paragraph 43 of Schedule B1 to the Insolvency Act 1986’.\(^{53}\) In granting such relief, the court must be satisfied that ‘the interests of creditors […] and other interested persons, if appropriate, including the debtor, are adequately protected’.\(^{54}\)

The court in *Re Bernard L Madoff Investment Securities LLC, between Picard v. Fim Advisers LLP and others*\(^{55}\) interpreted these articles to mean that it only had jurisdiction to make an order under Article 21 if the information sought by a US corporate trustee in bankruptcy concerned the assets, affairs, obligations or liabilities of the insolvent US company. The subsequent case of *Akers and McDonald v. Deutsche Bank AG (Re Chesterfield United Inc and Partridge Management Group SA)*\(^{56}\) saw a departure from this restrictive approach. In Chesterfield, the court held that the power of general assistance contained in Article 21(1)(g) was not to be construed narrowly with reference to the categories of discretionary assistance specifically listed elsewhere in Article 21(1). Accordingly, the court made an order under Section 236 of the IA86 (an information disclosure provision) that required Deutsche Bank to make substantial disclosure to the liquidators of two BVI companies.

Practitioners should also note the cases of *Nordic Trustee ASA and another v. OGX Petróleo e Gós SA (Em Recuperação Judicial) and another*,\(^{57}\) and *Ronelp Marine Ltd v. STX Offshore & Shipping Co Ltd*.\(^{58}\) In *Nordic Trustee v. OGX Petróleo*, the High Court held that, when a foreign insolvency office holder makes an application to the English court for recognition under the Cross-Border Regulations, the office holder must disclose to the court the possible impacts of recognition on third parties not represented before the court, for example, as a result of a stay order made following recognition. In *Ronelp Marine v. STX Offshore*, the High Court considered the ‘exceptional’ circumstances in which it should lift a stay made under the Cross-Border Regulations to allow English litigation proceedings against STX Offshore for recovery of an unsecured monetary claim to be continued, rehabilitation proceedings in South Korea relating to STX Offshore notwithstanding. The identified factors of ‘sufficient weight’ that persuaded the High Court to lift the stay included: the complexity of the legal issues involved (the High Court felt it more appropriate for it to make a determination on an English law governed illegality argument than the Korean court before which STX Offshore had entered rehabilitation proceedings); the reasonably well advanced stage of the English litigation together with the costs involved in preparation for trial; the adjudication and quantification of the claim more speedily in the English proceedings would allow the claimants to vote on the rehabilitation plan in the Korean proceedings; the lifting of the stay would not impede the rehabilitation plan, and could potentially assist it; and allowing the English litigation to proceed would not unduly advance the interests of the claimants over the interests of STX Offshore’s creditors as a whole.

### iii Judicial assistance to proceedings commenced in another jurisdiction

Section 426 of the IA86 provides for the UK courts to give assistance upon request to the courts of other designated jurisdictions, which are mainly Commonwealth countries. Where Section 426 applies, it provides an alternative means of relief and assistance to the Insolvency

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\(^{53}\) Article 21(1)(g), Schedule 1 of the Cross-Border Regulations.

\(^{54}\) Article 22(1), Schedule 1 of the Cross-Border Regulations.

\(^{55}\) [2010] EWHC 1299 (Ch).

\(^{56}\) [2012] EWHC 244 (Ch).

\(^{57}\) [2016] EWHC 25 (Ch).

\(^{58}\) [2016] EWHC 2228 (Ch).
Regulation and the Cross-Border Regulations, and the UK courts can apply the insolvency law of either jurisdiction in relation to the assistance requested. For example, in the case concerning the Australian-based insurance group, HIH,59 the House of Lords allowed the repatriation of funds to the Australian liquidators pursuant to a letter of request from the Australian court under Section 426. In HSBC Bank plc v. Tambrook Jersey Ltd,60 pursuant to a letter of request from the Royal Court of Jersey, the English Court of Appeal confirmed that a company with its COMI in Jersey could commence administration proceedings in England in a case where there are no extant or anticipated formal insolvency proceedings in Jersey.

In the important case of Rubin v. Eurofinance SA,61 the Supreme Court confirmed that English courts have a common law power to recognise and grant assistance to foreign insolvency proceedings. On the question of enforcing foreign insolvency judgments, however, the Supreme Court held that the English courts will only enforce a foreign judgment against a party that was present in the foreign jurisdiction when the proceedings were commenced, or that made a claim or counterclaim in the foreign proceedings, or that appeared voluntarily in the foreign proceedings, or that otherwise agreed to submit to the foreign jurisdiction. See Section III, supra, for a discussion of a further recent case of note in this area.

Further, although they are becoming increasingly rare, there are also examples of insolvency protocols being used in cross-border insolvencies involving the UK in order to harmonise the separate proceedings commenced in different jurisdictions. For example, protocols were used in the Maxwell Communications case in 1991, and more recently in the case of the UK shipping business, Cenargo.

Practitioners should also note the case of Re DP Holding SA (In Provisional Liquidation): Hellard and another v. Chen and others,62 in which the High Court refused an application by the respondents to set aside a Section 426 order granted by the High Court permitting the provisional liquidators of DP Holding SA, a company incorporated in Switzerland, to issue an application under section 236 of the IA86 to seek the private examination of the respondents in aid of proceedings taking place in the British Virgin Islands. The High Court dismissed the respondents’ arguments that the Section 426 order should be set aside on the basis that: there had not been any intention or attempt to mislead the BVI court in relation to the provisional liquidators’ failure to act in accordance with commitments made to the court in the British Virgin Islands and their delay in serving the order, meaning that it would be disproportionate to discharge the order and compel the applicants to start afresh; and while the fee arrangement between the applicants and their solicitors was highly unusual, the applicant’s solicitors had made proposals that disposed of the respondents’ justified concern.

VI FUTURE DEVELOPMENTS

i The UK as a forum of choice for international restructurings

The UK is an attractive jurisdiction for restructuring because of the flexible and business-friendly legal procedures available, and because of the expertise shared by its specialist insolvency

60 [2013] EWCA Civ 576 (22 May 2013).
62 [2017] All ER (D) 21 (March).
judges and practitioners. Companies from other countries, and in particular other EU Member States, have frequently used UK insolvency processes for successful restructurings and the UK has become a forum of choice for international restructurings, with the UK scheme of arrangement serving as the principal competitor to US Chapter 11 proceedings in the international restructuring market.

Two main methods may be used by foreign companies to benefit from a UK insolvency process. First, the Recast Regulation and the Cross-Border Regulations allow a foreign company to enter a UK insolvency process, which in most cases would be administration, if it can be established that the COMI of the business is in the UK. Given sufficient time and resources, a COMI shift may be achieved, through which enough factors pertaining to the central management and control of the business are moved to the UK to satisfy a court that the COMI is located in the jurisdiction.63

Second, a scheme of arrangement in relation to a foreign company may be sanctioned by the English court if it is satisfied that there is a sufficient connection with the jurisdiction. The sufficient connection test and some significant jurisprudence in this area are discussed in more detail above, but in terms of international restructurings it is worth noting the continuing utilisation of the scheme jurisdiction by foreign companies where the governing law of the relevant finance documents is English law or where the governing law is changed to English law in order to avail the company of the UK scheme jurisdiction to implement a restructuring. While the English courts, and in particular, Snowden J, have sought to increase the threshold for acceptability of schemes and the level of scrutiny on scheme evidence, these developments are aimed at strengthening the quality, and therefore desirability, of the UK’s scheme of arrangement.

ii The impact of Brexit

The UK’s relationship with the EU appears likely to change significantly in the coming years as a result of the recent UK referendum decision to leave the EU, and this may have an impact on the recognition and enforcement of schemes of arrangement (as well as UK insolvency processes such as administration) in EU jurisdictions. It is not possible at this stage to predict with any certainty the form of relationship that will exist between the UK and the EU in the future, and it is, of course, possible that the UK will not in fact leave the EU. If the UK does leave the EU, there is a range of possible outcomes, from (at one extreme) European Economic Area (EEA) membership, which would put the UK in a similar position to that of Norway, to (at the other extreme) no trade agreement, which would place relations between the UK and the EU on a World Trade Organization (WTO) basis. It is possible that a unique arrangement will be reached that does not reflect any current precedents, but considering the possible position under these two extremes provides an indication of the issues that are likely to arise.

If the UK were to retain EEA status, it would be open for the UK to seek to agree with the EU that the Recast Regulation would continue to apply to the UK, although this would be unprecedented as the Recast Regulation does not currently apply to any non-EU members. The continuation of the Recast Regulation would be essential for the automatic recognition of UK insolvency processes in the EU. Where Member States have passed laws

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63 Note that judicial endorsement for the practice of COMI shifting has been expressed in UK cases such as *Re Hellas Telecommunications (Luxembourg) II SCA* [2009] EWHC 3199 (Ch) and *TXU Europe German Finance BV* [2005] BCC 90.
based on the Model Law, this may help UK insolvency office holders seeking recognition, but as at the time of writing, the only other EU Member States that have done so are Greece, Poland, Romania and Slovenia. The Recast Regulation is not relevant to the recognition and enforcement of schemes in the EU, although the option of shifting COMI to the UK to establish jurisdiction for a scheme could be more difficult if the Recast Regulation were no longer in force. In a situation where there is no trade agreement between the UK and the EU, the continuation of the Recast Regulation with regard to the UK appears very unlikely, which would mean that recognition of UK insolvency processes in the EU would depend on judicial comity, as decided by courts on a case-by-case basis.

Importantly, in the context of the UK’s possible departure from the EU, the scheme jurisdiction over foreign companies does not depend on the Recast Regulation. Nevertheless, when sanctioning a scheme, the scheme company must satisfy the English court that the scheme will have a substantial effect that, for a foreign company, involves establishing that it is likely to be recognised in any key jurisdictions where it could be challenged, such as the jurisdiction where the scheme company is incorporated or where it has significant assets. Arguments for the recognition and enforcement of schemes of arrangement in the EU are usually based on private international law and the Brussels Regulation. As with the Recast Regulation, the Brussels Regulation does not currently apply to any non-EU members, and so its continuation with regard to the UK after the UK’s departure from the EU would be unprecedented. A more viable option is, however, presented by the existence of the Lugano Convention, which currently applies to the EU, Switzerland, Norway and Iceland and is similar to the EU Judgments Regulation. As an EEA member, therefore, it seems likely that the UK could accede to the Lugano Convention, which would support the continuing recognition and enforcement of schemes in the EU. If the UK had no trade agreement with the EU, Lugano Convention membership would appear to be unlikely, and recognition and enforcement of schemes of arrangement in the EU would be a matter entirely for the private international laws of EU Member States; nevertheless, it is likely that in these circumstances EU Member States would not have a problem with continuing to recognise and enforce the effect of schemes of arrangement in accordance with their own private international laws and without the added assistance of the Brussels Regulation.

iii The EU’s proposal for a directive on preventive restructuring frameworks

On 22 November 2016, the European Commission released a proposal for a directive on preventive restructuring frameworks, second chances and measures to increase the efficiency of restructuring, insolvency and discharge procedures, amending Directive 2012/30/EU. Among others, one main objective of the proposal is to ensure that Member States

64 Council Regulation (EU) 1215/2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (recast) (also known as the Recast Brussels Regulation), which has applied from 10 January 2015, superseding the 2001 Brussels Regulation.

65 Convention on jurisdiction and the enforcement of judgments in civil and commercial matters signed in Lugano on 30 October 2007.

66 Directive 2012/30/EU of the European Parliament and of the Council of 25 October 2012 on coordination of safeguards that, 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 Text with EEA relevance.
The EU has recognised that the current differences between the insolvency regimes of the different Member States translate into additional costs for investors in cross-border restructurings. The scheme of arrangement is widely used in this context and was used as a template for the preventive restructuring frameworks presented in the proposal. The main points of the proposal are summarised below:

a. debtors accessing restructuring procedures should remain in control of their assets and existing management should have day-to-day operation of the business;

b. appointment by court of an insolvency practitioner should be limited to exceptional cases;

c. preventive restructuring frameworks should be available on the application of debtors, or of creditors with the agreement of debtors;

d. a debtor should be able to initiate a temporary moratorium for up to four months through a court application;

e. the stay should cover individual enforcement actions and the opening of insolvency proceedings where they may adversely affect a restructuring and the obligation of a debtor to file for insolvency would be suspended for the duration of the stay; and

f. if complex restructurings require more time Member States may allow courts to grant a longer stay up to a maximum of 12 months.

The proposal further provides that the Member States should determine a framework for the adoption of restructuring plans. Any affected creditors should have the right to vote on the adoption of a restructuring plan. Member States may also grant such voting rights to affected equity holders. For voting purposes, the affected creditors should be separated in classes that should be formed in such a way that each class comprises claims or interests with rights that are sufficiently similar to justify considering the members of the class a homogenous group with commonality of interest and as a minimum secured and unsecured claims should be treated in separate classes. A restructuring plan shall be deemed to be adopted if a majority in the amount of claims is obtained in every class. The level of majority may be determined by Member States but may not be higher than 75 per cent of the claims in the class. Where the necessary majority is not reached in one or more voting classes, the plan may still be confirmed by a cross-class cramdown procedure, whereby if the plan has been approved by at least one class of affected creditors other than an equity-holder class and any other class that, upon a liquidation of the enterprise, would not receive any payment or other consideration, the court may approve the plan.

It remains to be seen if and how the proposal will be implemented by the European Parliament, the Council and ultimately the Member States. It is already apparent that the proposal has been welcomed by many practitioners in Europe. The proposed frameworks have considerable similarities with the scheme of arrangement procedure as well as restructuring under US Chapter 11. Therefore, if the frameworks proposed become widely adopted in the EU, the UK’s position as the forum of choice for European cross-border restructurings may in time be adversely affected, although no legislation can provide for the institutional and cultural advantages that form a large part of the UK’s attractiveness in this area.

iv Conclusion

The possibility of the UK’s departure from the EU may have an adverse impact on the ability of EU companies to benefit from UK insolvency processes. Further, if the EU were
to develop more attractive restructuring procedures as set out in the proposed directive discussed above, European businesses may choose to pursue cross-border restructurings in other jurisdictions. It is anticipated, however, that the factors that make the UK an attractive forum for international restructurings, and the structural and cultural shortcomings that make many foreign companies, both within and beyond the EU, reluctant to pursue complex restructurings in their home jurisdictions, will continue regardless of the political events to come.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

In Finland restructuring and insolvency activity has been decreasing for many years. The Finnish economy is expected to finally recover after almost a decade of downturn. During 2016 the increase of total production was 1.4 per cent. In 2017 the GDP is expected to grow by 1.2 per cent and the growth is broader based than last year. The increase is mainly owing to the increasing confidence of the consumers as well as good indications in the rate of employment, both causing growth in private consumption. Private investments have also been increasing. However, it is to be noted that the industry production has grown only in a very moderate way. The economy is, nevertheless, expected to grow slightly in the coming years. The Finnish economic situation mirrors the global situation. There are concerns that politicians will not be able to implement labour law reforms. The rise of protectionism is also a growing concern.

The liquidity of companies seems to be adequate. There are sufficient funding possibilities in the markets, reflecting the companies’ financial situation. On the other hand, the decreasing amount of bankruptcies can partly be explained by the assumption that many small companies do not go through the whole liquidation process as initiated bankruptcy proceedings will collapse because there are no funds to cover the costs of the proceedings and usually the debtors are not willing to participate by paying the costs.

Global events such as the worldwide economic crisis still influence the financial markets. From the Finnish perspective the main effect seems to be the relatively cheap price of funding. It has caused consumers to view the economic situation in a more optimistic way and to support the economic growth. In addition, the construction sector is growing, as there are many large-scale building initiatives ongoing. Furthermore, the level of the oil price and the value of the Russian rouble keep exports to Russia at a more moderate level than previously.

During 2016 there were 2,845 finalised bankruptcy proceedings, which is 10.2 per cent less than in 2015. In addition, the amount of bankruptcies has decreased by 29.6 per
cent between January 2017 and April 2017. One of the main initiators in the bankruptcy proceedings, the Finnish tax administration, filed 55.6 per cent fewer bankruptcy applications between January 2017 and August 2017 than in the corresponding period in 2016.

The majority of the bankruptcy proceedings have lapsed due to the lack of required funds to finance the proceedings. This indicates that the majority of the bankrupt companies are small.

In 2016 there were 6.8 per cent fewer finalised restructuring proceedings than in 2015. However, between January 2017 and April 2017 there were 118 applications for restructuring, which is 14.6 per cent more than in the corresponding period in 2016. In addition, 98 of these applications were approved. During 2016 the majority of restructuring proceedings ended with a court-approved restructuring programme. However, restructuring proceedings are very often discontinued as the applicant goes bankrupt.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

Finnish legislation recognises two alternative overall insolvency proceedings for companies: bankruptcy and restructuring. Bankruptcy aims to divide the remaining assets of an insolvent company between its creditors. Restructuring aims to arrange the debts and to rehabilitate the viable business of the company in order to keep the business running.

i Bankruptcy proceedings

Bankruptcy proceedings are regulated in the Finnish Bankruptcy Act and begin with a district court's order upon an application. The application may be filed by the debtor or by a creditor. In practice, a majority of bankruptcy proceedings commence by a petition of Finnish insurance companies or tax authorities.

The main prerequisite for a bankruptcy is that the company is insolvent, (i.e., other than temporarily unable to repay its debts as they fall due). When the debtor itself petitions for a bankruptcy, its own announcement of insolvency is generally sufficient. If the bankruptcy has been petitioned by a creditor, the district court must investigate the claimed insolvency in more detail. If the debtor contests the petition, the matter will be handled in the court as a non-contentious civil case.

Unless the debtor proves otherwise, the district court generally deems it insolvent if: (1) the debtor has discontinued its payments; (2) it has been determined in enforcement proceedings that the debtor cannot repay the claim in full; or (3) the debtor has not repaid the clear and due claim of the creditor within a week of the receipt of a reminder. In practice debtors are deemed insolvent relatively easily. A debtor may not be declared bankrupt on the petition of a creditor if the creditor holds adequate collateral. Bankruptcy may be ordered reversed on the joint petition of the debtor and the creditor who filed the bankruptcy petition or, if the debtor has been declared bankrupt on his or her own petition, on the petition

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5 Statistics Finland, publication 17 May 2017.
6 Statistic Finland, publication 7 June 2017.
7 There are two other insolvency methods, the adjustment of the debts of a private individual and the general enforcement, but they are not presented here in more detail.
8 Finnish Bankruptcy Act 20 February 2014/120. The Act came into force on 1 September 2014.
of the debtor. The application for reversal must be filed within eight days of the order of bankruptcy. There must be a valid reason for the reversal. Said valid reason is, in practice, usually that the receivables of the creditor who filed the bankruptcy petition have been paid.

At the beginning of a bankruptcy, a district court appoints an estate administrator. The estate administrator is usually an attorney-at-law that the creditors have suggested. When bankruptcy proceedings begin the debtor loses its authority over the company’s assets and the assets are transferred to the possession of the estate and are governed by an estate administrator. The creditors who have a claim in bankruptcy proceedings exercise their authority over the bankruptcy estate in the creditor’s meeting. The main rule is that the creditors must lodge their claims before a certain lodgement date in order to become creditors of the bankruptcy process.

A claim in bankruptcy proceedings means a debt is owed by the debtor and based on a commitment or other legal basis that has arisen before the beginning of bankruptcy. The debts that have arisen after the beginning of bankruptcy are not claims in the bankruptcy proceedings and the bankruptcy estate is obliged to pay them when they fall due. This means that a bankruptcy estate can also be declared bankrupt.

The purpose of a bankruptcy is to divide between the creditors as high a level of disbursement as possible. Secured debts have the primary right to disbursements. A bankruptcy ends either with the certification of the disbursement list and the payment of disbursements or with the collapse of proceedings. In practice many small companies do not go through the whole liquidation process as the proceedings collapse because there are no funds to cover the costs of the proceedings. Usually the debtors are not willing to participate in funding the bankruptcy process. In some cases, the bankruptcy may continue as a public receivership, in which the costs of bankruptcy proceedings are paid from state funds in so far as the funds of the bankruptcy estate are insufficient to cover the costs of bankruptcy proceedings. Commencing the public receivership requires in practice adequate public interest to conduct the estate administration. This means a need to clarify the estate, for example, in order to be able to file a request for criminal investigation to police officials. The public receivership can also be commenced if the funds are not sufficient to cover the costs of the bankruptcy proceedings or if there are other significant reasons.

The estate administrator is obliged, within two months from the beginning of bankruptcy, to draft an estate inventory and a debtor description (the trustee’s clarification and observations of the debtor’s business and \textit{inter alia} reasons that led to insolvency, as well as observations made by the trustee). As from 1 March 2013 the estate administrator is obliged to present the debtor description to the prosecutor, the debtor, the main creditors and, at request, also to other creditors and the pretrial investigation authority, namely, the police. Also as from 1 March 2013 the estate administrator is – with certain limitations – obliged to draft a request for investigation for police authorities if the estate administrator has any reason to suspect that the debtor has committed a crime.

\textbf{ii Restructuring proceedings}

Restructuring proceedings are regulated in the Finnish Restructuring of Enterprises Act.\textsuperscript{9} Restructuring proceedings include debt arrangements that are made in order to rehabilitate a distressed and insolvent company’s viable business and to ensure its continued viability.

Restructuring proceedings require that the company is insolvent or at least faces imminent insolvency, but should commence before the cash flow forces the company or its creditors to reconsider bankruptcy. Restructuring proceedings are fairly expensive and time consuming as it normally takes about a year before a possible restructuring programme is approved and the proceedings end. If the company’s assets are not sufficient to cover the costs of the proceeding, the proceeding cannot be started. During the proceedings the company normally faces difficulties with suppliers etc., owing to entries in the official records stating that the company is undergoing restructuring proceedings. These entries are indicators of insolvency and they tend to lead to suppliers etc. requiring payment up front, which can be harsh on an insolvent company.

Restructuring proceedings cannot be started if the debtor is insolvent and it is probable that the restructuring programme will not remedy the insolvency or prevent its recurrence other than for a short period, nor can they be started if it is probable that the debtor will not be able to repay debts arising after the commencement of the proceedings. In addition, any debtor’s offences or other criminal actions by the company or anyone acting on its behalf, or material defects in the company’s books, will also form a barrier for restructuring proceedings.

The application for restructuring proceedings may be filed by the debtor, creditor, several creditors together or a probable creditor. Restructuring proceedings begin with a district court’s order upon an application, which normally is filed by the debtor company itself. When the restructuring proceedings begin, the court appoints an administrator. A court-appointed administrator, most often an attorney-at-law, will help the company to find different ways of rehabilitating the business.

The administrator shall prepare a report of the debtor’s assets, liabilities and other undertakings and regarding the circumstances that affect the financial position of the debtor and its expected development. The purpose of the report is to enable the creditors to assess the possibilities for an enforceable restructuring programme. The administrator monitors and supervises the debtor’s activities that are subject to the proceedings and sees to an audit of the debtor’s activities.

The administrator’s main task is to prepare a draft-restructuring programme together with the debtor and with the assistance of the creditors. The debtor and the creditors are also allowed to submit their own competing programmes to the court. It is common for the debtor to submit a competing programme but very rare for the creditors to do so. There are no regulations or case law on how a creditor-based programme should be dealt with together with the administrator’s programme. The restructuring programme shall specify the measures and arrangements designed to improve the debtor’s activities and the measures and arrangements that affect the status of the debtor and the creditors, as well as the reasons for the same. The programme should contain provisions on the debtor’s activities, whether they are to be continued or altered, the measures and arrangements relating to the assets of the debtor, such as allowing the debtor to retain assets, the liquidation or transfer of assets, the manner of liquidation or transfer, and the resulting or expected revenue from the same, arrangements regarding restructuring debts and the duty to make supplementary payments, arrangements regarding the personnel and remunerations to the debtor or an entity or person close to it for their services, and the financing and monitoring of the programme.

The restructuring programme must be approved by a majority of the creditors of the company. Therefore, if there is a justifiable reason to believe that the necessary conditions for the preparation or approval of a restructuring programme for the debtor do not exist, the application should not be approved in the first place or the proceedings should be interrupted.
One significant difference between restructuring and bankruptcy proceedings is that the commencement of restructuring has no effect on the debtor’s authority to dispose of its property and to decide on its activities. Some activities, such as taking on a new debt or the transfer of business require the consent of the court-appointed administrator.

The commencement of restructuring proceedings has no effect on the existing undertakings of the debtor, but the commencement of proceedings interrupts the accrual of overdue interest on restructuring debts. An interdiction of repayment of restructuring debts follows from the commencement of the proceedings. The restructuring debts can only be paid based on an approved restructuring programme or with the administrator’s approval (e.g., small debts). After the commencement of the proceedings, no measures can be directed at the debtor in order to collect on a restructuring debt. This provides the debtor time to find ways to rehabilitate the business.

Debt arrangements cover only restructuring debts that have arisen before the filing of the restructuring application, and all debts arisen after the filing must be paid when falling due. Restructuring proceedings cannot be used to prevent a creditor from collecting his or her claim or otherwise to violate the rights of a creditor. There must, hence, be a genuine aim to rehabilitate the company.

The restructuring programme should contain and specify, for example, the measures and arrangements that are meant to improve the debtor’s business, the measures and arrangements that affect the status of the debtor and the creditors, as well as the reasons for the same. The programme must also contain a payment programme, which includes a schedule of payments of the restructuring debts. The payment programme includes information about the percentage to be cut from the debts. The average cutting percentage ought to be around 40 to 60 per cent. There are no provisions on how long the programme can be but the majority of programmes are between five to 10 years, only a small minority lasts less than two years or more than 10 years.\(^\text{10}\)

When a restructuring programme has been approved by the district court, all entries are removed and the company can perform its business with only the restrictions that are mentioned in the programme. The programme itself is enforceable, so should the debtor not pay its restructuring debts in accordance with the programme or otherwise act as required in the programme, a creditor can file for bankruptcy.

### Duties of directors of companies in financial difficulties

The Finnish Limited Companies Act\(^\text{11}\) includes provisions covering the directors’ liabilities in financial difficulties. Many of the provisions originate from the need to inform the shareholders and debtors as well as official authorities of the difficulties. The main principles according to the Finnish Limited Companies Act are that the management of the company shall act with due care and promote the interests of the company. The requirement to act with due care is connected to the liability issues: the board members, CEO as well as the member or members of the administrative board are always liable for the damages for the loss that they, in violation of the duty of care, or by violation of other provisions of the said Act or the articles of association of the company, have deliberately or negligently caused to the company while in office.

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\(^{10}\) The Office of Bankruptcy Ombudsman 24 January 2017.

The requirement to act with due care can be interpreted widely and thus it can be applied to various situations. The definition of due care shall be interpreted by comparing the actual actions taken to actions expected from a diligent person in an equivalent position. The concept of due care and the liability of the management has been specified through case law. It is typical that the liability issues are observed thoroughly in bankruptcy situations as it is in the interest of the bankruptcy estate as well as the creditors. The liability is mainly collective covering the board as a whole and can take place simply on the basis of participation in a specific board meeting. It is also typical that the liability of the CEO is wider than the board members owing to the CEO typically being better informed and having a greater ability to act when needed.

When insolvency is forthcoming or a possible scenario, the equity of the company often turns negative. This triggers the duty to register the loss of share capital. The same applies to publicly listed companies, in which case the obligation to make a register notification is triggered when the equity of the company is less than half of the share capital. The board is responsible for making the register notification. Neglecting the register notification is a violation of the Finnish Limited Companies Act and may lead to personal liability of board members.

The Finnish legislation does not include any obligation for a company to start insolvency proceedings. The company may continue loss-making business. However it is noted that if the equity has turned negative, the rules of the Criminal code of Finland\(^\text{12}\) of and the rules of the Act on Recovery to a Bankruptcy Estate\(^\text{13}\) shall apply. The board can also be seen to have caused the company damage if they did not apply for insolvency proceedings in time. The criminal aspect includes acts aiming to favour a creditor and dishonesty by a debtor. The main duties the directors of a distressed company have relate to the obligation to provide accurate information to all parties. This means that the board needs to be duly informed by the CEO and all the contracting parties will need to be aware of the financial situation of the company in order to be able to evaluate the risks involved. The board should take extra measures in order to confirm that the decisions are properly documented.

### Clawback actions

In Finland clawback actions are regulated in the Act on Recovery to a Bankruptcy Estate, and the Act is applicable to both bankruptcy and restructuring proceedings.\(^\text{14}\) Transactions made by the debtor prior to applying restructuring or bankruptcy proceedings may be subject to clawback if the transactions are harmful for the creditors.

The main and most commonly applied provisions are the general recovery provision (Section 5) and provision regarding the recovery of payment of a debt (Section 10). They are typically invoked together, but there are also cases that are based only on the general recovery provision.

According to Section 10, a payment of a debt carried out later than three months prior to applying the insolvency proceeding may be subject to clawback if the payment has been performed with unusual payment instruments or prematurely or with an amount that is considerable in relation to the assets of the debtor. An amount corresponding to around 10 per cent of the net assets of the estate is considered to be considerable. If the payment has

\(^{12}\) Criminal Code 19 December 1889/39.


been made to a person closely associated to the debtor, the time limit for clawback is two years. Clawback may be performed even if the transaction itself is valid and the creditor has acted in good faith.

The general recovery provision in Section 5 covers all kinds of transactions up to five years prior to applying of the insolvency proceedings. However, Section 5 is applicable only to inappropriate transactions that are made in order to evade the legal consequences of bankruptcy or restructuring. The prerequisite for applying this recovery provision is that the creditor has acted in bad faith.

In addition to the aforementioned clawback provisions, the Finnish Act on Recovery to a Bankruptcy Estate includes several specific provisions regarding for example, clawback of gifts, unreasonable benefits and collateral.

The clawback provisions are not applicable to customary transactions. Therefore, a transaction may not be recovered if it is, considering the specific circumstances of the case, an usual payment related to the ordinary business. In order to be subject to clawback, the transaction must be in deviation from previous practices and related to the future insolvency of the company.

A clawback claim may be made by a creditor or an administrator. A valid transaction made by the debtor is recovered, and the assets transferred in the transaction are returned to the bankrupt’s estate or, in restructuring proceedings, to the company. However, in restructuring proceeding if the claim for clawback is carried on solely by a creditor (without the support of the administrator), the assets are transferred directly to the creditor. If the transferred assets do not exist anymore, the creditor must compensate the value of the assets.

Clawback claims are common especially in bankruptcies in Finland. As the clawback regulations may be used to recover actions that without the insolvency proceedings would be considered valid, clawback claims are presented in almost every bankruptcy proceeding that does not lapse. The threshold in the presentation of evidence is considered to be fairly low.

III SIGNIFICANT TRANSACTIONS AND KEY DEVELOPMENTS

There have been no fundamental alterations to the insolvency legislation or legal praxis. One of the current hot topics is the bankruptcy estate’s liability for the waste caused by the bankrupt company as well as the environmental views regarding the role of, for example, the bankruptcy estate. The below sections concerning future developments include our views of the possible forthcoming reforms.

During the last years there have been problems regarding cost-effectiveness in the retail trade sector. The increasing global trend of online shopping is likely to be one major reason. As a result, we have seen some large-scale bankruptcies and restructuring proceedings in this field. The latest bankruptcy case was a company named Anttila, which was declared bankrupt in July 2016. At the time of bankruptcy the company had a chain of 28 department stores and during 2014 the company employed approximately 1,500 persons. It is argued that the company’s lack of both cost efficiency and specialisation together with the pressure caused by internet trade were the major reasons for the bankruptcy.

One of the latest major financial distresses in the retail trade sector was the restructuring of a chain of retail shops named Hong Kong Oy. The entity consisted of 25 warehouses. In January 2017 restructuring proceedings of Hong Kong Oy commenced. The same happened to a major retail chain named Seppälä Oy, which was granted restructuring proceedings in April 2017. At the time of the major financial difficulties the company had 78 stores, and
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according to the restructuring decision the company’s problems were caused mainly by too wide structure causing costs the business could not cover. The company intends to reduce the amount of stores to 39. Both Hong Kong Oy and Seppälä Oy sought restructuring proceedings only after their creditors had filed a petition for the bankruptcy.

Some smaller publicly listed companies (Talvivaara Mining Company Plc, Trainers’ House Oyj, Componenta Corporation) have entered into restructuring proceedings during the last few years. The reason for these companies’ insolvency differ. Talvivaara Mining Company Plc was a holding company whose daughter company entered into restructuring proceedings at the same time but entered into bankruptcy proceedings after a short time. Restructuring of a holding company with no business of its own and no valid holding business forced the company to undertake in the restructuring programme to bring new business to the company within a specific period. Talvivaara Mining Company Plc had the exceptionally low payment of 1 per cent approved by the court. Componenta Corporation has also acted as a holding company. One binding factor for the above-mentioned companies is conversion of receivables as a means of restructuring during the proceedings. The companies have either during the proceedings issued a convertible loan, the noteholders of which have the right to convert their receivables into shares or issued new shares to their restructuring creditors. There are no regulations on how such a conversion of receivables should be enforced but it has been accepted by the courts. There is now a working group to discuss whether a forced conversion could be added in the restructuring proceedings.

At the same time as Componenta Corporation filed an application for restructuring in Finland, one daughter company in Finland and several daughter companies in Sweden filed for restructuring and one daughter company filed for bankruptcy in the Netherlands. This is the most international Finnish insolvency case in the past few years.

IV RECENT AND FUTURE DEVELOPMENTS


The New Insolvency Regulation is directly applicable in Finland as well as in other member states of the EU (excluding Denmark), that is, it is in force without also being implement into national legislation. Finland is, however, currently preparing several amendments to the national insolvency Acts. The first amendments based on the New Insolvency Regulation came into force on 26 June 2018 and the rest of the suggested amendments are expected to enter into force during 2018.

The central matters in the New Insolvency Regulation are to regulate: (1) which member state is competent to commence insolvency proceedings; (2) which Member State’s jurisdiction is applicable; and (3) how the decisions of other Member States are recognised and implemented. In addition, the Regulation includes new provisions regarding insolvency registers and insolvency proceedings of groups of companies.

As a result of the national implementation measures, the current Finnish insolvency registers will be expanded and made available to the public via internet and the notice
procedures in insolvency proceedings will change. The amendments include also several practical matters (e.g., in future filing of claims in insolvency proceedings may also be carried out in English).

Another EU-based regulation that may later lead to amending the national insolvency Acts is the 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 (COM (2016) 723 final). This could have an impact *inter alia* on pre-pack proceedings, which are currently not regulated in Finnish legislation.

In addition to the aforementioned amendments based on EU law, the Finnish government has established a working group to examine the possibility of regulating the liability for environmental damages in the Act on Bankruptcy and to simplify the provisions of the said Act. The working group is currently preparing its suggestions and is expected to submit them in Autumn 2017.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

With a GDP growth of 1.1 per cent in 2016 (compared to 1.2 per cent in 2015, 0.2 per cent in 2014 and 0.3 per cent in 2013), restructuring and insolvency activity in France continued to decrease, broadly speaking, in 2016 compared to previous years. A total of 58,057\(^2\) insolvency proceedings (safeguard, rehabilitation and liquidation proceedings, see Section II, infra) were opened in 2016 (down 8 per cent compared with 2015). However, the bulk of these proceedings relates to very small enterprises as only 3,152 insolvency proceedings were opened for SMEs and bigger enterprises, a 9.8 per cent decrease compared with 2015.

In this context, the industries that have faced the most restructuring issues are the oil and gas sector, because of the continuing slump in energy and commodity prices, as well as the retail and tourism sectors (restaurants, carriers and hotels) because of sluggish household consumption, poor weather conditions and the geopolitical background (and, notably, the aftermath of the Paris terror attacks of November 2015 and July 2016).

As in 2015, restructuring and insolvency activity continued to witness a decrease of failing LBOs in 2016 (compared to the 2008–2010 and 2012–2014 rounds of restructuring). However, bankruptcy practitioners have dealt in 2016 with a surge in sizeable and complex out-of-court restructuring matters compared to the previous years.

In addition, 2016 saw the implementation of numerous total or partial sale plans in rehabilitation proceedings to transfer the business and assets of companies for which restructuring options were or proved impossible or that needed to scale down their operations (see Section IV, infra). Turnaround funds have also been very active in this period and participated in most of these court-monitored auctions.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

French bankruptcy law was extensively reformed in 2005 to promote reorganisation at a preventive stage and prompt creditors to take a more active role in pre-insolvency and insolvency proceedings, essentially through creating a safer environment for them to extend new credit facilities during both pre-insolvency and insolvency phases.

The major innovation was the creation of safeguard proceedings, which are intended to enable debtors that are in financial distress, but not yet insolvent, to reorganise and restructure under the court’s protection (essentially with a stay of enforcement actions,
subject to very few exceptions) and negotiate a consensual restructuring plan with creditors. French bankruptcy law has been regularly amended since 2005 and an ordinance dated 12 March 2014 (the 2014 Ordinance) recently reformed the bankruptcy law, with a view to favouring reorganisation at a preventive stage, strengthening the efficiency of out-of-court proceedings and increasing the rights of creditors in insolvency proceedings. In addition, a bill dated 6 August 2015 (the 2015 Bill) partially amended the French bankruptcy code and, in particular, introduced the possibility, under certain conditions, to squeeze-out the shareholders of a bankrupt company in rehabilitation proceedings. Bankruptcy law was also slightly reformed in 2016 so as to improve certain technical provisions regarding insolvency proceedings.

Two types of proceedings are available to distressed French companies (or foreign companies that have their centre of main interests (COMI) in France):

\[ a \] out-of-court proceedings: ad hoc proceedings and conciliation proceedings; and

\[ b \] court-monitored bankruptcy proceedings: safeguard (as well as pre-packaged safeguard proceedings), rehabilitation proceedings and liquidation proceedings.

The main provisions of each of these proceedings are set out below.

i Out-of-court proceedings

Ad hoc proceedings

Ad hoc proceedings are flexible, voluntary and confidential proceedings in which the president of the court appoints an agent to carry out appropriate tasks. In practice, these proceedings are used to organise informal negotiation between a company and its major creditors under the supervision of the court-agent.

Only the company’s legal representative can file a petition to the president of the court. It is usually considered that ad hoc proceedings are available to solvent companies only, but there have been some recent precedents where ad hoc proceedings were opened for insolvent companies (but for a very short period of time only). Major creditors are invited to consider debt rescheduling, cancellation and new money injection. In addition, the main shareholders can be invited to negotiate and potentially recapitalise the company. A debt-restructuring agreement accepted by some creditors cannot be imposed on other dissenting creditors, as the process is consensual and no cramdowns can be imposed. In practice, majority rules provided for in the existing credit documentation (loan, bond, etc.) apply.

In addition, the opening of ad hoc proceedings does not trigger any automatic stay. However, the debtor can apply for a moratorium (for a maximum of two years) if any creditor attempts to enforce its rights while ad hoc proceedings are pending. Under the 2014 Ordinance, ipso facto provisions are now deemed null and void in ad hoc proceedings: creditors are, therefore, prohibited from accelerating a loan, or terminating an ongoing contract, by the sole reason of the opening of ad hoc proceedings (or of any filing for that purpose). More generally, any contractual provision increasing the debtor’s obligations (or reducing its rights) by that sole same reason is also null and void.

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3 Please note that the French insolvency test is a pure cash-flow test (in contrast to a balance-sheet test) where a company is deemed insolvent when it is unable to meet its current debts out of its current assets (i.e., those in the form of cash or those that can be quickly turned into cash), taking into account undrawn committed facilities and other credit reserves and moratoriums or standstills accepted by creditors.
If an agreement is reached between a company and its creditors, the agent's duties end. If there is no solution to the company's financial difficulties and it later becomes insolvent then the only option is to initiate insolvency proceedings.

**Conciliation proceedings**

Conciliation proceedings are also flexible, voluntary and (to a certain extent) confidential proceedings that, under the supervision of a court-appointed agent, aim at facilitating negotiations between the company and its major creditors, and reaching a workout agreement that sets out the terms and conditions for the restructuring of the existing debt (waiver, rescheduling, etc.) and, if any, new loans extended by creditors or shareholders. Since the 2014 reform, the court-appointed agent may be entrusted with the mission to arrange a pre-packaged sale of a business in conciliation proceedings, the sale of which could ultimately be implemented in safeguard, rehabilitation or liquidation proceedings.

The debtor company must face legal, economic or financial difficulties (whether actual or foreseeable) so as to benefit from conciliation proceedings. Conciliation proceedings are available to solvent or insolvent companies provided they have been insolvent for less than 45 days before the petition is filed.

Conciliation proceedings are opened by the president of the court for a maximum period of four months, which can be extended to five months in total at the agent's request. The management must cooperate with the court-appointed agent and the major creditors to negotiate a solution to the company's difficulties. The court agent does not have any management responsibilities. There are no restrictions on business activities.

Trade creditors and major shareholders can also be invited to take part in the negotiations. Social and tax authorities can be asked to consent to a debt-rescheduling plan or a cancellation of debts. As in *ad hoc* proceedings, a restructuring workout accepted by some creditors cannot be imposed on other dissenting creditors in conciliation proceedings (subject to the opening of accelerated safeguard or accelerated financial safeguard). Majority rules provided for in the existing finance documentation will apply.

Even though the opening of conciliation does not trigger any automatic stay, the court can force any creditor that attempts to enforce its rights while conciliation is pending to accept a two-year maximum moratorium. As in *ad hoc* proceedings, creditors are prohibited from accelerating a loan, or terminating an ongoing contract, by the sole reason of the opening of *ad hoc* proceedings (or of any filing for that purpose). More generally, any contractual provision increasing the debtor's obligations (or reducing its rights) by that sole same reason is also null and void.

When an agreement is reached between the debtor and its creditors, the parties have two options:

- the debtor can request a formal court approval of the workout agreement. This is to encourage creditors to extend new credit facilities. Indeed, new money facilities granted in the framework of a court-approved workout benefit from a statutory priority of payment should the company subsequently file for insolvency. Except where fraud has taken place, a court-approved workout agreement is also protected from the risk of being voided in the future. However, this court approval must be recorded in a full judgment accessible to the public and, therefore, subject to challenge by a third party or appeal; or
- the parties can obtain a simple acknowledgment from the president of the court. This option does not involve publicity, but implies that the creditors, having granted new
money facilities in the framework of such conciliation proceedings, waive their right to priority of payment and, more generally, to protection against the risk of clawback in the future.

ii Court-monitored bankruptcy proceedings

Safeguard proceedings

Safeguard proceedings allow companies that, though still solvent, face difficulties that they cannot overcome, to be restructured at a preventive stage under the court’s supervision. Safeguard proceedings have three objectives in the following order of priority: (1) to allow the company’s business activities to be continued; (2) to preserve jobs; and (3) to repay creditors.

To open safeguard proceedings, the company must be solvent, but facing difficulties that cannot be overcome. In the Coeur Défense case, the Supreme Court held that no restriction should apply to the concept of ‘difficulty’ justifying the opening of a safeguard. In particular, to be granted the benefit of safeguard court protection, the debtor cannot be requested to characterise such difficulty as affecting its business activities. In that particular case, the Court ruled that the necessity for the debtor to renegotiate, in the case of an event of default, the terms and conditions of a loan may constitute a difficulty allowing such debtor to petition for safeguard proceedings. The 2016 reform specified that if it appears that the debtor’s difficulties could be overcome, the court must invite the debtor to request the opening of conciliation proceedings before ruling on the opening of safeguard proceedings.

If the company is insolvent or becomes insolvent after the opening of safeguard proceedings (that is, the company is unable to pay its due and payable liabilities arising post-filing), the court orders the proceedings to be converted into rehabilitation or liquidation proceedings.

Safeguard proceedings begin with an observation period of up to six months to assess the company’s financial position. This period can be extended once for six months, and in exceptional circumstances, can be further extended at the public prosecutor’s request for an additional six months. During this period, any decision that does not fall within the scope of day-to-day management must be approved by the bankruptcy judge. The bankruptcy judge must also approve any decision to settle pending disputes.

Once safeguard proceedings have been ordered by the court, there is an automatic stay of all creditor payment actions – subject to few exceptions (and notably claims secured by a security interest conferring a retention right, claims secured by a fiduciary agreement and set-off of related claims) – against the main debtor and individuals acting as guarantors and joint debtors, but not against companies acting as guarantors or joint debtors. Hence the need, when group companies are acting as guarantors, to have all of them, as well as the main debtor, placed under court protection.

Interest for loans with a duration of one year or more, or for contracts having a deferred payment of one year or more, will continue to accrue but cannot be paid cash when due, and will be restructured as part of the safeguard plan.

The general outcome of safeguard is the approval by the court of a safeguard plan that can involve debt restructuring, recapitalisation of the company, debt-for-equity swap, sale of assets and a partial sale of the business. The safeguard plan cannot include a proposal to sell the business as a whole.
For companies of a certain size (that is, companies with more than 150 employees or with an annual turnover of more than €20 million), three classes of creditors (two committees and one bondholder group) must be set up (this is optional for smaller businesses subject to court approval):

- **a** financial institutions, comprising all banking institutions, financial creditors (investment or hedge funds, etc.) that have purchased bank debt or trade claims, or creditors that have lent money to the debtor by way of a loan (this may include shareholders and shareholder loans);
- **b** major trade creditors (that is, trade creditors with more than 3 per cent of the total trade claims); and
- **c** bondholders (gathered into one single class, regardless of the currency or applicable law of the various bond indentures).

Each member of the creditor classes must inform the court-appointed administrator of the existence of any subordination agreement, agreement restricting or conditioning its vote and agreement allowing for third-party payment of the debt. The administrator must then submit a proposal for the computation of its voting rights to the relevant class member. If there is disagreement, the concerned class member can petition the president of the court through motion proceedings. To reinforce creditors’ role (so far reduced to making mere suggestions to the administrator), the 2014 Ordinance provides that any member of the committees (that is, financial institutions or major trade creditors, but not bondholders) can submit an alternative safeguard plan competing with the plan prepared by the debtor.

The plan is deemed approved by the classes if a two-thirds majority of the creditors (in value) in each class votes in favour of the plan. If the plan provides for a debt-equity swap (or any other operation requiring shareholder approval), shareholders must also be consulted and vote in favour of the plan at a two-thirds majority (no cramdown of shareholders is possible in safeguard). However, the 2014 Ordinance provides that the majority applicable to shareholder meetings convened on first notice can be reduced by court order to a simple majority of the shareholders present or represented, provided they represent at least 50 per cent of the voting shares. Social and tax authorities are not members of the classes; they are invited to negotiate and can grant a debt rescheduling or cancellation.

If classes of creditors are not set up, or if one of the classes rejected the draft plan, the plan must be negotiated on a one-to-one basis with each creditor. If the creditors consulted individually refuse to approve the draft plan prepared by the company, the court can impose a 10-year maximum term-out to dissenting creditors. However, this 10-year maximum term-out is without prejudice to any longer maturity date agreed in the original loan agreement. Consenting creditors benefit from the shorter maturity date (if any) that they would have negotiated. The court cannot impose any debt-to-equity swap or debt write-off of principal or interest claims in a term-out scenario. The yearly instalments under the term-out plan must not, after the third year following court approval of the plan, be less than 5 per cent of the total admitted pre-filing liabilities, except if the contract initially provides for a longer maturity date.

Once approved by the court, the safeguard plan is enforceable against all members of the creditors’ classes (financial institutions, trade creditors and bondholders), including the dissenting minority. Upon the approval of a safeguard plan, the court appoints an agent to supervise its implementation. If the company fails to meet its obligations under the plan and
becomes insolvent, the court must order the plan to be cancelled and initiate rehabilitation proceedings or, if the rescue of the company appears obviously impossible, liquidation proceedings.

**Pre-packaged safeguard proceedings**

Two types of pre-packaged safeguard proceedings are available: accelerated financial safeguard and accelerated safeguard. Their global purpose is to implement a quick, simple process that allows the speedy reorganisation of a distressed company. Pre-packaged safeguard proceedings are opened at the debtor’s request provided the following eligibility criteria are satisfied:

- the company must meet certain thresholds (number of employees, minimum turnover or balance sheet test, consolidated accounts);
- conciliation proceedings must be pending (direct access to pre-packaged safeguard proceedings is strictly prohibited);
- the company must be solvent (from a cash flow standpoint) or, as the case may be, must have been insolvent for less than 45 days when it applied for conciliation; and
- the company must have prepared a draft plan in conciliation likely to receive sufficient support from its creditors.

The opening of accelerated financial safeguard proceedings only has effects in relation to financial creditors and, as the case may be, bondholders (therefore, excluding trade creditors from the process). Financial institutions and, as the case may be, bondholders, must approve the restructuring plan at a two-thirds majority in each class. The accelerated financial safeguard process must be completed within one month, renewable once for a maximum of one month.

In accelerated safeguard proceedings, all pre-filing creditors are included in the process (including trade creditors). The class of financial institutions, the class of major trade creditors (and as the case may be, the class of bondholders) are invited to vote on the plan proposed by the company at a two-thirds majority in each class. The accelerated safeguard process must be completed within a maximum of three months from the date of the opening judgment.

If creditors refuse to approve the pre-packaged plan, the court closes the proceeding and, if the company becomes insolvent, orders the opening of rehabilitation or liquidation proceedings.

**Rehabilitation proceedings**

Rehabilitation proceedings are the appropriate remedy if the company is insolvent (from a cash flow standpoint) but rescue does not appear to be impossible. Any company must file for rehabilitation (or, as the case may be, liquidation if there is no prospect for recovery) no later than 45 days from the date on which it becomes insolvent (provided that conciliation proceedings are not pending).

The objectives of rehabilitation proceedings are the same as for safeguard proceedings. Rules applicable to the observation period, the automatic stay and classes of creditors are also the same as in safeguard (with some exceptions, notably regarding shareholder consent).

In rehabilitation proceedings, the court-appointed administrator can simply assist the management to make decisions or can be appointed to take control of the company’s management in whole or in part. Any decision that does not fall within the scope of day-to-day management must be approved by the bankruptcy judge. The bankruptcy judge must also approve any decision to settle pending disputes.
There are two main possible outcomes for rehabilitation proceedings: a rehabilitation plan, where the same principles apply as in a safeguard proceeding; and a sale plan, where unlike in safeguard, should the debtor prove unable to present a sustainable restructuring plan (as the case may be a term-out plan), the court can authorise the administrator to auction the business as a whole or in part. Creditors (except for limited exceptions, e.g., creditors benefiting from a retention right) have no say on the choice of the purchaser, which is made by the court when approving the sale plan. No credit bid is allowed (there are some precedents, but in exceptional circumstances, e.g., pure SPV with no employees and only one creditor benefiting from a security over the quasi-sole asset).

The 2014 Ordinance introduced a limited possibility to have a court-appointed agent vote at shareholder meetings which was amended in 2016: if the insolvent company’s net equity is not restored and the shareholders have refused to increase the company’s equity to at least half of its share value (which is a legal requirement in France), the administrator can petition the court to appoint an agent in charge of convening the shareholder meeting and to vote, on behalf on the dissenting shareholders, on the recapitalisation of the company for the amount suggested by the court-appointed administrator, when the draft plan provides for a change in the share capital in favour of one or several committed investors.

In addition, the 2015 Bill further introduced the possibility to squeeze out shareholders of a company under rehabilitation proceedings through a forced sale of all or part of the shares of the shareholders that have refused to implement the required change in the equity structure and that hold directly or indirectly a majority stake or a blocking minority stake in the capital of the company, or an imposed dilution of their equity stake. However, the application of this squeeze-out is limited to the following circumstances:

- the shareholders have refused to implement the change in the equity structure contemplated under the draft rehabilitation plan;
- the bankrupt company employs (directly or indirectly) 150 employees minimum;
- the disappearance of the company is likely to cause serious disturbance to the local economy and employment; and
- a share capital reorganisation is the only solution to allow business activities to continue (a partial or total sale of the company’s assets must be contemplated before allowing such squeeze-out).

Liquidation proceedings

Liquidation is the appropriate remedy when the company is insolvent and its rehabilitation appears to be impossible. The aim is to liquidate a company by selling its business, as a whole or by branch of activity, or by selling its assets one by one. Liquidation is the only possible outcome when a rehabilitation is attempted without success. Creditors are, as far as possible, repaid according to their rank and privilege out of the proceeds of the sale of the company’s business or assets.

Liquidation proceedings trigger an automatic stay of proceedings against the company. All pre-filing creditors are barred from enforcing their rights to seek payment from the debtor, subject to some exceptions (the same as those applicable in safeguard and in rehabilitation). In a liquidation (unlike a safeguard or in rehabilitation), secured creditors benefiting from a pledge can also enforce their security interest through a court-monitored allocation process, that is, request the court to be transferred ownership of the pledged assets.
Liquidation proceedings last until the liquidator finds that no more proceeds can be expected from the sale of the company’s business or assets. After two years (calculated from the judgment ordering liquidation), any creditor can request the court to order the liquidator to wind up liquidation proceedings.

There is a simplified form of liquidation proceedings available for small businesses, which lasts for a maximum of one year.

iii Selected topics

Directors’ liability

Liability can arise in liquidation proceedings where, as a result of management errors (other than mere negligence), a company’s assets do not cover its debts: an action for mismanagement, which only applies in liquidation proceedings, can lead to an insolvent company’s management being liable for all or part of its debts. This liability can extend to formally appointed directors or managers with representation powers, and to any individual or entity that is not officially a director or manager but that has repeatedly influenced the company’s management or strategic decisions (that is, shadow (de facto) directors or managers).

A parent company can also be held liable for an insolvent subsidiary’s debts if it has been appointed as a director or is deemed a shadow director or manager of that subsidiary (e.g., through an individual appointed at the shareholders’ request).

The liquidator or the prosecutor can initiate the action. In addition, the majority of the supervising creditors (which would have been appointed by the court to assist the liquidator) can summon the liquidator to bring an action or commence proceedings on their own initiative if the liquidator does not do so after such summoning.

Directors found liable for certain specific breaches can be (independent of any liability action or criminal prosecution based on the same facts) forced to assign their equity interest in the company and prohibited from managing any business for up to 15 years, and holding any public office for up to five years.

Breaches include:

a using the company’s assets or credit for their own benefit, or the benefit of another corporate entity in which they have a direct or indirect interest;

b using the company to conduct and conceal business transactions for their own benefit;

c carrying out business activities at a loss to further their own interests, knowing that this would lead to the company’s insolvency;

d fraudulently embezzling or concealing all or part of the company’s assets; and

e fraudulently increasing the company’s debts.

Clawback

In rehabilitation or liquidation only (but not in safeguard proceedings), any transaction entered into during the hardening period (including transactions entered into with members of the same corporate family) can be subject to clawback provisions. The hardening period runs from the date when the company is deemed insolvent, and can be backdated by the court by up to 18 months before the insolvency judgment. If rehabilitation or liquidation proceedings are preceded by a pre-bankruptcy conciliation workout, the insolvency date cannot be backdated to a date before the court order approving the workout agreement.

The following transactions are automatically void (that is, the court must declare these transactions void on petition by the administrator, the liquidator or the public prosecutor) if performed during the hardening period:
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a any deed entered into without consideration transferring title to moveable or immovable property;

b any bilateral contract in which the debtor’s obligations significantly exceed those of the other party;

c any payment by whatever means, made for debts that have not fallen due on the date when payment is made;

d all payments for outstanding debts, if not made by cash settlement or wire transfers, remittance of negotiable instruments, or daily assignment of receivables or any other means commonly used in business transactions;

e deposits or consignments of money made under Article 2350 of the Civil Code (governing pledges over certain intangible assets, including claims) in the absence of a final judgment;

f any mortgage or pledge (both contractually agreed or court-ordered) granted to secure a pre-existing debt;

g any protective measure, unless this measure gave rise to a recordation or registration before the date of insolvency;

h any granting, exercise or reselling of stock options made under Article L225-177 et seq of the Commercial Code;

i any transfers of moveables or assignment of rights into a trust estate, unless this transfer or assignment occurred as a guarantee of a debt concurrently undertaken;

j any amendment to a trust agreement affecting the rights and moveables already assigned or transferred to a trust estate as a guarantee of debts undertaken prior to such amendment; and

k any declaration of non-seizability filed by the debtor, under Article L526-1 of the Commercial Code. A declaration of non-seizability can be cancelled if made during the six months preceding the insolvency date.

Any payment made or any transaction entered into during the hardening period is also subject to optional voidance (that is, subject to the court’s discretionary decision on petition by the administrator, the liquidator or the public prosecutor) if proper evidence is brought before the court that, at the time of the payment or transaction, the contracting party knew the company’s insolvency. When dealing with intra-group transactions, this knowledge is presumed for companies belonging to the same corporate group. Third-party rights, including bona fide third parties, can be affected by those voidance provisions.

III RECENT LEGAL DEVELOPMENTS

The 2014 Ordinance (applicable to pre-insolvency and insolvency proceedings since 1 July 2014) reformed the French bankruptcy law, with a view to favouring reorganisation at a preventive stage, strengthening the efficiency of out-of-court proceedings and increasing the rights of creditors in insolvency proceedings.

One of the main features of the 2014 reform was the introduction of pre-packaged sale plan, namely, the possibility for the court-appointed agent to prepare a partial or total sale of the business in conciliation proceedings, the sale of which will ultimately be implemented in safeguard, rehabilitation or liquidation. The major purpose of such procedure is to shorten the period during which the company is under bankruptcy proceedings so as to preserve the value of the business transferred. The first pre-packaged sale plan was implemented in
June 2015 when the business and assets of NextiraOne, a spin-off of Alcatel-Lucent, were transferred (alongside all of its 1,400 employees) to a purchaser only one month after the opening of rehabilitation proceedings. Later in 2015, the business and assets of Fram, a French tour operator, were also transferred through a pre-packaged sale plan.

The 2014 Ordinance also introduced a limited possibility to have a court-appointed agent vote at shareholder meetings if the insolvent company’s net equity is not restored. However, some practitioners considered that in this respect, the 2014 reform missed its initial purpose, which was to allow a squeeze-out of shareholders through forced sale of their shares or forced dilution of their equity stake. Even though the enforcement of a debt-equity swap against dissenting shareholders when the equity has lost all value and conversion of debt is the only solution to preserve the business as a going concern is viewed as essential by most practitioners, squeeze-out provisions were not adopted in 2014, as they could be assimilated into the creation of a new right to ‘expropriate’. This created constitutional law issues, which needed further review. The 2015 Bill sought to address this issue and provided for a limited squeeze-out of the shareholders in rehabilitation proceedings (see Section II, supra). However, such squeeze-out remains untested to our knowledge.

In addition, the 2015 Bill also purported to enhance the restructuring of ‘large’ companies and group companies through: the creation of specialised commercial courts having jurisdiction to supervise insolvency proceedings opened against companies of a certain size or that feature multi-jurisdictional aspects; the extension of the jurisdiction of the same commercial court to group’s subsidiaries or affiliates of a company under insolvency proceedings; and the obligation for the court, under certain conditions, to appoint at least two administrators and two creditors’ representatives.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

As described above, the most active sectors in 2016 were the retail, oil and gas, and tourism sectors. Although there has been a decrease in the number of insolvency proceedings in 2016, there were still quite a few active situations on the restructuring market with a surge in the number of sizeable situations in the third quarter of 2016, many of them being listed companies.

The most significant French insolvency cases of 2016 were the sale plans of Cauval (bedding manufacturer), Pixmania (online retailer), Viadeo (online professional network services), Bata (shoe retailer) and SNCM, the ferry operator between Corsica and continental France.

With respect to out-of-court and pre-packaged proceedings, the major situations of 2016 were the restructuring of Foraco (drilling services) and Vivarte (apparel retailer) as well as the consensual debt-equity swap of Camaïeu (apparel retailer). The creditors of Solocal (directories) also implemented a debt-equity swap through a change in its accelerated financial safeguard plan. The end of 2016 also witnessed the commencement of certain significant cases, such as CGG (geophysics services) and Financière Turenne Lafayette, the holding entity of several food-processing companies, including William Saurin.
V INTERNATIONAL

France has not adopted legislation based on the UNCITRAL Model Law on Cross-Border Insolvency. The recognition and enforceability of insolvency proceedings commenced in another jurisdiction depends on whether such jurisdiction is party to a treaty with France. As such, Regulation (EC) 1346/2000 on insolvency proceedings (the Insolvency Regulation) allows insolvency procedures in different EU Member States to be automatically recognised. Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (Recast) reforming the Regulation 1346/2000 only applies to insolvency proceedings to be commenced after 26 June 2017.

If a company’s COMI is in France, the main proceedings can be commenced before the French courts under the Insolvency Regulation. A company’s COMI is presumed to be the place of its registered office unless it is proven that its COMI, as defined in the Eurofood decision of the European Court of Justice (case C-341/04, Eurofood IFSC Ltd), is in a country other than its place of incorporation, and that the company’s trade and financial partners are fully aware that the COMI of such company is not its place of incorporation.

Secondary proceedings can subsequently be commenced to liquidate an establishment’s assets located in another EU Member State. Secondary proceedings under the Insolvency Regulation are also appropriate if a company has an establishment in France, but its COMI is in another EU Member State.

In the Mansford case (Court of Appeals of Paris, 25 February 2010), several Luxembourg holding companies filed for safeguard in France on the grounds that their COMI was in France. In early 2010, the Paris Court of Appeals, applying the rationale of the Eurofood decision, held that French courts had jurisdiction over the matter for the following reasons:

a. all management and other meetings were held either in Paris or locally where the real estate assets were located;
b. the companies had no assets or activities other than a property asset and a letting activity in France (no Luxembourg activity whatsoever);
c. the two holding companies’ sole purpose was to hold 100 per cent of their 10 subsidiaries (themselves carrying no activity in Luxembourg);
d. the ultimate parent company’s sole purpose was to own 100 per cent of holding companies that had no activity in Luxembourg; and
e. the relationship with the lenders was initiated in France and the renegotiation of the financing documentation took place in France.

If the Insolvency Regulation does not apply and insolvency judgments are made in a jurisdiction that does not have a treaty with France, they are not automatically recognised. Foreign judgments can only be enforced if they have been subject to an inter partes procedure known as *exequatur*, which is intended to verify that the foreign court had proper jurisdiction, international public policy has been complied with and no fraud has taken place. Such *exequatur* process usually takes a couple of months, excluding appeal, which could lengthen the process.

VI FUTURE DEVELOPMENTS

French bankruptcy law was reformed in 2014, 2015 and 2016, and there is no pending legislation to further reform the French Bankruptcy Code.

The current focus of the recent reforms relates to civil law and employment law and it is yet to be seen how any of these measures would potentially impact the French restructuring practice.
Chapter 11

GERMANY

Christian Bärenz and Anne Bach

I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

i Liquidity and state of the financial markets (May 2017)

Lending in the eurozone remained cheap in 2016/2017. After lowering the central rate of interest to 0.00 per cent in March 2016 the Governing Council of the European Central Bank (ECB) decided on 27 April 2017 that the interest rates will remain unchanged at 0.00 per cent at least until the end of 2017. In addition, the ECB confirmed that net asset purchases at a new monthly pace of €60 billion are intended to run until the end of December 2017 or beyond, if necessary, to supply capital markets with more liquidity (‘quantitative easing’). In doing so, the ECB buys the bonds from commercial banks, which in turn lend the money on in credit form to companies and consumers. The ECB is even considering increasing the programme in terms of size or duration, if the outlook becomes less favourable or if financial conditions become inconsistent with further progress towards a sustained adjustment in the path of inflation.

This monetary policy has led to the negative effect that interest rates for depositors continue to fall. While in the past, short-term borrowing by the government temporarily brought negative interest rates to a stop, it is unlikely that negative interest rates will continue to be a rarity. Some banks have already started to designate negative interest rates for their business clients.

The low-to-negative deposit rate as well as other factors, such as the weak euro exchange rates, improved economic data and the outcome of the French presidential elections generally perceived as market and Europe-friendly, led to investors bringing cash to the capital markets: the historic height of the German stock market, which reached 12,000 points in March 2015, has now again been reached, first in February 2017, and again in May 2017.

ii Impact of specific regional and global events (May 2017)

According to experts, Germany’s economy is enjoying above-average health. Neither the euro crisis, nor the tense situation in relation to the refugee crisis, has stopped the growth of the German economy. After a year of stagnancy in 2013, the GDP in Germany grew by up to 1.6 per cent in 2014, 2.1 per cent in 2015 and 1.9 per cent in 2016. Growth forecasts for 2017 are outlined as follows: the German Federal Bank anticipates growth of up to 1.8 per
cent, the Institute for Economic Research, one of Germany’s largest economic think tanks, forecasts a growth of 1.4 per cent, and the RWI, a leading non-profit research institution, forecasts economic growth of 1.5 per cent.

High demand for German goods, reduced costs for energy and significantly reduced export costs, resulting from a weak euro, have led to Germany obtaining a top-ranked export surplus of €253 billion in 2016. In comparison with 2015, the export rate in 2016 increased by 2 per cent.

In the past three years, developments in the job market have been increasingly positive. In April 2015, the unemployment rate stood at 6.5 per cent (this equals 2.84 million people without a job). In April 2016, the unemployment rate decreased to a new record low of 6.3 per cent (2.74 million people), only to decrease to, again, a new record low of 5.8 per cent (2.57 million people) in April 2017, the lowest unemployment rate in 25 years. According to expert opinions, the increase of refugee immigration will have no significant (negative) impact on the German job market: the Institute for Economic Research forecasts a further decline of unemployment for 2017/2018 resulting in possibly only 2.37 million people being unemployed by 2018.

As a result of the rising economy, in 2016 the German mergers and acquisitions market experienced excellent growth. The number and volume of most transactions with German participation on the buy-side or sell-side amounted to US$200 billion (2015: US$116 billion, 2014: US$224 billion), where more than half of the value (about US$118 billion) was attributable to the second quarter of 2016.

iii Market trends in restructuring procedures and techniques employed during this period

It can be observed that in almost all large insolvency proceedings the debtor applies either for debtor-in-possession-proceedings or for the ‘protective shield procedure’ (see Section II.iii, infra). A number of these proceedings have been successful, and therefore it is not too optimistic to say that both instruments have been tested and proven.

Since the new Debt Securities Act became effective in 2009, a large number of successful bond restructurings have been carried out. The 2009 Debt Securities Act allows the debtor to restructure its bonds in an out-of-court proceeding, subject to certain requirements (see Section II.iii, infra).

Avoiding insolvency proceedings remains an important objective in almost every restructuring strategy. Whether through consensual negotiations, out-of-court trusteeships or bond restructuring, if a financial restructuring can avoid formal insolvency proceedings, most of the stakeholders would subscribe to such a strategy to avoid both the stigma and uncertainty connected with formal insolvency proceedings.

iv Statistics

The number of insolvencies peaked after the financial crisis in 2008. In 2009, 32,687 companies had to file for insolvency at German insolvency courts. After this peak year, the number of insolvencies has consistently decreased. After 2015, where the number of company insolvencies fell by 4 per cent from a total of 24,085 to 23,123 compared to 2014, the
number of insolvencies has again decreased in 2016 by another 6.9 per cent (compared to 2015) resulting in a total of 21,518 companies. This is the seventh decline in a row, and the lowest number since 1995.²

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

German insolvency law provides for a single gateway into formal insolvency and rescue procedures. Regardless of whether it is intended that the debtor company be dissolved and liquidated, or that a formal arrangement with creditors be concluded, the commencement of formal insolvency proceedings always follows the same rules. These rules are governed by the German Insolvency Code of 1999, which was reformed by the Law for the Further Facilitation of the Restructuring of Enterprises (ESUG) in March 2012 and by the Law for the Improvement of Legal Certainty with regard to Clawback Actions pursuant to the German Insolvency Code and the German Avoidance of Transactions Act in April 2017.

i Objectives of insolvency proceedings

Overall, German insolvency law is creditor-friendly. Section 1 of the Insolvency Code states that insolvency proceedings serve the purpose of collective satisfaction of a debtor’s creditors by liquidating the debtor’s assets and by distributing the proceeds. The statement that the collective satisfaction of a debtor’s creditors can also be reached by way of an insolvency plan, particularly in order to maintain the enterprise, has been included recently.

In sum, insolvency proceedings serve the purpose of maximising returns for creditors. Other objectives, such as the protection of jobs (however desirable this may be), are subordinated to the creditors’ financial interests. If the liquidation of a business is more beneficial for the creditors than its continuation, the insolvency administrator is obliged to opt for liquidation. However, an emphasis on rescue and rehabilitation (i.e., the continuation of the debtor’s business) exists to the extent that in most scenarios, the continuation of a business results in a higher return for creditors than liquidation does. In practice, it is often observed that (smaller) insolvency courts and certain insolvency administrators tend to pay greater attention to the protection of jobs.

ii Preliminary insolvency proceedings

Debtors and creditors both have the right to file an insolvency petition with the competent insolvency court. During the interim proceedings, the insolvency court must secure the assets of the debtor and determine whether the debtor is legally insolvent. To achieve this, the court usually appoints a preliminary administrator. The powers of the preliminary administrator are subject to the discretion of the insolvency court. Typically, the power to manage the business remains with the management of the debtor. However, the consent of the interim administrator is required for any dispositions over assets (a ‘weak preliminary administrator’). Depending on the circumstances, the court can also vest the power to dispose over the debtor’s assets with the preliminary administrator (a ‘strong preliminary administrator’). Furthermore, the court can, and usually will, order a moratorium to prevent creditors from enforcing their claims.

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² All data from Destatis, the German Federal Statistical Office, available at: www.destatis.de.
The preliminary insolvency proceedings are a crucial stage of the proceedings. This is often the time at which decisions must be taken as to whether and to what extent the business is continued or wound up. The preliminary administrator will negotiate the financing of the business with management and the main creditors. If there is no potential to continue the business (e.g., because of a lack of financial resources), it will be ceased immediately and the employees will be made redundant. However, if the administrator thinks that an investor can be found during the course of the proceedings, and that the business can be continued without incurring substantial losses, the decision will likely be made to keep the business going. If the business is continued during the preliminary proceedings, it is possible to finance the salaries and wages of the employees of the debtor business by way of government funds, for a period of up to three months.

The preliminary administrator – on behalf of the court – must establish whether the debtor is insolvent within the meaning of the Insolvency Code. The Insolvency Code sets out three tests for insolvency:

1. Illiquidity (this is a ‘cash-flow test’, i.e., the company is unable to meet its liabilities as these become due);
2. Over-indebtedness (this is a ‘balance-sheet test’, meaning that the company’s assets are worth less than its liabilities); and
3. Imminent illiquidity, which occurs where it is foreseeable that a company will become illiquid in the future.

Creditors and debtors may file a petition asserting illiquidity and over-indebtedness. Only the debtor is entitled to file a petition asserting imminent illiquidity. The balance sheet test was amended on 17 October 2008 by the Act to Stabilise the Financial Markets. The new test relaxes the rules on over-indebtedness. Now, a company shall not be deemed to be over-indebted where the value of its assets is worth less than its liabilities, provided that the continuation of the business is predominantly likely (‘positive going concern’). The last test is fulfilled if, under the specific circumstances, continuation is more likely than the cessation of the business.

The new balance sheet test was originally limited until the end of 2010 and was extended until 31 December 2013. Meanwhile, the term-limitation of the test has been abandoned, and it applies without limitation.

If the preliminary administrator establishes that the company is insolvent and that the costs of the proceedings can be covered from the proceeds of the debtor’s estate, the administrator will recommend to the court that final insolvency proceedings be commenced. Upon such commencement, the court will appoint an insolvency administrator. In practice (but not necessarily), this will be the same person as the preliminary administrator.

Under the new insolvency law, which is aimed at expanding creditor participation in insolvency proceedings, the provisional creditors’ committee can influence the selection of the insolvency administrator. According to Section 22a of the Insolvency Code, the insolvency court has to appoint a provisional creditors’ committee if the debtor satisfied two of the following three criteria in the previous business year:

1. Total assets of €4.84 million following the deduction of losses reported on the asset side of the balance sheet within the meaning of Section 268, Paragraph 3 of the German Commercial Code;
b a minimum of €9.68 million in sales revenues during the 12 months prior to the balance sheet date; or
c at least 50 employees on an annual average.

In addition, a preliminary creditors’ committee shall be appointed at the request of the debtor, the preliminary insolvency administrator or a creditor, provided that at the same time, the persons who may be considered for membership in the provisional creditors’ committee are named and the declarations of consent of the persons named are enclosed with the request.

The power to dispose over the debtor’s assets is vested with the administrator. The court will also set a date for the first creditors’ meeting and will invite creditors to file their claims with the administrator. Further, the creditors must inform the administrator of any potential security interests that these creditors claim to possess with regard to any assets of the insolvent debtor’s estate. Another effect of the commencement of (preliminary) insolvency proceedings is a comprehensive moratorium that prevents any further enforcement of claims.

If the company is not insolvent, or – far more relevantly – where the costs of the proceedings are not covered, the court will terminate the insolvency proceedings, and creditors are again free to enforce their claims against the company.

iii Insolvency proceedings, insolvency plan and debtor-in-possession procedures

After the commencement of insolvency proceedings, the insolvency administrator will realise the value of the estate. As noted above, the administrator has a duty to obtain the best financial result for the creditors. To achieve this, the administrator has various options. Depending on the circumstances, the business can be sold as a going concern in parts or as a whole, or the assets can be sold piecemeal.

Insolvency plan

A further option is the implementation of an insolvency plan.

The insolvency plan aims for the reorganisation of the debtor and seeks to enable the business to continue as a going concern under the court’s supervision. The proceedings can result in the outcome that the business is restructured and continues as the same legal entity, or that the business is sold and the proceeds are distributed among the creditors.

One of the most important principles of the insolvency plan is that the creditors are divided into different classes depending on how they are affected by the plan. Contrary to ordinary insolvency proceedings, it is possible to deviate from the principle that all of the creditors must be treated equally. Provided that all of the creditors of the same class are treated equally, different classes of creditors can be treated differently. Subject to the consent of the respective class, it is even possible to modify the rights of preferred creditors.

Until March 2012, there was a strict division between company and insolvency law in Germany. Shareholder resolutions had to be passed by the shareholders according to company law rules. The implementation of reorganisation measures, therefore, required shareholder consent. The ESUG led to a fundamental change. Since the reform, it is possible for the provisions of an insolvency plan to encroach upon original shareholder rights. Matters that were formerly exclusively the subject of shareholder resolutions can now be incorporated into the insolvency plan, and the resolution can be replaced by the adoption and confirmation of the plan. Furthermore, the insolvency plan may provide that the creditors’ claims may be
converted into share rights or membership rights in the debtor (‘debt-equity swap’). In this context, the plan may provide for a decrease or increase in capital, contributions in kind, the exclusion of subscription rights or the payment of compensation to outgoing shareholders.

The insolvency plan is subject to the approval of the creditors’ meeting. Such approval initially requires consent by the majority of all creditors of each class attending, and secondly, by the majority of the total amount of existing claims. However, the plan is not automatically rejected if not all classes grant their consent. The Insolvency Code provides that dissenting classes may be crammed down, provided the dissenting classes participate appropriately in the proceeds. In addition, the plan may not prefer creditors of the same rank over the dissenting creditor, and the dissenting creditor must not be worse off than in liquidation.

If the creditors’ meeting has granted its consent, the insolvency plan is submitted to the court for approval. The court will only withhold such approval if the content of the plan or the procedure violates the provisions of the Insolvency Code. Furthermore, the court shall refuse the approval at request of a creditor or if the debtor is not a natural person, a person with a participating interest in the debtor, if:

a) the person filing the request opposed the plan at the latest in the voting meeting; and

b) this person is likely to be placed at a disadvantage by the plan compared with the situation without a plan.

To avoid delays, the ESUG implemented Section 251, Paragraph 3 of the Insolvency Code, which sets out that the request shall be rejected if the plan provides for funds to be made available in the event that a party concerned shows to the satisfaction of the court that it will be placed at a disadvantage (i.e., to compensate that party).

Upon the approval of the court, the plan becomes binding upon the parties involved. These include dissenting creditors, and even creditors who have not filed their claims and consequently have not voted on the plan. An appeal against the order approving the insolvency plan is only admissible if the party filing the appeal has objected to the plan by or during the voting meeting, has voted against the plan, and has shown that it will be placed at a significant disadvantage as a result of the plan (in comparison to without it) and that such disadvantage cannot be compensated for by the above-mentioned funds.

After the approval of the insolvency plan has become final, the formal insolvency proceedings are terminated. The plan may provide that its implementation is supervised by a custodian. Supervision is ceased upon fulfilment of the terms agreed to in the plan.

If the plan fails and not all claims are fulfilled according to the plan, all claims are revived in full; the moratorium comes to an end, and waivers and other agreements are no longer binding. Creditors are therefore free to enforce their claims against the debtor, although this will likely result in another insolvency.

Self-administration (debtor-in-possession)

Another procedure introduced with the Insolvency Code in 1999, and subsequently strengthened by the ESUG, is ‘self-administration’, consisting of a debtor-in-possession procedure. Self-administration allows the management of the debtor to continue carrying on business under the supervision of a custodian. Self-administration can be used provided it does not delay the proceedings and where it does not disadvantage the creditors. During self-administration, the debtor retains the power to dispose over its assets. The custodian must continually monitor the economic situation of the debtor and supervise the management. While under the old insolvency law regime self-administration was, in practice, only ordered
after insolvency proceedings were formally opened and preliminary self-administrators were the rare exception, practice has changed. Section 270a of the Insolvency Code now states that the court shall order preliminary self-administration if the debtor’s request for debtor-in-possession management does not manifestly lack the prospect of success.

The Insolvency Code allocates responsibilities and authority among the debtor, the custodian and the creditors. The most important are:

- **a** transactions that are of particular significance for the insolvency proceedings generally require the consent of the creditors’ committee or the creditors’ meeting;
- **b** in ordinary insolvency proceedings, the insolvency administrator would be entitled to decide whether or not to fulfil contractual obligations; in self-administration scenarios, the debtor is vested with the same right; and
- **c** the custodian has the power to set aside transactions occurring prior to insolvency. Further, creditors are obliged to file their claims against the debtor with the custodian. The debtor pays the proceeds to the creditors based on the claims registered.

Self-administration is often combined with an insolvency plan.

In practice, self-administration is becoming more and more established. According to estimates, in large insolvency proceedings, more than 75 per cent of the debtors apply for self-administration.

**Preparations for reorganisation**

To facilitate the preparation of a pre-packaged insolvency plan, provisions for the preparations for reorganisation (Section 270b of the Insolvency Code) were newly incorporated into the German Insolvency Code. The (informal, but better known) name for the proceeding is the ‘protective shield procedure’.

The protective shield procedure is a restructuring instrument that permits the debtor to prepare an insolvency plan within a maximum of three months. During this period, the debtor acts independently and without any enforcement measures being implemented. This does not mean that creditors are suspended from accelerating their claims, but compulsory and enforcement measures are excluded.

First of all, the procedure requires that the debtor has requested debtor-in-possession management. The requirements for such management must be met. Furthermore, the protective shield procedure can apply only if the request for the commencement of insolvency proceedings is based on imminent insolvency or over-indebtedness. There is no opportunity for a protective shield procedure if the company is illiquid at the moment of filing. Secondly, the restructuring cannot clearly be futile. Both requirements have to be proven by providing a certificate prepared by a tax adviser, accountant or lawyer with experience in insolvency matters or a person with comparable qualifications. The occurrence of illiquidity during the protective shield procedure does not lead to an automatic termination of the procedure, but the court must be informed of the illiquidity.

For the period during which the insolvency plan is being prepared, the court appoints a provisional custodian who supervises the debtor’s management and who informs the court as well as the creditors if the creditors’ position appears to be prejudiced. Other than in a ‘normal’ self-administration, it is the debtor who has the right to propose a person as a provisional custodian, as long as he or she is not the same person issuing the certification mentioned above. The court is only allowed to deviate from the debtor’s proposal if the proposed person is manifestly unsuitable for the office, which in practice is very seldom.
Informal methods of restructuring companies

It is possible to enter into a settlement agreement with creditors (creditors’ arrangement) at any time. However, the lack of a moratorium is the major problem arising in informal restructuring scenarios. It is, therefore, absolutely crucial that all, or at least the main, creditors agree on a stay of enforcement. Further, the various parties must actually have an incentive to participate in an out-of-court restructuring. If creditors refuse to take part for whatever reason, the informal approach runs a high risk of failure.

A trusteeship aiming at an out-of-court restructuring can be an effective tool to dispose of the business, or parts of it, and repay the debtor’s liabilities (or parts of these). The main advantage for the lenders is to avoid locking-up equity (which is often underwater) and to have more control over the disposal process.

Bond restructuring in a nutshell

Until 2009, bond restructuring played only a minor role in Germany. Only a very limited number of bond restructurings were undertaken, since the scope of the old Debt Securities Act of 1899 was very limited. The previous Debt Securities Act only applied to bonds issued by a company having its seat or a permanent establishment in Germany, and it did not cover the frequently occurring case of bonds issued by subsidiaries – usually located in the Netherlands – that were backed by a guarantee from the German parent company. Furthermore, lack of flexibility and predictability were major disadvantages.

To make German bond restructuring more competitive with other legal regimes and to bring it into line with modern international standards, Germany adopted the new Debt Securities Act of 2009, which came into force on 5 August 2009. The Act covers all bonds issued under German law on or after 5 August 2009.

Under the 2009 Debt Securities Act, the bond terms can be amended by a majority resolution of creditors if and to the extent that the bond terms provide for such modification. Impending insolvency – or even grounds for insolvency – is, on the other hand, not necessary for the 2009 Debt Securities Act to apply.

The 2009 Debt Securities Act lists examples of restructuring measures; this list is not, however, exhaustive, and the extension of the term of a corporate bond, modification of interest rates, a change in the principal amount and subordination are possible. In addition, the conversion of bonds into shares in the company or an exchange for such shares is possible if the bondholders adopt a resolution to that effect. This applies accordingly to the exchange and release of security. It should also be pointed out that the right of bondholders to declare an event of default may be eliminated or restricted.

Resolutions must be adopted at a meeting of bondholders and, if material amendments are made, a majority of at least 75 per cent of the votes cast is required.

A quorum is deemed to be obtained at the meeting of bondholders, if at the first meeting at least 50 per cent of the voting rights are represented, or where at a (subordinate) second meeting, at least 25 per cent of the voting rights are represented (the issuer cannot vote if it itself holds bonds). It is therefore possible to achieve a modification of the major terms and conditions of a bond with as little as 18.75 per cent of all voting rights.

According to the 2009 Debt Securities Act, a joint representative can be appointed who has the right to summon bondholder meetings, manage the passing of resolutions, obtain information from the issuer and assert the claims of bondholders in the issuer's insolvency.
Such a joint representative usually assumes a very important stakeholder role in any related restructuring, not because of the representative’s legal power, but because the representative manages and facilitates (inter-creditor) communication.

**The taking and enforcement of security**

Security interests held by creditors are generally not affected by insolvency proceedings. The Insolvency Code distinguishes between the right of separation of assets and the right of separate satisfaction. Where a creditor has rights *in rem* to assets and these rights have not been assigned to the creditor as security (in particular, rights regarding retention of title), these assets do not form part of the insolvency estate, and the assets to which these attach may be physically repossessed by the creditor. If a creditor has a registered security interest in real property (land charge or mortgage), the creditor can enforce its claim outside of insolvency proceedings according to the Act Governing Auctions and Sequestration. The creditor may either appoint an agent to sequester and distribute rental income from the property, or it may sell the property by way of auction and collect the proceeds. Further, creditors secured by a pledge over an asset belonging to the estate, or creditors to whom the debtor has assigned personal property or rights as security, are entitled to the proceeds that the administrator realises in the respective sale of such assets or rights. In this case, an all-in fee for the enforcement is charged. Security granted shortly before the commencement of insolvency proceedings can often be set aside by the administrator.

**Duties of directors of companies in financial difficulties**

Directors of insolvent companies are obliged to comply with a number of duties. The most important duty is to file for insolvency without undue delay after the company has become insolvent (i.e., the company is either illiquid or over-indebted). The law provides for a very short restructuring period of up to three weeks. The directors may defer the application for up to three weeks, but only if realistic rescue prospects exist within this time frame. If it becomes clear that the restructuring cannot be achieved within this time frame, the directors must file for insolvency immediately. A breach of this filing duty results in civil as well as criminal personal liability. The directors will be obliged to compensate the company and creditors who suffer a loss caused by the failure of the directors to file a petition in time. During these three weeks, the directors are only entitled to make payments that are essential for keeping the business going.

If the company is ‘merely’ imminently illiquid, the directors are entitled to file for insolvency, but they are not subject to a duty to file.

Even more duties exist for directors if the company is not (yet) insolvent, but in a financial crisis. The general rule is that managing directors are required to exercise the diligence expected of a prudent businessperson in their conduct of the company’s affairs. In a company crisis, this includes the duty to consider all remedial actions and, as far as possible, to initiate such measures. Special rules apply, *inter alia*, to cash pooling and the treatment of shareholder loans. Summing up, the continuation of business in a crisis can give rise to considerable risks for directors. In particular, the continuation of business in a group of companies is very difficult to manage.

**Clawback actions**

To ensure that all creditors are treated equally, the administrator has the power to set aside transactions that took place prior to the insolvency proceedings. All of the respective
provisions under German law with respect to avoidance actions require that the transaction
the administrator seeks to set aside must be disadvantageous for the creditors. Hence, if the
debtor receives consideration of equal value for the payment made within a short time frame,
the transaction does not disadvantage creditors (because of the rather sophisticated case law,
many pitfalls remain). Further, most avoidance and ‘clawback’ provisions require both that
the debtor is insolvent at the time the transaction was entered into and that the creditor
is aware of the insolvency. The relevant time periods for avoidance or clawback provisions
depend on the nature of the transaction the administrator seeks to set aside. The most relevant
period is the three-month period prior to the insolvency application. However, the maximum
period is 10 years (under specific circumstances).

In the context of the reform of German corporate law in 2008, the wording of Section
135 of the Insolvency Code was amended. Section 135 of the Insolvency Code governs the
clawback of transactions in which shareholder loans are repaid (such loans are subordinated
in insolvency proceedings). In the past, the loan had to be an equity-replacing shareholder
loan; now, any shareholder loan repayment can be set aside.

On 4 April 2017, the Law for the Improvement of Legal Certainty with regard to
Clawback Actions pursuant to the German Insolvency Code and the German Avoidance of
Transactions Act came into force. The law seeks to enhance legal certainty and to prevent
extraordinary clawback claims from being brought. The main changes include a restatement
of Section 133, Paragraph 1 of the German Insolvency Code, which allows prior transactions
intentionally prejudicing creditors to be set aside within a look-back period of 10 years.
Because of various court decisions on the application of Section 133, Paragraph 1 of the
Insolvency Code, many commercial transactions bore disproportionate and unpredictable
risks, especially because the clawback period of 10 years is the longest clawback period in the
entire German Insolvency Code. The law now states that transactions that grant security or
provide for the satisfaction of the counterparty can only be set aside within a period of four
years (Section 133, Paragraph 2 German Insolvency Code). Also, a transaction is protected
from clawback action if fair market values have been exchanged and if the creditor was not
aware of any dishonest motives the debtor had when performing the transaction (Section 142,
Paragraph 1 German Insolvency Code), the latter having been added to improve protection
of creditors (mostly suppliers). In addition, it also has been explicitly clarified that employee
remuneration is protected from any clawback action where the payment of remuneration has
occurred within three months (Section 142, Paragraph 2 German Insolvency Code).

If no formal insolvency proceedings are commenced, creditors may be entitled to
claw back certain transactions that diminished the debtor’s assets, resulting in that creditor’s
disadvantage, pursuant to the German Avoidance of Transactions Act. These rules are
similar in principle to the insolvency avoidance provisions and are also covered by the
above-mentioned reform.

Restructuring of banks and other financial institutions

On 1 January 2015, the Act for the Recovery and Resolution of Credit Institutions (SAG)
came into force. This Act is based on the Directive on the Recovery and Resolution of Credit
Institutions 2014/59/EU (BRRD) of the European Parliament and of the Council for
establishing a framework for the recovery and resolution of credit institutions and investment
firms, and it aims to manage imbalances of institutions in the future without compromising
financial stability and making use of tax funds. One of the most important improvements
of the SAG is shareholder and creditor participation in an institution’s damages liability and
managing costs. Furthermore, there is now a duty to prepare a recovery plan. There are also new provisions on group internal financial support, and on cross-border cooperation between national regulatory and liquidation authorities.

III RECENT LEGAL DEVELOPMENTS

On 13 April 2017, the German parliament passed the Law for the Facilitation of Group Insolvency Proceedings, which will come into force as of 21 April 2018. The reform does not conceptually deviate from the respective approach at EU level: the law introduces provisions strictly focused on procedural law regarding German members of a group of companies becoming insolvent. Under existing German insolvency law, each legal entity of a corporate group has to file for insolvency separately. This may lead to different venues and to the appointment of different insolvency administrators for each entity. This legal concept remains unchanged, but the law aims at improving the effectiveness and coordination of individual insolvency proceedings opened for each single entity by providing for:

\[
\begin{align*}
a & \quad \text{a group venue;} \\
b & \quad \text{the possibility of appointing the same person as (group) insolvency administrator or receiver; and} \\
c & \quad \text{the initiation of group coordination proceedings, which may include the appointment of a group coordinator and the development of a group coordination plan aiming at the overall restructuring of the group.}
\end{align*}
\]

In addition, insolvency courts, creditor committees and appointed insolvency receivers are obliged to coordinate and to exchange information on a group level.

The newly introduced provisions may prove useful, especially with respect to the group venue and the group coordination plan in prepared restructurings. However, given the lack of enforceable rights of the group coordinator, there appears to be little leeway in cases in which other insolvency administrators or receivers are not willing to support a joint effort.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

Although the number of business failures in recent years and to date in 2017 is at its lowest level in 20 years, there have still been numerous significant insolvency proceedings and restructurings.

The renewable energy sector remains under pressure. Increased competition, open markets and the amendment of the Renewable Energies Act have led to a wave of insolvencies in the wind energy sector; for example, Prokon, Windwärts and Windreich.

This has also affected companies in the solar panel industry, such as Sunways (which had filed for insolvency in 2013, but the proceeding was not commenced because of a creditor agreement), SAG Solarstrom and Solon (which already passed through an insolvency proceeding in 2012) and Rena. There have also been a number of out-of-court restructurings. The most famous of these is probably Solarworld, which reduced its debts by more than €500 million through an out-of-court debt-to-debt and debt-equity swap. Despite this out-of-court restructuring, Solarworld recently had to file for formal insolvency
proceedings in May 2017. In September 2016, KTG Energie, specialised in the operation of biogas plants, filed for debtor-in-possession proceedings and was, together with 21 of its subsidiaries, restructured through an insolvency plan.

The shipping industry also continues to be distressed. For many years, closed-end ship funds generated profitable yields. Since the financial crisis in 2008, however, cargo rates have fallen significantly, and as a result, more than 340 ship funds have had to file for insolvency.

In the fashion sector, the market-listed fashion retailer Steilmann had to file for regular insolvency proceedings in March 2016. Meanwhile, numerous subsidiaries followed. Furthermore, Zero, a German fashion company with about 1,000 employees, filed for insolvency in April 2016 and St. Emile, a German luxury fashion label, followed in October 2016. Also, Butler’s, a well-known German home furnisher with more than 1,000 employees and more than 100 stores in Germany, Austria and Switzerland had to file for insolvency in March 2017.

The automotive industry will most likely face substantial restructurings soon due to the anticipated transition from internal combustion engines to hybrid or electric solutions. For the time being, restructurings in the automotive industry remains scarce in Germany and are generally related to international insolvency or restructuring cases, such as the global restructuring of the Japanese supplier TAKATA following the worldwide largest recall in automotive industry due to defective airbag modules or the AMTEK crisis, which resulted in insolvency filings of its German automotive subsidiaries REGE Holding and Küppers Group.

Finally, the restructuring of Heta Asset Resolution AG, an Austrian ‘bad bank’ and former Hypo Alpe Adria group, kept German courts busy; German creditors, owning the vast majority of its €12 billion in debt instruments, had challenged before German courts the first intended wind-up under the BRRD. A first-instance decision by the Munich Regional Court declined to recognise the legal effects of a moratorium imposed by Austria’s Financial Market Authority. In May 2016, a large creditor group entered into a MoU with Austria to provide for an out-of-court settlement, which was successfully closed in October 2016. As part of this out-of-court settlement, creditors agreed to withdraw their lawsuits.

V INTERNATIONAL

Reform of the European Insolvency Regulation

In December 2012, the European Commission adopted a proposal to amend the current European Insolvency Regulation (EIR). The amendments will apply to insolvency proceedings opened after 26 June 2017. The EIR establishes common rules on the court competent to commence insolvency proceedings, the applicable law and the recognition of the court’s decision when a debtor becomes insolvent. The rules apply to cross-border insolvency proceedings within the European Union (but not in Denmark).

With regard to group insolvencies the amended EIR limits itself to imposing cooperation and communication duties instead of substantive rules. In addition, in group insolvency situations it is now possible to apply for ‘coordination proceedings’. Coordination proceedings require that the national law provides for such a proceeding. Furthermore, the amended EIR provides a clarification of the definition of the ‘centre of main interest’, which is one of the key connecting factors in European insolvency law, and has caused many practical doubts in the past. The new rules now contain safeguards against ‘abusive forum
shopping’. The new EIR provisions also lead to a renewal of the rules for secondary insolvency proceedings. Specific situations now exist where a court can adjourn or refuse a request to open secondary insolvency proceedings.

ii EC proposal for a directive on preventive restructuring frameworks


The directive contains provisions in the area of substantive insolvency law, which are subdivided into three main topics:

a  ‘preventive restructuring procedures’;

b  discharge for entrepreneurs; and

c  measures to increase the efficiency of insolvency procedures in general.

The purpose of the preventive restructuring procedures is to enable enterprises to restructure at an early stage and to avoid insolvency. Whereas the German legal framework already provides for such early-stage initiation of insolvency proceedings if the debtor is over-indebted or faces imminent illiquidity, the EC Proposal seems to provide for no serious entry test as a ‘likelihood of insolvency’ is considered sufficient for the initiation of such preventive restructuring proceedings. For this and other reasons it is expected that the implementation of the EC Proposal will lead to extensive changes in German insolvency law. Besides it is discussed how the implementation of the EC Proposal could be harmonised with existing duties of directors, especially with regard to filing obligations (see Section II, supra).

VI FUTURE DEVELOPMENTS

After the German general election in 2009, the parties that formed the coalition government announced a reform of insolvency law in their coalition agreement. The reform was split into three steps. The first step contained the implementation of the ESUG in order to make a contribution toward the continuation of potential recoverable companies. The second step included the reform of consumer insolvency and the discharge of residual debt. Both reforms have led to the implementation of corresponding provisions in the German Insolvency Code. The third and last step was related to the introduction of a group insolvency law and has been implemented as of April 2017 (see Section III, supra).

Besides this three-step-plan, the German legislator originally did not plan to implement further changes to the insolvency-related legal framework any time soon. This view, however, has been challenged by the recently published EC Proposal on preventive restructuring proceedings (see Section V, supra) as its implementation into German law will most likely require adjustments to fundamental principles of German insolvency law, i.e., the obligation to file for insolvency proceedings under certain circumstances, creditor and minority shareholder protection, mandatory court involvement, etc. The idea to strengthen restructurings, however, is generally supported. As the EC proposal as such has mainly been perceived as flawed, inefficient and technically inappropriate to achieve the objectives pursued by the EC, future discussions on the implementation of the EC Proposal are likely to cause lively debates.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

Liquidity and state of the financial markets

In 2016 Greece made a significant economic adjustment, which was a result of extensive fiscal consolidation and implementation of reforms. In 2016, the GDP amounted to €314.89 billion, the gross public debt amounted to 178.9 per cent of its GDP and there was a surplus of 0.7 per cent. Growth was at 0.3 per cent, while it is expected to reach 2.7 per cent in 2017. On the negative side, the enormous sacrifices and the internal devaluation had a strong impact on society, thus impairing poverty and unemployment rates, which reached 35.7 per cent and 23.06 per cent accordingly. Projections for 2017 provide that Greece’s GDP shall reach €318.6 billion and the gross public debt shall amount to 174.8 per cent of its GDP, while unemployment rate shall decrease to 21.3 per cent and inflation shall increase from zero per cent to 1.2 per cent.

Key reforms include improving of fiscal figures, restoration of the banking sector’s growth, through reduction of non-performing loans and debt restructurings, introduction of collective dismissals, opening-up of closed professions and boosting of investment and privatizations. There is a debate between European institutions and the International Monetary Fund (IMF) as to whether the Greek debt is sustainable. On one hand, a majority of the European institutions claim that the debt is sustainable and there only needs to be some technical readjustments of the loan agreements. On the other hand, the IMF reiterates the need for a debt relief, which will be complemented with strong policy implementation in order to restore growth and sustainability. Nonetheless, European institutions are reluctant to proceed with a second debt haircut, partly because of the Treaty of the Functioning of the European Union (no bailout clause) and partly because this would demonstrate a special and favourable handling of the Greek debt, in comparison with the handling of other Member States’ debts.

Moreover, the banking sector is on a close watch, as the three recapitalizations and the ongoing liquidity support from the European Central Bank and the Bank of Greece have not been enough to enforce their financial performance. Following issuance of a legal framework on the establishment and operation of credit servicing firms by the executive committee of

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1 Dorotheos Samoladas is a partner and Christina Kalogeropoulou is an associate at Sarantitis Law Firm.
3 Article 125 of the TFEU.
4 Executive Committee Act 118/19.05.2017 ‘Framework of establishment and operation of credit servicing firms (Law 4354/2015) – Replacement of Executive Committee Act 95/27.5.2016’.
the Bank of Greece, Banks have become very active on taking measures to handle NPLs as well as NPEs, such as implementing internal procedures or outsourcing such services to third parties. This activity can also be attributed to the recent legislation that releases managers, directors and any other person entrusted with the management of a banking institution's estate from any liability arising therefrom within the scope of a restructuring, rehabilitation, special administration procedure or haircut of debts and claims. Finally, provision of financial support has also been relatively low, making it thus very hard, if not highly unlikely, for small and medium-sized enterprises (SMEs), which dominate the Greek economy, to gain access to financial help from the banks. An exception to this practice is lately noticed within the scope of a restructuring procedure, in which case the banks rely upon a well drafted business plan and are more willing to proceed with a refinancing of the existing debts, especially in view of the preferential ranking of claims arising from such agreements.

ii Impact of specific regional or global events

Undoubtedly, 'Brexit' (after the referendum in United Kingdom regarding its membership in the European Union) has created new conditions. While it is very hard to quantify the exact consequences, both political and financial, of this event, no one can claim that this will be an easy path for either side. A first estimation is that Brexit will have a great impact on immigration, as the United Kingdom shall be able to restrict immigration from Europe, depending on their future relationship. It is likely that Britain will restrict the number of low skilled workers entering the country and will focus more on highly skilled workers. In any case, Britain will design specific and probably strict migration requirements that will affect Greece, as many highly skilled Greek workers have moved to UK. On the other hand, this could be a good outcome for Greece as they will contribute their know-how and thus, help Greece increase its competitiveness.

Among others, trade and manufacturing as well as financial services will be affected, since Britain will be considered a third country and thus, tariffs shall be imposed on imports and exports. Regarding financial services, Britain may also lose its 'passporting rights', which currently allow UK-based institutions to provide services to the European Union without having a branch in another Member State. The loss of such rights may lead UK-based banks to establish a subsidiary in the European Union in order to process business there regardless of the fact that such work may be essentially done in London. Such outcome could also be positive for Greece and its maritime economy, as many shipowners cooperate with British banks and could lead to an increased presence of British banks and bank services on Greek territory.

Despite Brexit and contrary to what many analysts and journalists had reported, the Netherlands was not another domino that fell to populism and the staunchly anti-Islam, anti-EU and anti-immigration PVV party of Geert Wilders lost the elections. The same happened in the French presidential elections, in which Emmanuel Macron and his party, who are seeking EU reform as well as deeper European integration in the form of a eurozone budget and eurozone finance ministers, won, thus keeping alive the European dream. While many were afraid that Europe would crack under the test of all the upcoming European elections, it seems that anti-populism and sanity make slow but steady victories. It is likely

5 Article 65 Paragraph 2 of Law 4472/2017.
that this will also happen in the German elections. It goes without saying that all these political events do affect Greece, both in terms of its membership and role in the European Union and the handling of the Greek debt.

Apart from the economic recession, Greece is struggling under the weight of what is perhaps in its recent history the largest refugee crisis in scale. Greece has become a country of entry and transit for hundreds of thousands of refugees from the Middle East. It is estimated that 1.03 million people have entered Greece since 2015, of which at least 57,000 are stranded in Greece after the closure of the borders on March 2016. Consequently, Greece is also grappling with a huge number of asylum applications and an ineffective immigrant detention system, both of which entail high administrative costs and expenditures that Greece cannot afford. The refugee crisis has had a deleterious effect upon the political environment and has raised questions about how the refugees will be integrated into society, public schools and the public health system. Undoubtedly, this will be a substantial budgetary cost for Greece, which is difficult to address due to fiscal and budgetary adjustments.

### iii Market trends in restructuring procedures and techniques

A large number of medium-sized companies proceed with informal and out-of-court restructuring following a mutually agreed business recovery scheme with the banks, under which the banks have become involved or take over the debtor’s management and look for a potential investor. This is heavily applied to outward-looking companies that have increased exports activity, such as those of the aquaculture industry, or those that have good potential to remain sustainable and regain their profitability because of their financial contribution to the Greek market, such as companies in the food industry (mainly supermarkets). Small companies usually apply for a formal restructuring procedure, which is typically a longer and costlier process.

Although the competent authorities do not regularly issue a report regarding the insolvency statistics, the Hellenic Statistical Authority recently published some figures referring only to the bankruptcy procedure and for the period of 2004–2014. According to these statistics, the average number of companies that applied for a bankruptcy procedure each year during the said period, amounts to 1,061. Of these petitions, 914 (86 per cent) were accepted and 457 bankruptcies were declared. Moreover, of these statistics, 42 per cent concerns sole proprietorships, 11 per cent partnerships and 47 per cent entities limited by shares. The most bankruptcies have been recorded in the industry of retail and wholesale (45.7 per cent), the industry of manufacturing (22.8 per cent), the hotel and food services industry (11.6 per cent) and infrastructure industry (5 per cent).

Unfortunately, there are no formal reports regarding the number and course of bankruptcy applications. It is estimated that the time required to resolve insolvency cases is three-and-a-half years, and the recovery rate is 35.6 per cent. More than 16,000 SMEs closed in 2015, while 229,000 SMEs closed within the period 2008–2014. In 2016, only 28,250 businesses were registered and 33,606 were deregistered, of which the majority were sole proprietorships, creating the first negative result (-5,356) since 2012.

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iv Formal procedures entered into or exited
In general, the recent amendments of the Bankruptcy Code create three keystone frameworks, for its further modernisation, which are explained in Section III, *infra*, and can be summarised as follows:

- **a** enhancement of the restructuring procedures of entities in order to maximize their value to creditors, employees and the society in general;
- **b** enhancement of the procedures available to debtors and creditors in order to enable an efficient restructuring of viable entities or an expedited insolvency proceeding for non-viable entities;
- **c** provision of rules that enable an honest entrepreneur to try a fresh restart, especially when he or she could not succeed despite his or her good faith efforts;
- **d** introduction of additional procedure to enable a swift debt settlement process under specific conditions and
- **e** introduction of a more elaborated legal framework for the sale and management of NPLs and NPEs.

Regarding the formal procedures exited, it should be noted that the (once more) reformed Bankruptcy Code has abolished the process of initiating a restructuring procedure with an initial period, during which the debtor and his or her creditors would negotiate with the participations of a mediator, in order to reach a compromise agreement. This abolishment emerged from the fact that many debtors fraudulently and tediously initiated this process, in order to secure suspension of enforcement, but in reality, had no intent to reach a compromise agreement with their creditors. Thus, the restructuring procedure is now effectuated only with a pre-pack deal, namely an advance compromise agreement that is submitted before the court, for its ratification, together with the petition for the opening of the process.

Moreover, the new Bankruptcy Code has abolished the special liquidation procedure, as its practice had been very limited. The explanatory report of the new law provides two reasons for the abolishment of the special liquidation procedure; the first refers to the existence of a very similar process, which is the special administration procedure of Law 4307/2014 and the second refers to its nature, namely the fact that it addressed very specific needs and thus, it was subject to continuous amendments that are not congruent with the objectives of a codified Bankruptcy Code.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Legal entities
Greece has greatly focused on corporate insolvency law since 2007. The Bankruptcy Code has been updated many times since then, in reflection of the financial challenges faced by Greek corporations. Bankruptcy proceedings can be initiated by or against a merchant, either as an individual or as a legal entity. Corporate Insolvency law in Greece (Law 3588/2007)\(^9\) is structured in three main pillars: (1) voluntary liquidation; (2) involuntary liquidation; and (3) the restructuring procedure.

Voluntary liquidation

Voluntary liquidation is commenced by the entity itself, through its board of directors or a relevant management body. A legal entity must file a bankruptcy petition\(^\text{10}\) within 30 days following present cessation of payments, in a general and permanent way. Moreover, the Code provides that voluntary liquidation can be filed, anytime, in case of imminent cessation of payments or possibility of insolvency.\(^\text{11}\) A general and permanent inability of the legal entity to satisfy monetary obligations as they become due and payable may be present or imminent; essentially, a foreseeable result of illiquidity. In any case, present or imminent inability or possibility of insolvency, as the case may be, must exist at the time of the filing of the bankruptcy petition. Regardless of the existence of any of the aforementioned criteria, bankruptcy will not be declared if the court, based on the financial data submitted, believes that the assets of the entity cannot cover the bankruptcy’s expenses.\(^\text{12}\)

Once the court declares the legal entity bankrupt, the entity is placed in receivership. For this, the court appoints an insolvency practitioner (syndic or bankruptcy trustee) to start the liquidation proceedings and manage the legal entity’s assets and liabilities. The court may also appoint the legal entity’s management body (debtor in possession), which shall manage its assets and liabilities, along with the insolvency practitioner, and until the union of the creditors, granted that such appointment is in the interests of the creditors. The court, moreover, designates the date\(^\text{13}\) and place whereby the creditors shall convene before the judge rapporteur\(^\text{14}\) to discuss about the debtor’s financial condition and sustainability, the reasons for bankruptcy, the perspectives to maintain the debtor’s business and to file a reorganisation plan, as well as the probable outcome for the satisfaction of creditors. The court, finally, designates the date\(^\text{15}\) that the present cessation of payments occurred, which cannot be more than two years prior to the date of declaration of bankruptcy and in case of imminent cessation or probability of insolvency is the date of publication of the bankruptcy’s declaration.

The declaration of bankruptcy has the following significant results:

\(a\) the acknowledgment of the entity’s assets that exist at the time of filing the bankruptcy petition as ‘non-exempt’ property that is required for liquidation purposes;
\(b\) any claims not due at that time become immediately payable; and
\(c\) the suspension of all individual enforcement actions and proceedings, either future or existing, against the entity and its legal representatives.

The entity may file a reorganisation plan, in the case of present or imminent cessation of payments, but if insolvency is probable then the entity is obliged to file a reorganisation plan

\(^{10}\) According to the new Paragraph 4 of Article 5 of the Bankruptcy Code, the debtor must also submit his or her financial statements, if they exist, for the last available fiscal year as well as certificates witnessing the amounts of his or her debts, issued by the state.

\(^{11}\) This criterion was recently added, by virtue of Article 1 Paragraph 1 of Law 4446/2016.

\(^{12}\) Initially, the existence of assets that could cover the bankruptcy’s expenses constituted a negative condition, namely a reason for the court to reject the respective petition. Now, according to Article 1 Paragraph 1 of Law 4446/2016 it has become a positive condition to accept the petition, thus expediting the procedure and rendering it more efficient.

\(^{13}\) The date of the meeting shall take place within four months from the declaration of bankruptcy.

\(^{14}\) Judge rapporteur means the judge that is in charge of a particular case, incumbent to present the insolvency case before the general meeting of the court.

\(^{15}\) As amended by virtue of Article 1 Paragraph 7 of Law 4446/2016.
along with its bankruptcy petition, or within three months from its declaration of bankruptcy. The creditors, who represent 60 per cent of the total claims, including 40 per cent of secured creditors, may also file a reorganisation plan in case of permanent cessation of payments. The reorganisation plan must provide information regarding the corporation’s financial situation, a description of the current or future measures to be taken to secure satisfaction of creditors, and the creditors’ rights and legal status. Moreover, it may be subject to modifications and may now include provisions on the sale of the entire or part of the business. Similarly, to the restructuring procedure, the special mandator (appointed by the court in such cases) is entitled to substitute shareholders or stakeholders that deny their presence or vote for decisions that are required under the reorganisation plan applies here.

Finally, the court proceeds with a pre-review of the reorganisation plan within 20 days from its submission and if it is not rejected, either for typical or substantive reasons, it is subjected to the creditors’ approval within two months from the court’s order. Approval of the reorganisation plan requires a majority of 60 per cent of the total claims, which include 40 per cent of secured creditors. Then the reorganisation plan is ratified by the court and has a cramdown effect, thus binding all creditors, regardless of their participation or consent.

Involuntary liquidation

Involuntary liquidation is commenced either by any creditor with a relevant legitimate interest in case of present cessation of payments, or by the prosecutor for reasons of public interest (very rare in practice). The time and procedure of filing are the same as those of the voluntary liquidation. Moreover, creditors who represent 60 per cent of the total claims, which include 40 per cent of secured creditors may also file a reorganisation plan along with the bankruptcy petition. Following the pre-review of the plan by the court and before the commencement of the voting by the creditors, the entity (debtor) must approve the plan. Any objections raised by the entity do not prevent ratification by the court, if the court believes that the plan will not impair the legal status of the entity.

Restructuring procedure

The restructuring procedure is a pre-bankruptcy procedure that aims to restart and ‘rescue’ an entity’s going concern, while safeguarding creditors’ best interests. An entity in cessation of payments or approaching the imminent cessation of payments, or even probable insolvency (estimated as such by the court), may submit for ratification before the court a creditors’ compromise agreement (pre-pack deal), which must be approved at least by the supermajority (60 per cent) of the creditors, including 40 per cent of secured creditors. The procedure of initiating a restructuring, during which the debtor and his or her creditors would reach a compromise agreement has been abolished, in order to avoid fraudulent actions by the debtors.

The new Bankruptcy Code provides that from the date of the pre-pack deal submission until the issuance of the court’s decision, all enforcement actions against the entity are automatically suspended for a maximum period of four months. Such automatic suspension can occur only once for each debtor. Nonetheless, the court may accept any further provisional measures, following a respective petition by any person with legal interest in the case. An innovative provision of the new Bankruptcy Code states that both automatic suspension

16 Article 99 of the Bankruptcy Code.
and any further provisional measures may take place even before submission of the creditors’ compromise agreement for ratification if: (1) the petitioner produces a written declaration signed by creditors, representing at least 20 per cent of the total claims; and (2) the conditions of an emergency or imminent danger of the parties are met. Such measures shall be in force until the submission of the pre-pack deal and in any case for four months from the court’s respective order. It is noted that no extension of such measures can be ordered.

Until now, only the debtor could submit a pre-pack deal. The new Bankruptcy Code provides that creditors may also submit a pre-pack deal, without the debtor’s consent, if: (1) such deal is executed by the supermajority (60 per cent) of the creditors, including 40 per cent of secured creditors; and (2) the debtor is under present cessation of payments. In this case, the creditors must also file a petition for bankruptcy.

Regarding the conditions for the ratification of the restructuring plan, the court may ratify the restructuring plan regardless of the entity’s sustainability thereafter if it concludes that the following conditions have been met cumulatively:

- a. the restructuring plan includes an explicit statement that all participating creditors have agreed to its content;
- b. the restructuring plan includes a detailed analysis of the participants’ identity (creditors or not) and their claims, as well as clear reference to those claims whose enforcement may be affected by the restructuring plan; and
- c. the restructuring plan along with the business plan is disclosed to all non-participant creditors whose claims may be affected by the restructuring plan.

Furthermore, the new Bankruptcy Code introduced a new role for the special mandator. The court could also appoint a special mandator, who is responsible for certain actions, the safeguard of the debtor’s property etc. Currently, in the case of a pre-pack deal, due to present cessation of payments, the special mandator appointed by virtue of the ratification decision, is entitled to substitute any shareholder or stakeholder in the respective meetings, if such shareholder or stakeholder: (1) denies his or her participation or vote for the approval of actions required under the pre-pack deal either after its submission or as condition precedent; and (2) it is probable that he or she shall not participate in the liquidation proceeds. The special mandator shall exercise the aforementioned rights granted that the shareholder’s declared abstention or negative voting impairs the quorum and majority percentages. The same right (along with its limitations) applies in all other cases of a pre-pack deal ratification, if abstention or negative voting by the shareholder or stakeholder is a result of abusive behaviour.

**Special administration procedure**

Special administration procedure is provided under Law 4307/2014. It is mainly a ‘weapon’ for creditors to take-over the business of their debtor in order to sell the entire business or its assets and satisfy their claims with the proceeds. So far, only three entities have been subjected to special administration. In fact, any entity in cessation of payments or in case of a company, which meets, for two consecutive fiscal years, any of the conditions for judicial dissolution, under Article 48 Paragraph 1 of Codified Law 2190/1920 can fall under the special

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17 Under Article 48 Paragraph 1 of Codified Law 2190/1920: ‘The company can be dissolved by a court decision following a petition of any person with legitimate interest if: (a) at the incorporation of the company the share capital which should have been paid has not been paid either totally or partially in
administration procedure, following a petition of its creditors, including a credit institution, representing at least 40 per cent of the total claims. The petition must also be accompanied with a declaration by the proposed special administrator, accepting his appointment.

The special administrator has 12 months to complete the process, unless at least 90 per cent of the total assets have been sold and the special administrator thinks that based on the announcement of claims, the proceeds suffice for their entire satisfaction, in which case he may request for an extension. Otherwise, the special administrator must file for a bankruptcy petition.

It should be noted that in light of the abolishment of the special liquidation procedure, the special administration is the only similar alternative and thus, it should be reformed in a way that expands its scope and serves more efficiently its objectives.

Special administration under the Code of Civil Procedure

The Code of Civil Procedure provides that the court may impose a special administration upon the real estate property or even the business of the debtor, following a creditor’s petition. Such an order is issued only if the creditor’s claim is judicially verified and thus, the creditor has obtained a respective decision allowing him or her to enforce his or her claim against the debtor.

It should be mentioned that this procedure is not acknowledged as an insolvency or liquidation procedure, but as an alternative means granted to the creditor to satisfy his or her monetary claim. These provisions are not largely regulated, and thus, initiation of such procedure is not widely recorded. It appears that special administration is more applicable to very small businesses or merchant individuals. Nonetheless, in 201318 a large construction company was the first-ever debtor to be placed under special administration, following the respective petition of a minority creditor. As the court explained in its headnotes, courts may not impose a special administration upon a real estate property or business of the debtor if, among others, there are compelling reasons for not doing so. Compelling reasons are those that render the special administration unprofitable, that the business’s operation and success is closely related to the personal reputation and contribution of its managers or partners, or that the business’s operation falls within the provisions regarding the protection of trade secrets.

ii Insurance companies

On 5 February 2016, the Greek legislator abolished all the provisions19 that applied to insurance companies, by virtue of Law 4364/2016 (the Law). The Law is in compliance with Directive 2009/138/EC, regarding the undertaking and operation of insurance and reinsurance companies.

18 Decision No. 5461/2014 of the Single Member Court of Appeals of Athens.
19 The old provision is the Legislative Decree 400/1970, as amended by the Presidential Decree 332/2003.
According to the Law, such companies are required, as an integrated part of their business strategy, to maintain tools to proceed with a regular practice of assessing their overall solvency needs. The results of each assessment should be reported to the supervisory authority, which is the Bank of Greece.

The new provisions aim to create a trustworthy environment and minimise unexpected liquidations of insurance companies that have severe financial and social results. In this respect, Article 235 of the Law provides that insurance companies are not subject to the rules of bankruptcy or pre-bankruptcy proceedings. As such, the Bank of Greece is the only competent authority to decide on the revocation of its licence as well as on the restructuring measures for an insurance company, including the rise of capital, mandatory transfer of portfolio, suspension of payments to third parties etc., as well as on the winding-up proceedings following the suspension of their licence.

In the case of winding-up, the priority of claims is as follows: (1) employees’ claims arising from employment contracts and employment relationships; (2) claims of the state arising from due taxes; (3) pension funds claims; and (4) claims on assets subject to rights in rem.

### iii Credit institutions

According to the new rules on credit institutions, Article 145 Paragraph 1(a) of Law 4261/2014 provides that, subject to the specific provisions of Law 3458/2006 on Restructuring and Liquidation of Credit Institutions, such undertakings are not subject to the rules of bankruptcy or pre-bankruptcy proceedings.

To this extent, Law 3458/2006 provides for a special liquidation procedure that may be voluntary or involuntary. In any case, if the Bank of Greece suspends the licence of a credit institution, then such undertaking is immediately placed under involuntary liquidation.

### iv Investment services companies

There are a number of laws applying to investment companies, depending on their nature and the investment services provided. Thus, Law 3606/2007 applies to investment services firms and investment intermediation firms, Law 3371/2005 applies to portfolio investment companies, Law 2367/1995 applies to closed-end investment companies, Law 2778/1999 applies to real-estate investment companies and real-estate mutual funds, Law 2992/2002 applies to venture capital funds, Law 4367/1995 applies to venture capital companies, Law 4099/2012 applies to undertakings for collective investment in transferable securities (UCITS) and their managers and Law 4209/2013 applies to alternative investment funds and their managers.

In general, investment companies can be declared bankrupt, subject to explicit provisions of the law that require a specific liquidation procedure supervised by the competent authority. In this respect, Article 22 of Law 3606/200720 provides that a bankruptcy proceeding may be suspended if the Hellenic Capital Markets Committee revokes the licence of the company concerned (for reasons provided in Article 21 of Law 3606/2007), then a special liquidation procedure is commenced.

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20 As amended by Article 20 of Law 4474/2017.
It should be noted that Article 2 Paragraph 3 of Law 3458/2006 on Restructuring and Liquidation of Credit Institutions, as amended by Law 4335/2015, also applies to investment companies that are established as parent companies in Greece and that have subsidiaries in another Member State. It remains to be clarified whether this new amendment, which provides for a restructuring procedure rather than bankruptcy and liquidation, shall be applied to investment companies established as parent companies in Greece that do not have any subsidiaries in the EU area.

v Non-merchant individuals

Individuals that are not merchants are exempted from bankruptcy proceedings and fall under the protection of Law 3869/2010, which introduced measures to protect financially distressed individuals and households, such as extension of payments, increase of the number of payment instalments and deletion of debts. The debtor must file a petition before the Peace Court satisfying all statutory requirements, including a detailed certificate of debts, the status of personal assets and income, and the status of the creditors’ claims. The Peace Court will then try to achieve a pre-judicial compromise, but this stage has had a low success rate in practice. The Peace Court, thereafter, issues a preliminary judgment that suspends all enforcement actions against the debtor and orders the way and amount of instalments to be paid until the hearing date. The Peace Court’s final order sets out a binding adjustment of the debtor’s debts.

vi Informal methods to restructure companies in financial difficulties

Informal methods applied to restructure companies in Greece usually include the following:

a An amendment of debt repayment schedule, which is the plainest type of financial restructuring, aimed at making existing debt repayments consistent with the debtor business’s projected cash flows. Such amendment may also be accompanied by an enhancement of lenders’ security and may also include some additional financing to cover urgent needs of the debtor.

b Standstill agreements, under which, debt repayments to banks and bondholders are suspended over a specified period for the purpose of negotiating and reaching a compromise agreement on the financial and operational restructuring of the debtor. Usually, standstill agreements provide the enhancement of participating lenders’ security and may also include some additional financing to cover urgent needs of the debtor, as well as some changes in the debtor’s management.

c Restructuring agreements regarding the financial restructuring of the debtor, combined with operational restructuring of the debtor, on the basis of a business plan and a management team approved by the participating lenders. Such agreements include various components, such as (partial) debt-to-equity conversion, the refinancing of the debt that is agreed as sustainable (by the debtor’s business and on the basis of the approved business plan), the taking of a new enhanced participating lenders’ security package and new working capital financing, for supporting or restarting the debtor’s operation and growth. According to the debtor’s financial position and type

21 Article 2 of Law 4335/2016.
of business, restructuring may include negotiations with the employees and suppliers and agreement on certain payment arrangements in respect of outstanding amounts, to enable the debtor’s stable operation.

The above transactions would ideally take place with the participation of existing major shareholders, in the form of new equity contributions (a component that has been quite limited in Greece up until now) or of an investor capable of enhancing further debtor’s management efficiency, capital structure, and credibility in the Greek and international market.

vii Other laws relevant to insolvency and restructuring

The taking and enforcement of security

The new amendments to the Bankruptcy Code categorise Greece as an even more ‘creditor-friendly’ jurisdiction than before. The right of creditors to submit a pre-pack deal for ratification, without the debtor’s consent, in the case of present cessation of payments, the limitation of the available deadlines as well as the right of the special mandator to substitute shareholders or stakeholders that deny their presence or vote for decisions that are required under the pre-pack deal are major provisions that enhance the efficiency of the restructuring process and disregard any act that could jeopardise the operation of the entity in a way that promotes both creditors’ and society’s interests.

Moreover, financial assistance to companies is provided mainly by the banks, which enjoy multiple ways of security measures and a privileged enforcement, in case of insolvency. A bank providing a loan will take a mortgage on the company’s immovable property or a fixed or floating charge on its moveable property, particularly on its inventory and equipment. A very important amendment concerns the priority of those claims that arise from financing of the entity in connection to a restructuring or reorganisation plan. Such claims are now the top priority and must be satisfied in full. Thus, banks that in most cases provide such financing are fully protected and satisfied, under the new Bankruptcy Code.

In fact, following the announcement of the creditors’ claims, within one month²² from the publication of the court’s decision and their verification by the judge rapporteur and the insolvency practitioner, within one month and granted that a reorganisation plan has not been concluded, the insolvency practitioner commences the realisation of the company’s assets (unsecured and secured). First in priority are creditors with general preferred privileges.²³ The holder of the security in a specific asset of the company, whether immovable or moveable, has a specific privilege (second class) and may be satisfied after the general preferred privileges. The third (last) class of priority includes unsecured creditors, who are satisfied after general and specific privileges. Nonetheless, before payments to any of the aforementioned classes,

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²² Such deadline can be extended by the judge rapporteur for up to two months, only in exigent circumstances, because of the amount and nature of the claims as well as the number of the creditors. Article 93 Paragraph 1, Law 3588/2007.

²³ General privileges, mainly, include: financing of the debtor for its continuing operations, claims arising from the contribution of goods and services to the debtor, based on the reorganisation plan or the restructuring plan, even those that were granted 6 months, in maximum, prior to the submission of the pre-pack deal; if the debtor is an individual (an insolvent merchant); costs and expenses for his or her funeral, hospitalisation, daily necessaries; claims from dependent employment agreement; periodical fees for services that arose within two years prior to the filing of bankruptcy; lawyers’ fees, value added tax claims, taxes, pension funds’ claims; and any claims of the state and the prefectures.
bankruptcy expenses, expenses concerning the management of ‘non-exempt’ property\textsuperscript{24} and claims of collective creditors\textsuperscript{25} must be paid in full. Moreover, if the three priority classes coincide, the proceeds are separated as follows: after the general preferred creditors who have granted financing, goods or services in connection to the restructuring or reorganisation plan receive full payment, then the rest of the general creditors receive 25 per cent of the proceeds, special preferred creditors receive 65 per cent and unsecured creditors receive 10 per cent.

**Duties of directors of companies in financial difficulties**

In Greece, the law sets out two different categories of the directors’ duties: the first category concerns the payment of the entity’s tax liabilities and social security contributions, while the second category concerns the initiation of the bankruptcy proceedings.

With regard to the first category, in case the entity fails to withhold, collect or pay income tax, VAT, or its respective share of social security contributions and any surcharges, the directors, administrators, executive managers and directors, as well as syndic or bankruptcy trustees (now insolvency practitioners) of a legal entity, are rendered jointly and severally liable for payment of such taxes and contributions.\textsuperscript{26} This joint and several liability arises at the date of liquidation or merger or acquisition of the liable company. It should be noted though, that in the case of non-payment of withholding taxes (VAT, etc.) and social security contributions, the liability extends to all directors, administrators, etc., for claims arisen prior to and during their respective office.

A significant provision that should be mentioned is the extension of joint and several liability,\textsuperscript{27} arising from all due taxes, to shareholders of the company who hold at least 10 per cent of the company’s paid-up share capital,\textsuperscript{28} within three years prior to dissolution.

The second category of duties refers to the prompt and timely initiation of the bankruptcy proceedings by the company’s directors. The Bankruptcy Code envisages the joint liability of directors\textsuperscript{29} as well as of those who exercised undue influence on them, in case they fail to promptly file a bankruptcy petition, within 30 days from the date that there is present inability of the company to pay its liabilities as they become due. Such liability entails the restitution of creditors for damages arising from the reduction of the insolvency proceeds.

Similarly, joint liability is attached to the company’s directors if the initiation of the bankruptcy proceedings is a result of a fraudulent or grossly negligent act.\textsuperscript{30}

The importance of the bankruptcy rules, in terms of social and financial consequences, is also evident by the establishment of criminal liability against the company’s directors\textsuperscript{31}

\textsuperscript{24} ‘Non-exempt’ property refers to the bankrupt company’s assets as of the date of the bankruptcy’s declaration. ‘Exempt’ property refers to such company’s assets that are statutorily exempted from liquidation, such as necessaries, family rights, the debtor’s personality and his or her ability to work, rights that are strictly connected to his or her person (such as the right to use his or her name, to accept or waive inheritance rights, etc.).

\textsuperscript{25} Collective creditors are those creditors whose claims arose out of the insolvency practitioner’s actions in connection to the bankruptcy proceedings.

\textsuperscript{26} Article 50 of Law 4174/2013 and 31 of Law 4321/2015.

\textsuperscript{27} This extension is limited to amounts received by the shareholders as dividends or as payment in kind/cash and only for those claims that arose during acquisition of the shares.

\textsuperscript{28} Listed companies are exempted from such liability extension.

\textsuperscript{29} Article 98 Paragraph 1 of Law 3588/2007.

\textsuperscript{30} Article 98 Paragraph 2 of Law 3588/2007.

\textsuperscript{31} Article 176 Paragraph 1 of Law 3588/2007.
if they defraud creditors, conceal or fraudulently transfer assets of the company, dispose of inventory at very low prices, make false declarations or generally diminish the value of the company’s assets.

**Clawback actions**

Fraudulent exploitation of the entity’s assets is also avoided through the annulment of specific transactions that took place in the statutorily determined suspect period. The Bankruptcy Code distinguishes between transactions that must be annulled and transactions that could be annulled.

The insolvency practitioner must proceed with the mandatory annulment of transactions 32 made by the entity within the period of filing the bankruptcy petition and the declaration of bankruptcy (suspect period) and specifically:

- donations and gratuitous deeds or deeds that resulted in undervalued consideration for the entity;
- payment of debts that were not due and payable;
- payment of due debts with means other than cash; and
- imposition of security measures on the entity’s assets for preexisting debts, when the entity had not undertaken such obligation or for new debts arising from a novation agreement.

On the contrary, the insolvency practitioner may proceed 33 with the annulment of transactions, whereby the other party acted in bad faith, knew of the company’s cessation of payments and that such transaction was detrimental to the creditors’ interests.

Similarly, if the company entered into transactions with the intent to defraud creditors or benefit other creditors within five years prior to the declaration of bankruptcy, these transactions may be annulled, provided that the other party knew of the company’s intent. 34

Transactions that took place during the execution of a restructuring or reorganisation plan are explicitly exempted from such revocation. 35

It should be noted that there are some transactions that are exempted from bankruptcy revocation, even if entered into within the suspect period, specifically:

- regular business activities and arm’s-length transactions;
- the provision of services or goods by the company for which counter-consideration was an immediate and equivalent payment in cash;
- the granting of mortgage in favour of a company – especially a bank – according to Law 17.07/13.08.1923;
- the granting of pledge in favour of banks, regarding preexisting claims from loans or open accounts, according to Legislative Decree 4001/1959;
- the creation of a mortgage or pledge to secure the issuance of bond loans or transfer of claims, according to Law 3156/2003; and
- the granting of security by special purpose vehicles (SPV) or other third parties in favour of banks, or other third parties to secure claims against the SPV, acting within the scope of a public-private partnership (PPP) agreement, according to Law 3389/2005.

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33 Article 43 of Law 3588/2007.
34 Article 44 of Law 3588/2007.
35 Article 45(e) of Law 3588/2007.
III  RECENT LEGAL DEVELOPMENTS

The long-term financial and social distress of Greece highlighted the importance of the Bankruptcy Code and the need for its deep reform in order to restrain or at least reduce the serious impact of this crisis on enterprises, employees and employment. Thus, the Bankruptcy Code was recently updated by virtue of Law 4446/2017, which focuses on providing a second chance to honest entrepreneurs, enhancing the insolvency proceedings to avoid unnecessary delays and costs and enhancing the restructuring procedure in a way that preserves value and is beneficial for all stakeholders. These modifications are in alignment with the principles set out in the Commission Recommendation of 12 March 2014 on a new approach to business failure and insolvency,36 which promotes the restructure of economically viable but distressed businesses at an early stage and maximise the benefits for all stakeholders. These principles pervade the new provisions of the Bankruptcy Code.

The continuous changes to the Bankruptcy Code prove that national legislators are vigilant about the current needs of the market, the necessity to interfere efficiently in the operation of distressed businesses and the improvement of the corporate rescue framework. The recent amendments demonstrate a greater coherence and an increased efficiency in these rules that offer more opportunities and reduce costs and time loss.

i  Regulation of the insolvency practitioner profession

Since 2015, the Bankruptcy Code provided for a new role: the insolvency practitioner. The insolvency practitioner is responsible for undertaking the duties of the syndic or bankruptcy trustee, mediator, special agent and special liquidator, as these duties are set out in the Bankruptcy Code. The profession of the insolvency practitioner is now regulated by virtue of Presidential Decree 133/2016, according to which a natural person can be appointed as an insolvency practitioner, granted that he or she has succeeded in the relevant national exams and has obtained the required licence.

In order to participate in these exams, the natural person must have exercised the legal or audit or accountant of class A profession for at least five years. The insolvency practitioner shall exercise his or her duties with integrity, independence, honesty and professionalism and shall be liable for any wrongdoing. Personal liability is attached only in case of wilful misconduct or gross negligence. Liability under the provisions of the tort law is not excluded. Moreover, the insolvency practitioner is supervised by the Insolvency Administration Committee, which is also responsible to keep a register of accredited insolvency practitioners, while the Disciplinary Board shall be responsible to monitor the insolvency practitioner’s appropriate conduct and to impose the statutory disciplinary measures, in case of misconducts.

ii  Procedural changes in restructuring

The new Bankruptcy Code has simplified the restructuring procedure and introduced shorter and more internal proceedings, as explained below (see Section IV.ii, infra).

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iii General changes in insolvency procedure

Provisions regarding the debtor’s duties

The new Bankruptcy Code provides for two basic amendments regarding the debtor’s duties: (1) the first concerns the duty of the debtor to submit along with the bankruptcy petition his or her financial data and a certificate witnessing the amounts of his or her debts, issued by the state. These additional documents shall help the court to have a more accurate picture of the debtor’s financial situation; and (2) the second concerns the appointment of the debtor as a manager of the entity’s assets (along with the insolvency practitioner), regardless of whether he or she filed for a bankruptcy petition. In fact, the only criterion is whether such appointment in favour of the creditors’ interests.

Changes in the bankruptcy organs

The infrequent use of the creditors’ committee, which was entrusted to monitor the bankruptcy proceedings and assist the insolvency practitioner’s duties resulted in its abolition. Thus, the creditors’ committee is no longer one of the bankruptcy’s organs. Moreover, the duties of the judge rapporteur have been upgraded. As of today, the judge rapporteur is responsible for deciding upon conflicts between the creditors, granting his or her consent for specific actions, such as sale of real estate property, supervising the proceedings during the auction of the business as well as convening the creditors’ assembly, following a request by the insolvency practitioner or creditors representing 20 per cent of the total claims to decide upon the sale of the business either as a whole or in part.

Extension of liability

The new Bankruptcy Code provides for an extended liability for both the insolvency practitioner and the board of directors or other management body of the entity. On one hand, the insolvency practitioner is liable for any default in the performance of his or her duties, while a liability towards third parties may be attached only in case of wilful misconduct or gross negligence. Liability under tort law is not excluded.

On the other hand, the board of directors or other management body are liable if they fail to promptly file a bankruptcy petition within 30 days of the date that the entity is unable to pay its liabilities as they become due. Such liability entails the restitution of creditors for damages arising from the reduction of the insolvency proceeds. Similarly, joint liability is attached to the entity’s directors or management if the initiation of the bankruptcy proceedings is a result of a fraudulent or grossly negligent act.

Shortening of deadlines

In general, the deadlines of the insolvency procedure are shortened as follows: (1) the deadline for filing an appeal against the orders of the judge rapporteur is now 10 days from the issuance of such orders (previously 20 days); (2) the deadline for the submission of the

37 Article 80 of Law 3588/2007. The insolvency practitioner is similarly liable for agents used, if he or she was not entitled to appoint them. Otherwise, the insolvency practitioner’s liability is limited to the appointment of such person and the directions provided.

38 Article 98 of Law 3588/2007. The same rules apply to those people who exercised undue influence on directors and managers, holding them jointly liable.

39 Articles 60, 70, 82 and 84 of Law 3588/2007, respectively.
report by the insolvency practitioner is now five days (it was previously 10 days) prior to the creditors’ assembly and must be published in the Bulletin of Judicial Publications of the Jurists’ Pension Fund; (3) the deadline for the convention of the creditors’ assembly by the judge rapporteur is now five days (it was previously 10 days) prior to such meeting and must be published in the Bulletin of Judicial Publications of the Jurists’ Pension Fund; and (4) the deadline for the convention of the creditors’ assembly by the judge rapporteur is now 10 days (it was previously 20 days) following verification of the their claims and the deadline for informing the debtor and insolvency practitioner about such convention is now three days (it was previously five days).

Priority of claims

By virtue of Law 4446/2016, the priority of claims has changed again.

Financiers of the troubled entity are given motives to continue investing their money, as financial facility is in the first rank of general preferred privileges, whether the restructuring or reorganisation plan is ratified or not and shall be satisfied in full prior to any other payments. This privilege applies also to financing granted during negotiations up to six months prior to the filing of the restructuring or reorganisation plan, as long as this privilege is explicitly provided in such plans or financing agreements.

If the three priority classes coincide, the proceeds are separated as follows: after the general preferred creditors who have granted financing, goods or services in connection to the restructuring or reorganisation plan receive full payment, then the rest of the general creditors receive 25 per cent of the proceeds, special preferred creditors receive 65 per cent and unsecured creditors receive 10 per cent.40

Liquidation of small entities

The new Bankruptcy Code provides for important amendments to the liquidation of small companies. The law identifies small entities as those that meet at least two of the following criteria: (1) have total assets amounting up to €150,000; (2) have a turnover amounting up to €200,000; and (3) employ up to five people on average. If two of the aforementioned conditions are met according to the write-downs of the inventory, the court declares the initiation of liquidation of the small entity.

Announcement of the creditors’ claims must take place within one month of publication of the court’s decision. Any delay in such announcement does not allow for a second chance and the creditor may not file a third-party objection before the court for the judicial verification of his or her claim, as provided in the regular insolvency process.

Sales of assets that are subject to deterioration, or undervaluation, or if their preservation is costly can proceed without the consent of the judge rapporteur. Prior to the creditors union, if the business is unlikely to operate or be sold entirely, then the insolvency practitioner may proceed with the sale of moveable property and inventories following consent by the judge rapporteur. In this case, the debtor must be informed about such sale in order to raise any objections within three days. This obligation is not required after the creditors union.

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Sales of immoveable property take place in accordance with the regular insolvency procedure. If the first auction and its repetition within two weeks are fruitless, then the judge rapporteur may order the sale of the immoveable property without an auction, following such request by the insolvency practitioner.

**Discharge of debts**

In compliance with the Commission Recommendation C(2014) 1500, the new Bankruptcy Code gives a second chance to honest entrepreneurs. In fact, the court, after reviewing the judge rapporteur’s report on the assessment of the causes and circumstance that led to bankruptcy and after hearing the insolvency practitioner on the same matters, may excuse the debtor, if he or she cooperated in good faith with all the parties involved, during the insolvency procedure. If the insolvency has been completed with the sale of the business, then the debtor may request to be excused and the court decides on the same aforementioned basis. If the debtor is excused, he or she may not be arrested and any forfeiture from rights is suspended. For an entity, the final ratification of the reorganization plan or the conclusion of the insolvency due to full satisfaction of creditors are reasons for its revival.

Moreover, within two years from declaration of bankruptcy, the debtor may file for a discharge of debts and the court may discharge him or her for any outstanding claims if he or she can also be excused. This order must be issued within 60 days from the hearing. Of course, the debtor may not be discharged for claims arising from his or her wilful misconduct or gross negligence. In case the insolvency is completed with the ratification of a reorganisation plan, then the debtor is automatically discharged, unless otherwise provided therein. Finally, if the debtor is excused and three years pass from the declaration of bankruptcy, then the debtor is automatically discharged of his or her debts.

**iv Regulation of NPLs**

Another important legal development concerns the regulation of NPLs. As of today, the four systemic banks of Greece hold over €100 billion of non-performing loans, while efforts are being made to reduce them up to €67 billion by the end of 2019. Of those non-performing loans, a portfolio amounting to €16.4 billion is expected to be disposed or fall under the special administration procedure.\(^{41}\) In fact, the pressure for liquidity led to replacements of the banks’ boards of directors, in order to ensure that a highly qualified management can face the current challenges of the banking sector. The law of NPLs has been recently modified in view of making the respective legal framework more attractive and easier for the management and acquisition of Greek NPLs.\(^{42}\)

NPLs shall be managed: (1) either by special NPL asset-management companies limited by shares (with special and limited scope of business) that operate in Greece or in the European Economic Area; or (2) purchased and transferred to companies limited by shares that operate in Greece or in the European Economic Area or in countries outside the EU\(^{43}\) and part of their business scope is to purchase and acquire claims from loans or credit agreements.

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\(^{42}\) Law 4354/2015, as recently modified by Article 70 of Law 4389/2016, Article 4 of Law 4393/2016 and Article 48 of Law 4472/2017.

\(^{43}\) Companies established in countries outside of the EU may establish a branch in Greece provided that their registered seat is not in a non-cooperative country or in a country with a preferential tax regime.
The regulation of NPLs sets out the requirements for the establishment and operation of the eligible companies. For a special NPLs asset management company to acquire permission to manage NPLs (and any collateral immovable property), it must file with the Bank of Greece, among others, its article of association, the identity of any and all natural or legal persons that have directly or indirectly a special participation in the company, the identity of any and all natural or legal persons that exercise control in the company, a business plan including the company’s projected actions, strategy and available resources, a detailed report of the methods and procedures to be adopted for such management and questionnaires that assess its ability and suitability to deal with the restructuring of NPLs. The Bank of Greece shall grant the required licence within two months of the submission of the respective petition. Furthermore, a management company must have a minimum share capital of €100,000, and if it wishes to finance new loans or credit agreements, a share capital of €4.5 million.

The acquisition of NPLs, on the other hand, does not require a specific licence but the acquiring company must have signed a management agreement with a special NPL asset-management company. The sale and transfer of such loans shall be effective only upon delivery of a written extrajudicial invitation to the debtor (and guarantor) to settle his or her debt within 12 months prior to such sale and transfer, according to a debt settlement agreement in writing. The acquisition is effective against third parties following registration of the agreement in the books of the Registry of Pledges and notification of the assignment to the debtors and any guarantors.

It should be noted that the sale and transfer of NPLs shall have an income taxation on the goodwill, borne by the acquiring company, while both management and acquisition agreements shall be subject to a VAT taxation of 24 per cent. Stamp duties are explicitly excluded for the agreements executed by the Special NPLs Asset Management Company.

Finally, Law 4472/2017 introduces a major provision according to which those persons who are responsible for supervising and or managing: (1) public property (including all kinds of state property or property of state-owned entities); or (2) property of a credit or financial institution are immune from any criminal or civil liability arising from their actions or failure in connection to the restructuring or discharge of loans, claims or charges, within the scope of the Bankruptcy Code or the law on the extrajudicial debt settlement procedure or the law on financially distressed individuals and households or the law on special liquidation of credit institutions or the law on the NPLs, and in accordance with the provisions of their internal regulations and guidelines, rules and procedures and applicable laws. These actions or failures to act must also aim to settle or restructure debts or assist the operation of the business and should not deteriorate the financial situation of the entity in comparison to that which would result from a liquidation procedure.

v Restructuring of municipalities and communities

Until 2014, municipalities and communities (M&Cs), as entities of public interest, could not declare bankruptcy. But the long-term financial crisis challenged their economic independency and sustainability and led to the introduction of Article 174 of Law 4270/2014 on the Restructuring of Municipalities and Communities. The idea of this law is to closely watch the financial performance of M&Cs, alert their management bodies and impose restructuring measures in accordance with a respective plan.

The Financial Independency Observatory of M&Cs (the Observatory) is entitled to report to the Ministry of Internal Affairs as well as the M&Cs, the latter’s deviation of more than 10 per cent from budgetary targets and provide it with guidelines and methods to
overcome such deviation. If the Observatory concludes that an M&C is incapable of drafting a preliminary balanced budget or fraudulently records false financial data, it is also entitled to draft a report of its financial situation and propose restructuring measures, in accordance with a restructuring plan. Moreover, M&Cs may apply for a voluntary restructuring, which is reviewed (rejected or approved) by the Observatory and the Minister of Internal Affairs.

The measures of a restructuring plan may include:

- suspension of recruitments;
- voluntary or involuntary transfer of employees;
- realisation of mandatory expenses;
- increase of municipal taxes, fees and contributions; and
- granting of a loan by the Deposits and Loans Fund.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

i Value and significance of the transactions

**Marinopoulos Supermarkets**

In 2016, one of the largest supermarket chains in Greece was put under a restructuring procedure due to its financial distress. This case received great press coverage, since it was the first case of the specific industry and with financial and social interests of various stakeholders. The pre-pack deal provides for the establishment of a new company (NewCo), under the trade name ‘Hellenic SuperMarkets Sklavenitis SA’ in which Marinopoulos shall transfer assets amounting to approximately €715 million, liabilities amounting to approximately €1 billion, all its commercial claims and all its fixed assets. Sklavenitis SuperMarkets SA (another major player in the industry) shall acquire the NewCo and contribute in cash, through a share capital increase, an amount of approximately €125 million.

According to the pre-pack deal, which was ratified by the court, the restructuring plan envisages four basic components: (1) haircut of some claims; (2) extensions of credit line by the banks; (3) increase of the number of total instalments for claims towards the state and the Social Security Institution; and (4) specific provisions for the employees. In particular, claims of both secured creditors and unsecured creditors-suppliers of Marinopoulos (the latter’s claims amounting to approximately €647 million) shall be reduced by up to 50 per cent. Apart from Alpha Bank, which accepted a haircut of up to 20 per cent, banks (Alpha Bank, Eurobank, Piraeus Leasing, National Bank of Greece and National Leasing) shall receive full payment of their claims, amounting to approximately €196 million, within 20 years, after a five-year grace period and in 15 unequal instalments with interest, following a capitalisation of any due interest amounts, which shall take place at the execution date of the pre-pack deal. Claims of the state and the Social Security Institution shall be paid in full and in 250 equal and interest-free instalments.

The banks agreed to extend the credit line of Marinopoulos with an amount up to approximately €55 million and provide a credit line to NewCo up to approximately €352 million. Apart from the share capital increase in the NewCo, Sklavenitis SuperMarkets SA and Marinopoulos Bros. Holdings SA shall also provide an interim financing of up

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44 So far, two municipalities have applied for restructuring: the municipality of Salamina and Gortynia in Crete.
to approximately €15 million and €10 million accordingly. It is noted that all existing employment, leasing and tenancy agreements shall be transferred to the new company. Moreover, any and all administrative licences, trademarks, permissions of use, inventory, equipment and furniture are transferred to the new company.

**Dias Aquaculture SA and Selonda**

The restructuring of Dias Aquaculture (Dias) was one of the first that occurred in the fish farm industry. Dias applied for a pre-pack deal, which included a transfer of Dias’ business to Selonda Aquaculture SA. In particular, Dias contributed in kind its total assets, amounting to €69 million, and part of its liabilities, amounting to €29.6 million, to Selonda’s share capital. A part of Dias’ liabilities, which constituted 81.95 per cent of its total liabilities would not be contributed to Selonda; instead, it remained within Dias’s financial statements and was covered with the acquisition of 41,261,980 shares issued by Selonda, in accordance with its share capital increase of €12.4 million. The newly issued shares were subsequently transferred by Dias to its creditors, on a pro rata basis, for their satisfaction. It should be noted that Selonda itself had also applied for a restructuring plan, which resulted in a haircut of its debts held by the banks, amounting to €50 million. Selonda is now managed and operated by a new management appointed by the participating banks, which is seeking an interested investor to buy out Selonda.

**ii Restructuring techniques used**

As normal methods of restructuring are not enough to save distressed companies in the Greek crisis environment, debtors and their creditors are led to more complicated solutions, depending on the nature and size of their business. In particular, large companies that were listed in the Athens Stock Exchange preferred to go private, through acquisition by an interested investor. A greater percentage of medium-sized companies resorted to techniques such as debt-to-equity conversion and debt-forgiveness agreements. In such cases, the banks, which usually hold the largest percentage of their debts, take over their management, proceed with drastic restructuring measures and then search for an interested buyer. Restructured companies – especially those with increased exports – are able to obtain new working capital financing. More advanced tools like a debt push-up, or even the creation of new group structures with lower debt levels or the consolidation of existing players in each sector, are also used to rescue viable businesses and recover part of the existing debt.

**iii Distressed industries and market trends**

The industries of construction, textiles, electric appliance stores and supermarkets have suffered the most severe financial losses within the Greek market. The reasons for such distress can be explained by the fact that they are all capital-intensive industries, with high running costs, squeezed profit margins and, in addition, are overleveraged (through abundant financing provided to them before the crisis). Profit margins have decreased even more now that companies have limited access to working capital finance. Moreover, the recent changes in the income tax code, the real estate property taxation and the increase of VAT up to 24 per cent have significantly diminished the spending capacity of Greek consumers.
iv The extra-judicial debt settlement

A long-awaited procedure was recently legislated; the extra-judicial debt settlement. According to Law 4469/2017, any natural or legal person may file a petition for an extra-judicial debt settlement provided that their total debts to the state, social security contributions and banks (default of payment for at least 90 days) or claims from a payment order issued by the court, as of 31 December 2016 amount to €20,000 at least. In case such person or entity has applied for or has begun a pre-bankruptcy or post-bankruptcy procedure or special administration or liquidation or such person or entity has been finally convicted for tax evasion or money laundering then it is not eligible for the extra-judicial debt settlement. Moreover, the person or the entity must have had for at least one of the last three fiscal years before the petition: (1) a positive EBITDA, if it uses a single-entry accounting system; or (2) a positive EBITDA or positive net position, if it uses a double-entry accounting system.

The petition must be submitted before 3 December 2018 via the electronic platform of the Special Secretariat (Directory) of Private Debt Management. The petition must be accompanied by various documents, such as a creditors’ list, a list of all assets and any encumbrances, any affiliated persons, financial statements and various certificates. Thereafter, the special secretariat appoints a mediator who shall communicate with the debtor and the creditors and shall coordinate the procedure. Continuation of the procedure is subject to the participation of creditors, representing at least 50 per cent of the total claims (not including creditors that are affiliated with the debtor). The law provides that a joint decision by the Ministry of Finance, Ministry of Economy and Development, Ministry of Labour, Social Security and Welfare can promulgate that for debts between €20,000 to €50,000, the procedure is automatic, meaning that the creditors have to choose among predetermined solutions.

Upon notice of the mediator to the creditors to participate in the extrajudicial debt settlement, all enforcement actions (against claims set under the settlement) are suspended for a period up to 70 days. An extension of this period can be granted by the court, following petition of the debtor and approval by the majority of the creditors, for a period up to four months.

The debtor and the majority of the creditors shall appoint an expert to draft a restructuring plan, which may then be ratified by three-fifths of the represented creditors, including two-fifths of the represented secured creditors. Finally, the restructuring plan may be submitted before the court for ratification.

v The pre-pack deal

Since its implementation in 2011, the pre-pack deal has a distinctive position within the scope of bankruptcy law. First of all, it offers a good chance to the interested parties to find a mutually acceptable solution. The new Bankruptcy Code provides that the submission of the pre-pack deal is the only way to initiate the restructuring procedure, as it safeguards time and avoids delaying tactics by debtors. The recent changes that extend the circle of persons that can file for a restructuring procedure, allow creditors that represent at least 60 per cent of the total claims, including 40 per cent of the secured creditors to file a pre-pack deal without the debtor’s consent, if the debtor is in permanent cessation of payments, demonstrate a clear legislative intent to accelerate the restructuring procedure and facilitate further business rescue.
There have been some reservations on the pre-pack deal, mainly focusing on potential ‘cloudy’ negotiations, the partial or significantly diminished satisfaction of unsecured creditors or the impairment of the entity's value.

Despite those reservations, the case of the pre-pack deal was and continues to be successful in Greece, overturning those who believed that debtors and creditors cannot reach an amicable solution. The point that a restructuring plan not only promotes the interests of the creditors but mainly helps an entity stay alive, pay taxes, recruit and make a business plan, is well received.

It should be noted that in a country where bankruptcy was considered a social stigma for many years – the ultimate nightmare of a successful businessman – the idea of the pre-pack deal demolished many prejudices. The legislator has given room to the interested parties to find a way out and act in both personal and public interests.

V INTERNATIONAL

The principles of unity and universality45 pervade the rationale of the Greek law,46 which is applied in insolvency proceedings that are initiated in Greece. The EU Regulation 1346/2000, and all later amendments, were integrated to the Greek insolvency laws in May 2002. Similarly, the UNCITRAL Model Law on Cross-Border Insolvency was implemented almost in its entirety through Law 3858/2010.

Nonetheless, Greek jurisprudence on international insolvency cases is very poor. In fact, there are two main cases47 that were successfully tried before the Greek courts, regarding the recognition of a foreign decision and the initiation of secondary bankruptcy proceedings.

Many provisions of the EU Regulation have superseded any bilateral or multilateral agreements on insolvency proceedings or recognition of foreign decisions. Unlike France and Italy, Greece has not signed any respective agreements, and thus, the EU Regulation 1346/2000 remains in full force.

According to Article 81 of the Treaty of the European Union and Articles 7 and 35 of Law 3858/2010 on Cross-Border Insolvency, the Greek courts must cooperate with foreign courts or foreign insolvency administrators directly or through such administrators. Similarly, the Greek courts are entitled to communicate directly, request information or

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45 Unity and universality mean that the insolvency procedure, whether of individuals or legal entities, is one and the applicable law is that of the jurisdiction, where such procedure was initiated and any creditor, regardless of his/her residence, may participate therein.

46 Both the Bankruptcy Code and the Civil Procedure Code incorporate these principles. In particular, Article 780 of the Civil Procedure Code provides the requirements, regarding the recognition of foreign judicial decisions that: (1) the decision must apply substantive law, that according to the Private International Rules is applicable; (2) the decision must have been issued by the competent jurisdiction, in accordance with the substantive law of the jurisdiction applied; and (3) the decision must not be contrary to moral usage or public order. To the contrary, the EU Regulations 1346/2000 and 2015/848 provide for a more simplified recognition procedure, according to which the declaration of bankruptcy from the competent foreign courts is automatically recognised in other foreign courts, starting from the date of such declaration’s legal effects. The only exceptions to the automatic recognition are those of public order and individual rights.

47 Decision No. 494/2014 of the Single Member Court of First Instance in Kos and Decision No. 437/2013 of the Multi-Member Court of First Instance in Athens.
judicial assistance from foreign courts or foreign insolvency administrators or coordinate cross-border insolvency proceedings with other participant Member States. Although these provisions stand for a considerable time period, no respective cases have been reported.

A recent development in the European Union concerns the abolishment of the EU Regulation 1346/2000 on 26 June 2017. Any and all insolvency proceedings commencing thereafter shall be governed by the EU Regulation 2015/848, as amended by EU Regulation 2017/353. Many novelties of the EU Regulation 2015/848 have already been implemented in the Bankruptcy Code through Law 4336/2016, such as the introduction of the insolvency practitioner and the rescue of viable companies, while the Commission’s recommendations C(2014) 1500 have also been implemented by virtue of Law 4446/2016, including the expedited restructuring procedures and the rules for granting a second chance to honest entrepreneurs. Other novelties, such as the registry of insolvency, the interconnection with the respective registries of other Member States, publication to another Member State and the cooperation of insolvency practitioners both in main and secondary insolvency proceedings may be either implemented through further amendments to the Bankruptcy Code, or the new regulation shall be directly applied to cross-border insolvency cases.

VI FUTURE DEVELOPMENTS

The amendments to the restructuring procedure follow the trends of the European law and the current practices and needs of the Greek market. For the first time, creditors are also entitled to file a pre-pack, without the consent of the debtor, if the debtor is in permanent cessation of payments. This is a crucial provision, as creditors have a chance to rehabilitate entities with growth potential, despite their permanent cessation of payments. It is likely that the law will extend this right also in case of debtors with imminent cessation of payments, as this will help even more creditors who are ‘trapped’ owing to misleading practices by their debtors. It should be noted that a proposal to extend the scope of this procedure as aforementioned cannot be confused with the bankruptcy procedure, in which case only the debtor can file a bankruptcy petition due to imminent cessation of payments. This distinction lies in the heart of restructuring: creditors granting a second chance to businesses that are viable and can grow further, with a good business plan, if they are ‘released’ from their bad management or inefficiencies of their owners.

Moreover, the abolishment of the special liquidation procedure as mentioned above, highlights the importance of the special administration procedure (as described in Section II. i, supra). In order for special administration to play the role required today, some amendments should also take place. These amendments refer to: (1) the provision of the debtor’s right to file for a special administration procedure, as now can be initiated only by creditors; and (2) the extension of the special administration’s scope in order to include imminent cessation of payments as well as probability of insolvency as events or conditions for the initiation of such procedure.
Chapter 13

HONG KONG

*Tom Pugh*

I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

Hong Kong

China resumed its sovereignty over Hong Kong with the establishment of the Hong Kong Special Administrative Region of the PRC on 1 July 1997. The Basic Law – part of the constitution of Hong Kong – was adopted on 4 April 1990 by the National People’s Congress of China and provides for a 50-year period during which Hong Kong will be allowed to retain its current political, social, commercial and legal systems, including those that have made it an international financial and business centre.

Hong Kong operates a free trade economic system with minimal government intervention. A primary attraction is Hong Kong’s legal system, based on English common law and rules of equity, involving strict adherence to the principles of the rule of law and judicial independence.

Many head offices and holding vehicles for Chinese and foreign multinational corporations, financial institutions and regional investors with operations in China and South East Asia, have long maintained their base in Hong Kong. The Hong Kong Stock Exchange is one of the largest globally and a significant proportion of the companies listed on it hold assets and operations in China.

Given its proximity to and relationship with China, Hong Kong is often regarded as the primary intermediary platform for trade between mainland China and the rest of the world, and therefore serves a dual role as both conduit for access to the mainland Chinese market and a springboard for Chinese businesses to gain exposure to international markets.

Hong Kong has also pioneered offshore yuan business, being the first offshore market to launch in 2004. As China’s economy increasingly integrates with the rest of the world’s markets, the yuan will see increasing use as a payment currency. During April 2017, 5,441,688 million yuan was converted into Hong Kong dollars and other currencies, and an equivalent of 5,437,158 million yuan of Hong Kong dollars and other currencies was converted into renminbi through authorised institutions engaged in renminbi business. There were 40,672 renminbi remittance transactions from Hong Kong to mainland China, amounting to 1,100,765 million yuan.²

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1 Tom Pugh is a partner at Mayer Brown JSM.
2 Table 3.3 : Customer deposits by type, Monetary Statistics for March 2017, The Hong Kong Monetary Authority.
ii Economic conditions

Globally, financial markets have seen modest recoveries with ongoing financial volatility. Outside of Asia, the United Kingdom’s ongoing negotiation with the European Union on the terms of its withdrawal from the bloc and the unpredictable policy agenda of the Trump administration in the United States have created economic uncertainties. In China, its very high level of debt coupled with an economic slowdown continues to pose an elevated risk to financial wellbeing of the country and, by extension, that of Hong Kong as a result of the city’s exposure to the mainland market. Moody’s Investors Service has recently downgraded both China’s and Hong Kong’s credit ratings. Hong Kong cannot ignore these global concerns, not least because of China’s impact on its regional neighbours.

China continues to rebalance its economy, moving towards one increasingly driven by domestic consumers. Through the ‘Belt and Road’ initiative, China has pledged more than US$100 billion of investments in infrastructure projects, which span countries in Asia, Africa and Europe. Whether the Belt and Road initiative will help China alleviate its overcapacity through exports, time will tell. The continued uncertainty about China’s shifting exchange rate policy has also contributed to the overall economic uncertainties.

iii Market trends

A general shift from bank lending to alternative credit providers, which has been in evidence over the last few years, continues, but it appears that even with substantial cash reserves available there is uncertainty over how to deploy that capital. This is largely for two reasons: the weight of available capital and low interest rates have meant that the cost of borrowing has been low, keeping returns depressed; and uncertainty over the ability to enforce security close to the assets in the relevant Asian jurisdictions combined with unfavourable local court processes have muddied the risk-to-reward analysis.

A notable result of the move from credit provided by banks to alternative providers is that restructurings may in some circumstances appear to be merely a repackaging, enabling onward sale of relevant debt instruments to other alternative credit providers, allowing profits to be made but also ailing enterprises to survive but not prosper – the zombie company phenomenon.

Hong Kong operates on the basis of the English law approach to distressed enterprises (that is, generally a creditor-friendly approach) but without the benefit of any statutory corporate rescue procedures (such as administration). However, the trend has been away from liquidation and towards refinancing. Notwithstanding a small increase in 2009 following the global financial crisis, statistics from the Official Receiver’s Office show the number of compulsory winding-up petitions presented and orders made has broadly continued to decline. So where, for example, in 2003 the annual total petitions presented was 1,451 of which 1,248 received orders to be wound up, in 2016 the annual total petitions presented was 456, of which 325 were ordered into liquidation. Whether the current turmoil in the world’s economies will to some extent reverse that trend remains to be seen.

4 See www.oro.gov.hk/cgi-bin/oro/stat.cgi.
In Hong Kong, the scheme of arrangement has long been an important restructuring tool and that continues to be the case. As a number of entities listed on the Hong Kong Stock Exchange and otherwise are incorporated offshore, parallel schemes running in Hong Kong and the relevant offshore jurisdictions have become more common.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

Provisions covering the winding up of Hong Kong companies and foreign corporations registered in Hong Kong and the insolvency-related regime are found in the Companies (Winding-Up and Miscellaneous Provisions) Ordinance (the Winding-Up Ordinance) and subsidiary legislation. The Winding-Up Ordinance was recently amended by the Companies (Winding-Up and Miscellaneous Provisions) (Amendment) Ordinance 2016 (the Amendment Ordinance) and the new changes came into effect on 13 February 2017.

The statutory provisions applicable to individual bankruptcy as opposed to corporate insolvency are contained in the Bankruptcy Ordinance. Discussions below focus on corporate insolvency.

Insolvency of a Hong Kong company will generally result in a company being wound up by either voluntary or compulsory liquidation, the latter occurring pursuant to court order on a winding-up petition against the company. There are additional statutory provisions that are applicable in the case of certain regulated industries, such as banking and insurance, and there is also power for the government to petition for the winding up of a company if considered expedient in the public interest.

i Voluntary winding up

Voluntary liquidation may occur when the company is solvent, which is known as a members’ winding up; or when the company is insolvent, which is known as a creditors’ voluntary winding up.

A voluntary liquidation is started by a members’ resolution and then will become a members’ winding up if a certificate of solvency is issued by a majority of the company’s directors, noting their opinion that the company will be able to pay its debts in full within a period not exceeding 12 months from the commencement of the winding up specified in the certificate. If no certificate of solvency is made or if it is not effective because other prescribed criteria are not satisfied, the winding up will be a creditors’ voluntary winding up. The Amendment Ordinance has enhanced the requirements relating to the first creditors’ meeting upon the commencement of a creditors’ voluntary winding up.

The legislation also, uniquely, provides for a procedure allowing directors of a company to commence voluntary liquidation without holding a shareholders’ meeting. Instead, the voluntary liquidation is initiated by a directors’ meeting, resolving (among other things) that the company cannot by reason of its liabilities continue its business, the directors consider it necessary to be wound up and that it is not reasonably practicable for the company to be wound up under any of the other procedures prescribed in the legislation, giving supporting reasons. The Amendment Ordinance has introduced additional safeguards to reduce the risk of abuse in a director-initiated creditors’ voluntary winding up. In any event, the procedure is not frequently used, given the general availability of other procedures.
ii Compulsory winding up

Compulsory winding up pursuant to a court order is based on a petition presented usually by a creditor, although a shareholder or the company itself may also petition in appropriate circumstances. The legislation provides various grounds upon which a petition can be presented, the most common of which is an inability of the company to pay its debts, a matter that may either be proved on the balance of probabilities by the petitioner or deemed where the company has failed to pay or otherwise satisfy a statutory demand within three weeks of that demand being served on the company; and another of which is that it is just and equitable for the company to be wound up.

The legislation does not provide a specific definition of ‘insolvency’, instead, referring to the inability to pay debts, which is deemed to have occurred on satisfaction of one or more of the bases prescribed in Section 178 of the Winding-Up Ordinance. In considering an inability to pay debts, the court may consider applying either the cash flow or the balance sheet test.

For a creditor to bring a winding-up petition, there must be a debt (present, contingent or prospective) for a liquidated sum due from the debtor company to the creditor. Where the debt is not yet due, but is to fall due in the future or is contingent, the court will not hear the petition unless security for costs are provided and a prima facie case for winding up is demonstrated. If a debt is the subject of a genuine dispute, it cannot found the basis of a winding-up petition. Further, for the debt to be capable of supporting a winding-up petition, it must be at least HK$10,000.

iii The liquidator and committee of inspection

In Hong Kong there is no requirement for liquidators to be licensed, as is the case in certain other jurisdictions. Even so, in practice, appointed liquidators are licensed insolvency practitioners, accountants or other professionals with the requisite commercial experience.

In general terms, a court-appointed liquidator is required to investigate the affairs of the company in order to get in and realise its assets, before applying those realisations in discharge of the company’s liabilities, which will include investigating the conduct of the company’s past and present office holders to consider whether any wrongful conduct or criminal offence has been committed against the company.

In fulfilling these functions, liquidators have broad powers at their disposal, some that require sanction of the court or of a committee of inspection (if there is one) before being exercised (such as making any compromise or arrangement with the company’s creditors, contributories, claimants or debtors, and disclaiming onerous property); and some that do not (such as realising the property of the company and dealing with proofs of debt).

The committee of inspection is appointed at a meeting of creditors and is intended to be representative of the creditors of the company and capable of taking decisions in the interests of all creditors. Outside the powers only exercisable with sanction, it is for the liquidator to decide how frequently the committee of inspection is to be consulted. The Amendment Ordinance introduced a number of changes aimed at simplifying the proceedings of the committee of inspection and promoting court-free procedures, thereby potentially reducing the time and costs involved in the winding-up process.
iv Other restructuring methods

Workouts

Workout arrangements, pursuant to which a debtor company enters into contractual arrangements with its bank and other creditors, continue in Hong Kong and may be used in conjunction with a scheme of arrangement, as discussed above. The non-statutory guidelines issued jointly by the Hong Kong Association of Banks and the Hong Kong Monetary Authority provide principles as to how banks should deal with customers in financial difficulty, encouraging a standstill, during which an information gathering assessment can be undertaken with a view to reaching an informal decision as to the customer’s long-term future. Although non-statutory, banks are expected to adhere to the guidelines and to act cooperatively and in an expeditious manner in trying to agree a restructuring plan, and will be subject to scrutiny from the regulators if they fail to do so.

However, the guidelines are applicable only to banks and, therefore, other creditors such as bondholders, hedge funds, employees and trade creditors may proceed with enforcement actions during the period in which banks are seeking to implement a restructuring plan with the debtor company.

Scheme of arrangement

While a mechanism referred to as ‘provisional supervision’ was put forward by the government more than 15 years ago, Hong Kong continues to operate without a formal procedure by which a distressed company can reorganise its debt obligations and trade out of difficulties, such as administration in the UK or Chapter 11 in the United States.

The primary restructuring tool available, therefore, remains the scheme of arrangement, which can be used for both insolvent and solvent companies. Schemes may be used to supplement informal contractual workouts implemented by multibank creditor groups or other creditor constituencies.

As schemes of arrangement do not provide a statutory moratorium, there remains a risk of a creditor taking enforcement action, including winding-up proceedings, after a scheme of arrangement has been initiated. For this reason, schemes of arrangement in the insolvency context are frequently undertaken in conjunction with provisional liquidation (where appropriate) or liquidation, to create the necessary moratorium. As a result of the Legend case, it currently appears clear that restructuring alone is not sufficient to found the appointment of provisional liquidators so that an applicant will still have to show concern as to, for example, potential dissipation of the company’s assets and that it may reasonably be expected that liquidation will ultimately ensue.

For a foreign company incorporated outside Hong Kong, whether it is possible to have provisional liquidators appointed in its jurisdiction of incorporation for the purpose of facilitating a corporate restructuring will depend on the law of that jurisdiction. If provisional liquidators are appointed to a foreign company where it was incorporated, and the provisional liquidators would like their appointment to be recognised in Hong Kong, they can obtain a letter of request from the court of the jurisdiction where they were appointed, and then apply to the Hong Kong court for an order to this effect.

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5 Re Legend International Resorts Ltd [2006] 2 HKLRD 192.
6 Joint Official Liquidators of A Co v. B Co [2014] 4 HKLRD 374; and see Section IV, infra.
If the company is being wound up, an application to court to convene a creditors’ meeting to propound a scheme must be made by the liquidator or provisional liquidator. The court will consider whether the terms of the scheme are fair and could be supported by creditors exercising reasonable judgment. However, Hong Kong has not fully moved with the updated position in England so the court at the first hearing is not obliged to consider whether the classes of creditors involved in the scheme have been appropriately constituted. Therefore, there remains the risk of creditor classification being called into question at the second hearing, at which sanction is sought. The scheme will be legally binding on the company and the scheme creditors – including those scheme creditors who voted against the scheme and those who do not vote – if at the scheme meeting, the requisite majority representing a majority in number and at least 75 per cent in value of the creditors present and voting, in person or by proxy, at the meeting vote in favour of the scheme; the court sanctions the scheme; and an office copy of that order is registered by the registrar of companies in Hong Kong.

v Security

Hong Kong law recognises four forms of consensual security: the mortgage, the charge, the pledge and the lien. The formalities required for effective security, such as registration, will depend on the form of security. Failure to register a registrable charge will result in the charge being ineffective against a liquidator and any creditor of the company, although it will not affect the validity of the charge itself as between the parties to the security. Certain classes of assets (such as maritime vessels and aircraft) have separate registries, and registration will be required or expected at the relevant registry.

Secured creditors having a fixed charge will rank first for distributions from a company in liquidation. They are generally entitled to claim as unsecured creditors for any balance that remains unpaid after realisation of the security.

Where a company has granted a fixed and floating charge debenture (usually in favour of its bankers) over its undertaking, property and assets, the usual method of enforcement is through the appointment of a receiver. A receiver may be appointed outside liquidation but receivership is often indicative of insolvency. The validity of a floating charge created within 12 months if the person in favour of whom the floating charge is created is not connected with the company (or within two years if the person in favour of whom the floating charge is created is connected with the company) prior to the company’s winding up may be susceptible to challenge by the company’s liquidator to the extent that new monies were not advanced.

vi Duties of directors

Directors’ duties (statutory and fiduciary) are owed to the company. While a company is solvent, the duty to act in the company’s best interests is generally assessed by reference to the interests of shareholders, whereas upon insolvency the interests of creditors will supersede those of shareholders in that assessment.

The codification of the duty of care, skill and diligence for directors now found in the Companies Ordinance7 is based on Section 174 of the UK Companies Act 2006 and therefore applies a dual objective/subjective standard to directors’ duty of care.

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7 Section 465, Companies Ordinance.
The Winding-Up Ordinance provides a summary method of enforcing existing duties owed by past and present officers (who include directors, managers and company secretaries) of a company subject to winding-up proceedings. Conduct that may give rise to liability under this section might include a breach of directors’ duties, or claims arising from preferences or fraudulent trading.

A liquidator is the agent of the company and on appointment displaces the directors and assumes their powers and functions in respect of the company. The directors remain obliged to assist the liquidator in the course of the winding up, and failure to provide the required assistance may result in civil and criminal penalties being imposed on the offending directors. In contrast, the liquidator does not owe duties to the directors of the company and is not required to keep the directors apprised of his activities.

vii Clawback actions

As a starting point, there are two main categories of actions that a liquidator can bring:

a Company actions – The liquidator can commence proceedings in the name of the company to enforce rights and claims vested in the company prior to liquidation: the claim exists and can be pursued irrespective of whether or not the company is insolvent, and the proper plaintiff is the company.

b Liquidator actions – In addition to company actions, there are a number of special powers given to a liquidator that can be invoked to avoid or reverse the effect of certain transactions that would have remained binding on the company but for its liquidation. These ‘avoidance powers’ are available only in the context of winding-up proceedings and are contained in legislation.

If a company is compulsorily wound up within one year of a payment out of capital under statutory procedures for redemption or buy-back of any of its own shares, the Amendment Ordinance now provides that directors who signed the solvency statement in relation to the payment out of capital and past shareholders will be jointly and severally liable to contribute to the assets of that company. It is a defence for a director to show that he or she had reasonable grounds for believing his opinion expressed in the solvency statement.

The Amendment Ordinance has updated Hong Kong’s antecedent breach legislation, including the introduction of undervalue transactions for corporate insolvency (the concept is well known but previously only applicable in personal bankruptcy). Pre-insolvency transactions that can be challenged or set aside by the liquidator include:

a Transactions at an undervalue – Transactions entered into by a company for which the company received no consideration or consideration that is significantly less than that given by the company. A transaction at an undervalue will be liable to be set aside by a court unless the court is satisfied that the company entered into the transaction in good faith and for the purpose of carrying on its business, and at the time the company did so, there were reasonable grounds for believing that the transaction would benefit the company. The look-back period for transactions at an undervalue is five years.

b Unfair preferences – Action taken by the company, influenced by a desire to prefer, that puts one creditor in a better position in the event of insolvency than it would otherwise have been. A transaction will be liable to be set aside by a court if there is

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8 Section 276, Winding-Up Ordinance.
evidence that the desire to prefer the recipient influenced the company's decision to enter into the transaction (or make the subject payment) and if ‘... it was one of the factors which operated on the minds of those who made the decision’.\(^9\) The desire to prefer the recipient does not have to be the dominant factor; it may simply be one of a number of matters considered by the company. Transactions involving a person connected with the company (other than by reason of being its employee) are presumed to be an unfair preference. The look-back period in respect of transactions entered into between an insolvent company and a person connected with the insolvent company (other than by reason of being its employee) is two years, and in any other case of an unfair preference, the look-back period is six months.

c Extortionate extensions of credit to the company – The terms of the transaction are, or were, such as to require grossly exorbitant payments to be made or it otherwise grossly contravenes ordinary principles of fair dealing.

d Floating charges – The Winding-Up Ordinance invalidates a charge created as a ‘floating charge’ within two years prior to the commencement of the winding up if the floating charge was granted to a person connected with the company (other than by reason of being its employee) or within one year prior to the commencement of the winding up if the floating charge was granted to any person other than a person connected with the company, provided that, in either case, the company subject to winding up was insolvent when the charge was created, or, alternatively, the company became insolvent as a consequence of granting the charge.

e Transactions made with the intention of defrauding creditors – The standard of proof is high and consequently it can be difficult to pursue this action.

III RECENT LEGAL DEVELOPMENTS

Hong Kong is a gateway to business around Asia and investors continue to appreciate the certainty of its legal system and application of the rule of law. For a variety of reasons, including legal and tax considerations, enterprises running businesses through Hong Kong will often do so using corporate structures involving several jurisdictions. In addition, the assets underpinning those businesses are frequently situated outside Hong Kong.

It is inevitable, therefore, that the growing global trend of cross-border insolvencies is also being felt in Hong Kong. Two associated aspects have been the subject of continued judicial consideration: jurisdiction of the Hong Kong courts to wind up foreign companies and recognition of foreign liquidation proceedings.

Legislative developments include changes to the Winding-Up Ordinance through the Amendment Ordinance referred to above and the introduction of Hong Kong’s bank resolution regime.

i Winding up foreign companies

Hong Kong courts have power under the legislation to wind up a foreign company, including one that is not registered in Hong Kong.

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\(^9\) Re MC Bacon Ltd (No. 1) [1990] BCLC 324 at 336.
The courts will not exercise the power lightly and will determine the position on a case-by-case basis. The courts have formulated three core requirements for exercising their power to wind up a foreign company: 10

a. there has to be a sufficient connection with Hong Kong, although this does not necessarily have to consist of the presence of assets within the jurisdiction;

b. there must be a reasonable possibility that the winding-up order would benefit those applying for it; and

c. the court must be able to exercise jurisdiction over one or more persons in the distribution of the company’s assets.

The fact that the court considers itself to have jurisdiction does not mean that it will make a winding-up order and will maintain discretion whether or not to do so.

In the high-profile Yung Kee case, 11 the Court of Final Appeal (CFA) reversed the lower courts’ decisions and decided Yung Kee Holdings Limited (Yung Kee), incorporated in the BVI and indirectly holding the well-known Yung Kee restaurant in Hong Kong, has sufficient connection with Hong Kong to trigger the Hong Kong court’s winding-up jurisdiction, and to do so on just and equitable grounds.

Considering jurisdiction from a winding-up perspective, the CFA focused on the first core requirement, namely a ‘sufficient connection with Hong Kong’, holding that the test is whether the petitioner will derive significant benefit from a winding-up order in Hong Kong, even though the company is incorporated elsewhere.

In Shandong Chenming Paper Holdings Limited v Arjowiggins, 12 a Chinese company argued that the Hong Kong courts lacked jurisdiction to wind it up and that the ‘benefit test’ (core requirement (b) above) would not be satisfied without the Chinese company having assets in Hong Kong available for distribution to creditors.

A dispute had arisen between a Chinese Hong Kong/Shenzhen listed paper conglomerate and its Hong Kong joint venture party, with subsequent arbitration resulting in a substantial award in favour of the Hong Kong company.

The court broadly concluded that the pressure produced by a winding up was sufficient to constitute a benefit to the Hong Kong company in its efforts to enforce the arbitral award; and that as a matter of public policy a company who has chosen to list its shares in Hong Kong should not then be able to refuse to honour an award required under Hong Kong law.

## ii Recognition of foreign proceedings

In Singularis Holdings Ltd v. PwC, 13 the Privy Council Board considered the doctrine of modified universalism (whereby, broadly speaking, a court will give such assistance as it can to foreign insolvency proceedings, consistent with local law and local public policy, to ensure that a company’s assets are distributed under a single system), and held by a majority that there was a common law power to assist a foreign insolvency, although the power could not be used to enable foreign liquidators to do something that they could not do under the law of the liquidation under which they were appointed.

10 As summarised by Kwan J (as she then was) in Re Beauty China Holdings Ltd [2009] 6 HKC 351.

11 Kam Leung Sui Kwan, personal representative of the estate of Kam Kwan Sing, the deceased v. Kam Kwan Lai & Ors (FACV 4/2015, on appeal from CACV 266/2012, HCCW 154/2010).

12 Shandong Chenming Paper Holdings Limited v Arjowiggins HKK 2 Limited (HCMP 3060/2016).

In Hong Kong, where a UK administrator sought assistance from the Hong Kong court in recognising the moratorium created by the administration order in the UK to prevent disposal of the company’s assets, the court concluded that it could not provide the assistance because to do so would be an impermissible extension of common law principles: Hong Kong currently has no procedure analogous to administration in the UK and thus the order was not one that would be available to a Hong Kong office holder.14

In the recent matter of *BJB Career Educational Co Ltd (in provisional liquidation) v. Xu Zhendong*,15 the court noted16 that:

> … in the exercise of its common law powers the Hong Kong Companies Court can order the oral examination of a director of a Cayman Island company in liquidation in the Cayman Islands if satisfied that it is necessary and that it would not infringe the established limitations on the exercise of the power conferred by section 221 [of the Winding Up Ordinance].

That common law power did not contravene Article 96 of the Basic Law, which provides: ‘With the assistance or authorisation of the Central People's Government, the Government of the Hong Kong Special Administrative Region may make appropriate arrangements with foreign states for reciprocal juridical assistance.’

The Companies Court reiterated its view in *Bay Capital Asia*17 that banks should give assistance to foreign liquidators seeking information on receipt of a letter of request, albeit without a Hong Kong court order, having satisfied themselves that the liquidators have been appointed by the court of the place of the company’s incorporation.

The continued line of decisions shows that to the extent established common law principles require the Hong Kong court to recognise foreign liquidators, it is both prepared and willing to provide assistance to them.

**iii Bank resolution regime**

In the wake of the recent global financial crisis, the Financial Stability Board was tasked with developing a robust approach to allow systemically important financial institutions to fail safely.

Given Hong Kong’s status as an international financial centre and a Financial Stability Board member jurisdiction, the Financial Institutions (Resolution) Ordinance was enacted by the Legislative Council on 22 June 2016 and its commencement date was designated as 7 July 2017 (with the exception of certain provisions, which require the finalisation of additional rules).

The Ordinance is intended to establish a cross-financial sector resolution regime that is designed to strengthen the resilience of Hong Kong’s financial system and operates in the banking, insurance and securities and futures sectors.

The Hong Kong Monetary Authority, the Insurance Authority and the Securities and Futures Commission are given powers as resolution authorities, including the powers to: impose a write off or conversion of capital instruments issued by authorised institutions;

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16 Ibid at Paragraph 7.
17 *Bay Capital Asia LP v. DBS Bank (Hong Kong)* Ltd [2016] HKEC 2377.
resolve a holding company or group company of an entity within scope; and give effect to a resolution action taken by an overseas counterpart. Where a failing financial institution operates across more than one sector, one of the authorities will coordinate resolution as lead resolution authority.

Various stabilisation options are provided under the Ordinance, which the relevant resolution authority can apply individually or in combination, broadly: transfer of the failing financial institution, or some or all of its business, to a commercial purchaser, a bridge institution or asset management vehicle; statutory bail-in; and, as a last resort, taking the institution into temporary public ownership (involving the use of public funds).

Where a resolution process is cross-border in nature, a key question is whether foreign jurisdictions will recognise each other’s resolutions. The Ordinance provides for recognition to give effect to measures adopted by the foreign authority and supportive measures by the Hong Kong authorities to support the resolution action being taken by the foreign authority.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

i Schemes of arrangement

A foreign compromise does not necessarily discharge a debt unless it is discharged under the law governing the debt. In a creditors’ scheme purporting to vary contractual rights, the effectiveness of the scheme may require that the debtor seeks not only the sanction of the court in its jurisdiction of incorporation but also of the courts in the jurisdictions that govern its contractual debt obligations, to ensure that dissenting creditors cannot enforce their claims against the debtor company in jurisdictions other than that of its incorporation.18

Recent examples of schemes are becoming increasingly cross-border in nature given the mix of creditor constituencies involving bank debt as well as bonds subject to, for example, New York law. The result increasingly requires parallel schemes in Hong Kong, the relevant offshore jurisdiction (such as Bermuda, the Cayman Islands or British Virgin Islands, where companies listed in Hong Kong are frequently incorporated) together with Chapter 15 recognition in the United States, with a view to ensuring that claims in all relevant jurisdictions are extinguished.

Kaisa Group Holdings Limited

Kaisa Group is one of the leading Chinese real-estate property developers listed on the Hong Kong Stock Exchange, with interest-bearing borrowings in the billions of dollars, and has borrowings in China and offshore, through a mixture of bank and bond debt. Its default is the first time that a major property company operating exclusively in the PRC has defaulted on its offshore debt. Schemes of arrangement were sanctioned in both Hong Kong where Kaisa was listed and the Cayman Islands where it was incorporated; and the United States Bankruptcy Court for the Southern District of New York provided recognition of the scheme of arrangement proceedings then pending before the High Court of Hong Kong under Chapter 15 of Title 11 of the United States Code.

18 See Re Drax Holdings Ltd [2004] 1 WLR 1049.
Lehman Brothers

In the Lehman Brothers liquidations in Hong Kong, schemes of arrangement have recently been used to help accelerate the liquidation process.

One scheme was proposed with the objective of reducing the company’s creditor constituency and thereby simplifying its liquidation and reducing costs, providing for the full and final discharge of the scheme claims by the scheme creditors in return for them receiving a payment that, together with the interim dividends in the past, will give them the anticipated total recovery (calculated on a best-case basis) much earlier than if the liquidation were to continue without the scheme.

At the sanction hearing, the key legal issue was whether (moving on from Garuda) it is permissible to have a scheme of arrangement between an insolvent company and only some (i.e., not all) of its unsecured creditors, having regard to the principle of pari passu distribution in insolvency law. The liquidators relied on English and Hong Kong authorities to the effect that a scheme of arrangement can be used to achieve a departure from the pari passu principle in a liquidation and, although all creditors in a class must have similar rights, not all creditors with similar rights have to be joined in a class, notwithstanding the insolvency of the debtor.

Another addressed the uncertainties and litigation risk in connection with questions of payment priority with regard to post liquidation interest, matters forming the basis for many months of court time in the English ‘Waterfall’ cases.

Both schemes operated to impose a cut-off date by which creditors must, if not already admitted in the relevant company’s liquidation, submit claims against it, failing which they would be barred from participating in the scheme or the liquidation.

ii Addressing Legend

Z-Obee

Since the Legend decision, the general view has been that Hong Kong law does not strictly allow ‘soft touch’ provisional liquidation to restructure a company. Rogers VP pithily noted that ‘… [t]he power of the court … is to appoint a [provisional] liquidator … for the purposes of the winding-up not for the purposes of avoiding the winding-up … Restructuring a company is an alternative to a winding-up’.

In an ongoing restructuring case, the initial appointment of Hong Kong provisional liquidators (PLs) to Z-Obee, a Bermuda-incorporated company listed in Hong Kong, satisfied the ‘jeopardy to assets’ test of Legend but that state of affairs disappeared following their appointment.

The patience of the Hong Kong court began to wear thin with the company’s lengthy status in provisional liquidation for the, now sole, purpose of restructuring through a white knight investment and a battle to convince the Hong Kong Stock Exchange to allow a resumption of trading, which is inconsistent with Legend.

19 For example: HCMP 2762/2015; and [2017] HKCFI 203.
21 For example: [2017] UKSC 38.
22 [2006] 2 HKLRD 192.
23 Ibid at paragraph 36.
The Hong Kong judge was asked to adjourn the winding-up hearing further, whereafter the appointment of soft touch PLs was sought in Bermuda, with a subsequent discharge of the Hong Kong PLs and their appointment in Bermuda recognised in Hong Kong, allowing them to continue with the proposed restructuring and mitigating the impact of Legend.

The Companies Judge also directed the parties to consider how the recent Guidelines for Communication and Cooperation between Courts in Cross-Border Insolvency Matters formulated by the Judicial Insolvency Network could potentially be applied in this case. The guidelines aim to enhance the efficiency in the administration of parallel insolvency proceedings by establishing a framework for close cooperation between courts of different jurisdictions.

V INTERNATIONAL

i UNCITRAL Model Law

The United Nations Commission on International Trade Law (UNCITRAL) adopted the Model Law in light of the increasing incidence of cross-border insolvencies; and because national insolvency laws were recognised to have limited provision for cases of a cross-border nature, resulting in inconsistent legal approaches.

Currently, there is no statutory provision empowering a Hong Kong court to render assistance to a foreign court in an insolvency matter, as Hong Kong has not adopted the Model Law in its domestic legislation, or any other legislation to similar effect (except with regard to certain aspects of arbitration).

ii The Hong Kong courts’ approach

The approach taken by the Hong Kong courts to cross-border insolvencies has been pragmatic. There is increasing acknowledgement of the need for courts from different jurisdictions to assist one another where possible and to address the common law recognition of foreign liquidators (see Section III, supra).

The Hong Kong courts have a broad jurisdiction to wind up companies in Hong Kong. This extends not only to companies that are incorporated in Hong Kong, but also to overseas companies registered in Hong Kong and unregistered companies, providing certain requirements are met.

In the Lehman Brothers liquidations, where there are a number of office holders in different countries, the Hong Kong liquidators of certain key affiliates were instrumental in implementing a cross-border protocol for dealing with information sharing and creditor resolution proposals.

VI FUTURE DEVELOPMENTS

i Corporate rescue procedure

Notably absent from the Amendment Ordinance is any provision for some form of statutory corporate rescue procedure.

Recently, the Hong Kong Financial Services and the Treasury Bureau indicated that their target is to table a bill to the Legislative Council in 2018 for the introduction of a statutory corporate rescue procedure and insolvent trading provisions.24

I Overview of Restructuring and Insolvency Activity

The Indian economy is growing at a fast pace and studies suggest that India will remain the fastest-growing G20 economy. Despite the shock of demonetization, the real GDP growth of India has been projected to be between 6.75–7.5 per cent in financial year 2017–2018 as against a real GDP growth of about 7 per cent in 2016–17. Though the cash squeeze created due to demonetization impacted the growth of India’s GDP, reducing it by 0.25 to 0.5 per cent during 2016–17, reports state that these effects will disappear once the currency circulation normalises. The government is also coming up with mechanisms and key reforms, including the effective implementation of a goods and services tax (GST) with effect from 1 July 2017, which would bring in a unified tax for the entire nation, thereby replacing multiple indirect taxes such as VAT, service tax, luxury tax etc. Implementation of the GST would cascade the effect of tax on tax, thereby improving the competitiveness of the goods and services, which would result in improving the GDP rate of the economy. The GST would also decrease unhealthy competition among the states, which arose due to multiple taxes and would improve the ease of doing business in India.

On the banking front, a recent report by the Reserve Bank of India (RBI) which is India’s central banking institution, states that the Indian banking sector is well regulated and the financial and economic conditions of India are currently on a par with the rest of the world. The Indian banking system consists of 27 public sector banks, 26 private sector banks, 46 foreign banks, 56 regional rural banks, 1,574 urban cooperative banks and 93,913 rural cooperative banks, in addition to cooperative credit institutions. A report from ICRA (a leading rating agency) estimates that the sector’s credit growth will increase by 7–8 per cent in financial year 2017–18. The report also states that Indian banks have withstood the global downturn and are generally resilient. Furthermore, in line with international banking standards the majority of the banks have complied with the capital requirements of Basel III, while most banks have put in place the framework for asset-liability match, credit and derivatives risk management. According to a report published by the India Brand Equity Foundation (IBEF), the total assets in the banking sector have increased at a compound annual growth rate of 7.61 per cent from financial year 2013–16, from US$1.57 billion in 2013 to US$1.957 billion in 2016. Though the asset base of the banks has increased, one of the major problems being faced by the banking sector is the rising number of non-performing assets (NPAs), which is a result of continued deterioration in the quality and resulting profitability of the assets. Maintaining a high asset quality ratio (AQR) has always been essential for the banks. However, over the

1 Alok Dhir is the managing partner of Dhir & Dhir Associates.
past year it has been difficult, owing to a special inspection made by the RBI, whereby it noticed that some of the banks were under-reporting their NPAs and their asset classification practices were insufficient. The NPA level has gone up drastically from 2618.43 billion rupees from FY 2014-15 to 6974.09 billion rupees by 31 December 2016. Further, the RBI noticed that the banks were hiding bad assets as part of forbearance (the temporary postponement of mortgage payments). As a result, the RBI has come up with stricter norms for asset provision.

i  Liquidity and state of financial markets
After the RBI inspection, the disclosure and standard assets provisioning requirements were tightened by the RBI as part of a proactive approach in resolving stressed assets, which is presently a huge challenge to the banking sector.

Due to the deterioration in asset quality and profitability, the risk to Indian banks has increased and the banking stability indicator (BSI) has gone down drastically, resulting in the introduction of Basel norms pertaining to NPAs, forbearance, disclosures and adoption of IFRS 9.

The dip in the BSI acts as a warning to the banks against an increase in the number of non-performing assets. Further, the substantial transition in Indian accounting standards is posing challenges for Indian banks to maintain a higher amount of provisioning in case of non-performing and stressed assets.

ii  Impact of specific regional and global events
The growth and profitability of domestic Indian entities is being affected by the volatility in global markets, fluctuations in prices of commodities such as agricultural produce, oil and metal, etc. Apart from these factors, geopolitical factors, such as the slowdown in China, the debt crisis in Europe, and ‘Brexit’ have also affected the Indian markets.

Brexit, which decided the exit of UK from European Union in June 2016, has come more as a surprise to the markets than the setback for growth prospect and has led to speculation that other Member States may follow the same path as that of the UK. Brexit has already moved the foreign exchange markets towards a stronger euro whereas the pound has fallen by slightly more than 10 per cent against the rupee.

While Indian companies with heavy UK investments have started to be affected by the weakening of the UK economy, manufacturing set-ups in the UK are worried about possible restrictions that may be imposed on the free movement of goods and services to and from the UK and the EU. The data provided by the Ministry of Commerce and Industry shows that India’s bilateral trade with the UK was worth US$14.02 billion in the financial year 2015–2016, of which US$8.83 billion was exports and US$5.19 billion was imports. With Brexit the trade position of India with UK would strengthen as the EU will have to rework its negotiation strategy to gain access to the UK market.

iii  Market trends in restructuring procedures and techniques
The continued deterioration in the asset quality and profitability has led to the rise of restructuring of corporate loans in India, which is a cause of concern for the banking sector and for the economy as a whole.

Over the past few years the RBI’s approach has been to strengthen the banking sector by undertaking measures aimed at enhancing credit discipline, improving asset quality issues, encouraging market access, adopting a proactive approach for recognising stressed assets and devising a mechanism for taking appropriate actions. In order to tackle the challenges faced
by the commercial banks with respect to stressed assets, the RBI came up with a corporate
debt restructuring (CDR) mechanism with the objective of amicably and collectively
evolving policies and guidelines for working out debt restructuring plans in the interests of
all concerned.

The RBI also issued guidelines for restructuring of debts by way of constituting a joint
lenders forum (JLF) and formulating a corrective action plan (CAP) with the consent of the
majority of the JLF members. In addition, it introduced a flexible financing scheme that
allowed banks to extend long-term loans of up to 25 years in line with the cash flows of
projects while refinancing them every five or seven years (the 5:25 scheme).

The RBI also promulgated the strategic debt restructuring mechanism (SDR), which
permitted lenders to convert their debt into equity and take a controlling stake in the borrower
company. The bank also came up with a new concept of sustainable restructuring by slightly
modifying the concept of the SDR and the guidelines for this new concept are commonly
known as the ‘scheme for sustainable structuring of stresses assets’ (S4A).

The most recent development in the Indian restructuring regime has been the enactment
of the Insolvency and Bankruptcy Code 2016 (the IBC 2016). The IBC 2016 came into effect
from 1 December 2016 and provides for the maximisation of the value of assets, promotes
entrepreneurship, the availability of credit, and balances the interests of all stakeholders by
consolidating and amending the laws relating to the reorganisation and insolvency resolution
of corporate persons, partnership firms and individuals in a timely manner.

iv Number of restructuring procedures entered into or exited

As per the latest performance report of the CDR cell, as at 31 May, 2017, the data pertaining
to the number of references received, approved and rejected has been provided below:

<table>
<thead>
<tr>
<th>No. of cases</th>
<th>Aggregate debt (billion rupees)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total references received</td>
<td>656</td>
</tr>
<tr>
<td>Rejected before approval</td>
<td>125</td>
</tr>
<tr>
<td>Total approved</td>
<td>531</td>
</tr>
<tr>
<td>Successfully exited</td>
<td>103</td>
</tr>
<tr>
<td>Implemented</td>
<td>150</td>
</tr>
<tr>
<td>Under-implementation</td>
<td>-</td>
</tr>
<tr>
<td>Withdrawn on package failure</td>
<td>278</td>
</tr>
</tbody>
</table>

The CDR mechanism has not yielded the desired level of success, as is evident from the
increasing number of failed cases seen above.

A total of 10 cases have been filed under the S4A mechanism of which two proposals
have been approved while the remaining cases are under scrutiny.

From the date of enactment of the IBC 2016, a total of approximately 150 cases have
been submitted by the respective adjudicating authority (AA) and more and more new cases
continue to be filed each day.

II GENERAL INTRODUCTION TO THE FORMAL INSOLVENCY AND
RESTRUCTURING PROCEDURES

Prior to the commencement of the IBC 2016, the legislative framework in India to deal
with the insolvency and restructuring procedures of corporate entities, partnership firms and
individuals was comprised of multiple laws, namely, the Companies Act 1956 (substituted by Companies Act 2013), the Sick Industrial Companies (Special Provisions) Act 1985, the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002 (SARFAESI Act), and the Recovery of Debts due to Banks and Financial Institutions Act (RDBIFI Act) 1993, etc. The presence of multiple forums and complexities resulted in delays in the timely resolution of the distressed entities, partnership firms or individuals, which further led to the devaluation of the assets of the borrower, making insolvency negotiations redundant.

The enactment of the IBC 2016 paves the way for the complete overhaul of the insolvency and bankruptcy mechanism in India by integrating the laws dealing with insolvency and bankruptcy, thereby providing greater clarity.

i  Formal procedures

**The Companies Act 2013**

Chapter XV of the Companies Act 2013 provides for various measures, including schemes of reconstruction, takeovers, mergers, demergers, transfer of undertakings and restructuring of debts by way of which the liabilities of the distressed companies can be restructured. The Act contains the relevant provisions for the compromises, arrangements and amalgamations between a company and its creditors or members. Salient provisions of Chapter XV are summarised below.

Where a compromise or arrangement is proposed between a company and its creditors, or between a company and its members, the National Company Law Tribunal² (Tribunal) has jurisdiction and may, on an application filed by the company or any of its creditor or member (or in the case of a company that is being wound up, of the liquidator appointed under this Act or the IBC 2016, as the case may be) order a meeting of the creditors, or of the members (as the case may be) to be called, held and conducted in such manner as the Tribunal directs. If a proposal is agreed to by 75 per cent or more of the value of the creditors or members and if the same is sanctioned by the Tribunal, it shall be binding on the company, all the creditors or members or in case of a company being wound up, on the liquidator.

The Tribunal would, however, not sanction any scheme of compromise or arrangement unless such scheme is accompanied with a certificate from the company’s auditor stating that the scheme conforms with the applicable accounting standards and unless it is satisfied that all material facts relating to the company and the scheme have been disclosed and all other procedural requirements, such as convening a creditors meeting, have been complied with.

If the Tribunal reaches the conclusion that the compromise or arrangement cannot be implemented in toto and the company will not be able to pay its debts as per the scheme sanctioned, it may order that the company be liquidated.

Further, in the case of fast-track mergers, which involves the merger of two or more small companies, or between a holding and its wholly owned subsidiary or such other company as may be prescribed, the approval of the Tribunal is not required and the scheme needs to be approved by 90 per cent of shareholders and 90 per cent of creditors in value.

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² The tribunal of the state in which the registered office of the company is situated.
The IBC 2016

The IBC 2016 has brought a paradigm shift in the legal framework of dealing with the insolvency and bankruptcy situation in India. The code has consolidated the laws relating to the insolvency and bankruptcy of companies, limited liability entities, unlimited liability partnerships and individuals.

Prior to the enactment of the IBC 2016, the legislations stated in Section II, supra were largely in favour of the debtor as the debtors remained in possession and control of the assets they provided as security to its lenders, with restrictions on the disposal of such assets.

The IBC 2016 has shifted the focus from the ‘debtor in possession’ to a ‘creditor in possession’ regime, wherein the creditors of the corporate debtor, through their appointed interim resolution professional or resolution professional (IRP or RP), remain in control of the assets of the corporate debtor from when the application is submitted by the AA until such time as the resolution plan is sanctioned by the AA. Further, until the approval of a resolution plan by the AA, the company is run and controlled by the RP whereas any decision to be made during the corporate insolvency resolution process (CIRP) of the corporate debtor should be agreed by 75 per cent or more of the members of the committee of creditors (COC) constituted under the provisions of the IBC 2016.

The IBC 2016, empowers any creditor of a corporate debtor, irrespective of it being a financial or operational creditor or secured or unsecured creditor, or the corporate debtor itself, to make an application before the AA to initiate a CIRP against a corporate debtor, at their discretion, in the event of there being a default by the corporate debtor in payment of their dues for an amount of 100,000 rupees or more.

The CIRP process is initiated immediately upon submission of the application by the AA and an IRP is appointed, who acts on behalf of the creditors of the corporate debtor. The IRP or RP is required to manage and run the entire CIRP, which involves the following major steps:

1. making a public announcement inviting claims from the stakeholders of the corporate debtor;
2. making an appointment for two registered valuers to carry out the valuation to determine the liquidation value of the assets of the corporate debtor;
3. verifying the claims and constitution of the COC;
4. calling for a meeting of the COC and subsequently submitting an information memorandum along with the valuation reports to invite expressions of interest from potential resolution applicants;
5. analysing the resolution plan submitted by resolution applicants and presenting the same before the COC for obtaining their necessary approval; and
6. submitting the approved resolution plan before the AA for its approval, prior to completion of the CIRP period.

In addition, the IRP or RP would undertake the following tasks:

1. managing the affairs of the corporate debtor on a going concern basis;
2. collecting information relating to the assets, finances and operations of the corporate debtor in order to determine its financial position;
3. taking control and custody of the assets of the corporate debtor;
4. receiving and collating all the claims submitted by the creditors; and
5. constituting a COC; and
f running the complete CIRP and, if any discrepancy or difficulty is encountered due to any action or inaction of the corporate debtor or any key personnel of the corporate debtor, approaching the AA with an application seeking the appropriate direction.

The CIRP, as detailed above, shall be completed within a period of 180 days from the date of submission of the application by the AA to initiate such process. However, if the AA is satisfied that in a particular case the CIRP cannot be completed within the specified time of 180 days, the AA may extend the time period by not more than 90 days, which shall not be granted more than once during the CIRP.

If the CIRP is not completed within a period of 180 days (extendable by 90 days), the AA shall order the corporate debtor’s liquidation wherein the RP shall become the liquidator and shall continue to run the liquidation process. Apart from liquidation under the circumstances mentioned herein, the AA may also call for the liquidation of the corporate debtor if the RP communicates the decision of the COC to liquidate the corporate debtor even during the CIRP to the AA.

Immediately upon submission of an application by the AA under the provisions of IBC 2016, a moratorium is declared thereby restraining continuation of the following against the corporate debtor:

- coercive recovery proceedings, including: suits; execution of any judgments, decrees or orders in any court of law, tribunal or other authority against the corporate debtor;
- restriction on transfer, encumbrance, alienation or disposal by the corporate debtor of any of its assets or any legal right or beneficial interest therein; and
- prohibition on any action to foreclose, recover or enforce any security interest created by the corporate debtor in respect of its property including any action under the SARFAESI Act.

The CIRP proceedings also helps lenders to recognise the need for a corporate debtor’s operational and financial restructuring, which is supported by all stakeholders leading to minimisation of losses in recovering the dues. The immediate impacts of initiating CIRP under the IBC 2016 are as follows:

- the business operations of the corporate debtor are not affected and are continued on a going concern basis even during the CIRP by the IRP or RP;
- the appointment of an insolvency professional (IP), an independent professional, to oversee the CIRP brings a transparency to the whole process that is not subject to scrutiny or investigation by the lenders;
- since the IP would invite resolution plans from prospective resolution applicants, better restructuring options may emerge that would maximise the value for creditors and would revive the corporate debtor in a better way; and
- the moratorium from proceedings under any other law during the CIRP would provide more time to refine the resolution plan on the basis of views from various stakeholders.

ii Winding up

Section 271 of the Companies Act 2013, states the circumstances under which a corporate debtor can be wound up by the Tribunal, on grounds apart from its inability to pay debts, and these are as follows:

- the company has, by a special resolution, resolved that the company be wound up by the Tribunal;
if the company has acted against the interests of the sovereignty and integrity of India, security of the state, friendly relations with foreign states, public order, decency or morality;

c if on an application made by the registrar or any other person authorised by the central government by notification under the act, the Tribunal is of the opinion that the affairs of the company have been conducted in a fraudulent manner or the company was formed for fraudulent and unlawful purpose or the persons concerned in the formation or management of its affairs have been guilty of fraud, misfeasance or misconduct in connection therewith and that it is proper that the company be wound up;

d if the company has failed to file its financial statement or annual returns with the registrar for the five consecutive financial years immediately preceding; or

e if the Tribunal is of the opinion that it is just and equitable that the company be wound up.

Further, the IBC 2016 also provides for the voluntary liquidation of a solvent corporate debtor, subject to the following:

a a declaration is provided by a majority of individuals constituting the governing body of the corporate, or by a majority of designated partners in case of a limited liability partnership for the liquidation;

b an affidavit is provided along with the declaration, verified by such majority of persons as stated above and stating that:
• a full inquiry has been made into the affairs of the corporate person and they have formed an opinion that either the corporate person has no debt or that it will be able to pay its debt in full from the proceeds of the assets sold in liquidation; and
• the liquidation is not in order to defraud any person.

The SARFAESI Act

Apart from the above-stated legislation, the provisions regarding resolution of debt through an asset reconstruction company are contained under the SARFAESI Act, which also deals with foreclosure and aims to enable secured lenders to realise long-term assets, manage problems of liquidity, asset liability mismatches and improve recoveries by exercising powers to take possession of securities, sell them without the intervention of the court, and reduce NPAs by adopting measures for their recovery or reconstruction.

Under the SARFAESI Act, any secured creditor may enforce the security interest created in its favour without the intervention of a court by following the provisions of the said Act. Upon event of default by the borrower and its consequent classification of the account, maintained with the secured creditor, as NPA, the secured creditor may require the borrower to discharge its liabilities in full within 60 days by giving a notice to that effect, failing which the creditor is entitled to exercise all or any rights as conferred under Section 133 of the said Act.

Upon receipt of the notice, the borrower is restrained from selling, transferring, or leasing the secured assets mentioned in the notice without the consent of the secured lender.

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3 The lender may take possession of the secured assets or the management of the borrower’s business and also have the right to transfer same by way of lease, assignment or sale.
However, where a CIRP has been initiated against the borrower, a moratorium restraining all proceedings under the SARFAESI would apply immediately upon submission of an application by the AA to initiate a CIRP against the borrower.

**The RDDBFI Act**

The provisions of RDDBFI are solely directed to enable the banks and financial institutions to recover their debt quickly and efficiently, through the debt recovery tribunals (DRTs) under the aegis of the RDDBFI Act.

Under Section 19 of the RDDBFI Act, banks and financial institutions can file suits for recovery of their dues, known as original applications. After the evidence is presented and recorded, final arguments are heard and if all is in order, a decree is passed in favour of the banks and financial institutions.

### iii Informal procedures

There are several non-statutory informal mechanisms promulgated by the RBI that provide guidelines for carrying out the restructuring of debts, namely: bilateral restructuring; CDR; the JLF; a flexible restructuring scheme; an SDR; change of management outside of an SDR; and the S4A.

The stressed entity may enter into a bilateral restructuring agreement with the lender bank or may undergo CDR, a non-statutory and voluntary mechanism that allows a financially distressed company with two or more lenders and a minimum debt size of 100 million rupees the option to restructure its debts with the consent of 75 per cent or more (of the value of the debt) and 60 per cent consent in terms of the number of lenders. The legal basis for the CDR mechanism is comprised of debtor-creditor agreements (DCAs) and inter-creditor agreements (ICAs) wherein debtors are required to execute a DCA and abide by the terms of such DCA and the lenders are required to execute an ICA that is legally binding on all the lenders.

Another tool in the RBI’s armoury for restructuring of debts is the formation of a JLF wherein the lenders are mandatorily required to constitute a JLF, if the repayment of the principal or interest of an account reported to the central repository of information on large credits (CRILC) is overdue by 61–90 days and the aggregate exposure of the lenders in that account is 1 billion rupees and above. The lenders can also constitute a JLF, if the aggregate exposure in an account is less than 1 billion rupees, provided the principal or interest payment is overdue for a period not exceeding 61–90 days.

If a JLF is constituted, a credible and independent scrutiny of the expected future cash flows is conducted and if the cash flows are found not to support the current level of debt, schemes such as an SDR, recovery or rectification process are initiated as an early measure to save the account from turning into a NPA.

The flexible restructuring scheme enables banks to lend and restructure the debt extended to infrastructure and core industries for a longer period of, for example, 25 years with an option of refinancing the same every five years.

With the objective that the shareholders should bear the first loss instead of the lenders, the RBI has come up with another restructuring tool called ‘strategic debt restructuring’, by which the lenders are able to convert the entire or a portion of their debt into the borrower’s equity and, thereafter, transfer the same in favour of a ‘new promoter’ within a specified period.
The S4A provides for the restructuring of a sustainable loan from an unsustainable loan. A sustainable level of debt is one that, according to the banks, can be serviced by the borrower with its current cash flows. However, the sustainable level of debt should not be less than half the loans or funded liabilities of the borrower. The unsustainable portion of debt can be converted by the banks into equity or equity-related instruments, which are expected to yield an increase in their investments in the future.

iv Clawback actions

With regard to preferential, undervalued or extortionate credit transactions or any other transactions that have the effect of defrauding the creditors, if entered into by the corporate debtor during the relevant time (a period of two years in the case of a transaction with related parties and a period of one year in other cases), the RP may file an application before the AA for appropriate orders, including reversal of such transactions.

The IBC 2016 defines ‘transactions’ as: a transfer of property or an interest thereof of the corporate debtor for the benefit of a creditor or a surety or a guarantor for or on account of an antecedent financial debt or operational debt or other liabilities owed by the corporate debtor that have the impact of putting such creditor or a surety or a guarantor in a more beneficial position than it would have been in the event of a distribution of assets; gifts to a person; undervalued transactions and extortionate credit transactions.

The provisions of the SARFAESI Act provide that once a secured creditor has issued a notice under Section 13(2), a suo moto restraint becomes applicable on the transfer of the secured assets by sale, lease or otherwise and any attempt to enter into transactions in respect of such secured assets of the company can be annulled by the appropriate court of law.

However, any other transaction entered into by a company in financial distress in the normal course of business or activities is otherwise not susceptible to any limitation, unless there is a restraining order to that effect.

III RECENT LEGAL DEVELOPMENTS

Sections 7, 9 and 10 of the IBC 2016 provide for the submission or rejection of an application by the AA within 14 days of the date of receipt of application. However in JK Jute Mills Company Limited v. Surendra Trading Company vide its order dated 1 May 2017 the Tribunal held that the time limit of 14 days is advisory and not mandatory.

Recently, the amendment in the Banking Regulation Act 1949 has empowered the RBI to issue directions to the commercial banks in regard to the resolution of stressed assets. Pursuant to this amendment, the RBI identified 12 big corporate defaulters and issued directions to the concerned tribunals to take them up as a priority. The said amendment was, however, challenged in one of the cases before the Gujarat High Court, and subsequently, the RBI has modified the amendment to the extent that it can only empower itself to identify the major defaulters.

Further, to make the procedure under the IBC 2016 more effective, the regulations for the Insolvency and Bankruptcy Board of India (Fast Track Insolvency Resolution Process for Corporate Persons) Regulations, 2017 were notified on 16 June 2017 to expedite the resolution process of default in cases of small companies or start-ups or unlisted companies with total assets not exceeding 10 million rupees in the preceding financial year, within 90 days (as compared to 180 days in case of a normal CIRP), which may be extended by 45 days once during the CIRP is fast-tracked, if the AA is satisfied.
Under the fast-track process, a creditor or a corporate debtor may file an application (along with the proof of existence of default) with the AA for initiating the fast-track resolution process. After the application is submitted, an IRP is appointed, who, if based on the records of the corporate debtor, is of the opinion that the fast-track process is not applicable to the corporate debtor, shall file an application before 21 days have expired from the date of his or her appointment with the AA requesting for an order to convert the fast-track process into a normal CIRP.

On 1 April 2017 the Ministry of Corporate Affairs notified the Insolvency and Bankruptcy Board of India (Information Utilities) Regulations 2017 pertaining to the establishment and role of information utilities. The Regulations state that the main role of an information utility is as follows:

\[ a \] acts as a data storage entity that collects information from various sources and stores it in an electronic format in a safe and secure manner;

\[ b \] ensures that when information is uploaded about the (pending) financial liabilities of registered users, such information is verified by all necessary parties to ensure its authenticity. Once verified, the information utility shall provide the status of the information to its registered user, which shall assist the user in completing the process under the IBC 2016 on time; and

\[ c \] solves the problem of discovering and disclosing the true nature of the borrower’s financial liabilities to its various creditors.

The Regulations provided further information on the person or persons eligible for registration as an information utility:

- a publicly limited company with a minimum net worth of 500 million rupees;
- control should not be with any person resident outside India;
- no person resident outside India should hold more than 49 per cent of its voting power or paid-up equity capital; and
- promoters, directors, key managerial personnel and persons holding more than 5 per cent paid-up equity share capital or total voting power must be fit and proper.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

Upon coming into force, more than 240 cases have been submitted by the AA for initiation of a CIRP and more and more cases continue to be filed each day. Of the cases submitted for initiation of a CIRP, most are within the iron and steel sector, followed by the power and infrastructure sector and hospitality sector. However, it is expected that cases referred for CIRP under the IBC 2016 would get resolved within the timeline stipulated, which would result in a healthy restructuring of the corporate debtors with genuine business viability, and compulsory liquidation where restructuring is not possible, while maximising the value of the security of the creditors involved.

One of the key developments in the IBC 2016 has been the withdrawal of the cases from the AA pursuant to the settlement between the corporate debtor and its creditors. The provisions of the IBC 2016 envisage resolution of the debt of the corporate debtor during the CIRP and do not provide for withdrawal of the application once the application is submitted by the AA. However, in Lokhandwala Kataria Construction Private Limited v. Nisus Finance and Investment Managers LLP the Supreme Court vide its judgment dated
24 July 2017 exercised its power under Article 142 of the Constitution and permitted a withdrawal of the case while recording the consent terms between the corporate debtor and its creditors. The said judgment has set a new precedent as it overrides the provisions of the IBC 2016, which do not provide for withdrawal of a case after it has been submitted by the AA.

V INTERNATIONAL

India has not adopted the UNCITRAL model law. However, a company incorporated in a foreign country and with its office and assets in India may be wound up as an unregistered company under the provisions of Sections 375–376 of the Companies Act 2013, and, while foreign liquidation is pending, would not affect the jurisdiction making winding-up orders. Further an Indian company may enter into restructuring of its foreign debts with foreign lenders on a bilateral basis, provided the provisions relating to Foreign Exchange Management Act 1999 have been complied with along with any other RBI procedures.

The law for the recognition of foreign judgments and proceedings is contained in Sections 13 and 44A of the Code of Civil Procedure (CPC), which consider foreign judgments in reciprocating territories as conclusive, barring certain exceptions, such as fraud or the judgment not being based on the merits of the case. However, a judgment-debtor can only resist the decree-holder by raising any of the grounds under Section 13 of the CPC.

If the decree is from a court in a non-reciprocating foreign territory, a party has to file a fresh civil action suit on that foreign decree, or on the original underlying cause of action, or both, in a domestic Indian court of competent jurisdiction and, at the same time, ensure that the parameters of Section 13 of the CPC are met. If a foreign decree falls under the limitations subscribed by Section 13 of the CPC, it is not regarded as conclusive as to the matter thereby adjudicated upon. A decree, whether from reciprocating or non-reciprocating territory, that follows a judgment that is not on merits cannot be enforced in India.

Though the provisions of the IBC 2016 do not have any extraterritorial jurisdiction and are not applicable to companies incorporated outside India, Section 234 states that the central government may enter into an agreement with the government of any country outside India for enforcing the provisions of the IBC 2016. The IBC 2016 further states that the central government may, by way of notification in the official gazette, apply its provisions against a corporate debtor in respect to assets or property, including the personal guarantor of a corporate debtor, situated at any place outside India with which reciprocal arrangements have been made, subject to such conditions as may be specified. In such a case the AA may issue a letter of request to a court or any competent authority of such country to deal with its request.

VI FUTURE DEVELOPMENTS

To date, the nodal agency for implementing the insolvency and bankruptcy law has notified the regulations pertaining to insolvency and bankruptcy of companies and it proposes to notify and implement the regulations pertaining to the insolvency and bankruptcy of individuals and partnership firms by the end of fiscal year 2017–18.

The provisions for insolvency and bankruptcy of individuals and partnership firms would apply where the amount of default is not less than 1000 rupees or such other amount as specified by the central government but not exceeding 100,000 rupees. An insolvency resolution process against a debtor may be initiated by the debtor, either personally or
through a resolution professional, or by the creditor (either personally or jointly with other creditors) by applying to the AA (which is the debt recovery tribunal in case of insolvency for individuals or partnership firms).

The debtor shall prepare a repayment plan in consultation with the RP that would be approved by a three-quarters majority of the creditors in value. The repayment plan would authorise the RP to: (1) carry on the debtor’s business or trade on his or her behalf or in his or her name; (2) realise the assets of the debtor; or (3) administer or dispose of any funds of the debtor and would be implemented under the supervision of the RP.

However, a debtor or a creditor (either individually or jointly) may make an application for bankruptcy of a debtor in case the application for insolvency is rejected by the AA or the repayment plan is rejected by the AA or the repayment plan ends prematurely.

In order to have a comprehensive insolvency and bankruptcy regime in India, the Ministry of Corporate Affairs has come up with the Financial Resolution and Deposit Insurance (FRDI) Bill 2017, which provides for a framework to deal with the bankruptcy of financial sector entities such as banks and insurance companies.

The enactment of the IBC 2016 will prove to be a milestone in the Indian legal framework. Even though the law is in its initial stages, it has provided fresh impetus to the insolvency and reorganisation of financially distressed companies. The IBC 2016 would be better aligned with the best international practices with the introduction of provisions relating to insolvency and bankruptcy for individuals and partnership firms.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

In 2017 Indonesia's economy has improved. The recent Standard and Poor's credit rating upgrade shows improvements of the country's fiscal management and credibility. Economic outlook is positive due to a supportive global economy and strong domestic fundamentals. Private consumption is growing supported by a stable rupiah and muted inflation. Fiscal policy in 2017 has made a strong start, with improved revenue performance and quality of expenditure, supporting economic growth. Private consumption growth has been robust, supported by a stable rupiah and muted inflation. Investment growth continues to be strong on the back of the ongoing recovery in commodity prices, continued reforms to improve the business environment, lower financing rates, and better business sentiment.

In 2017 the government issued various regulations, including the following:

a. On 17 March 2017 the Indonesian Financial Services Authority (OJK) issued Circular Letter No. 12/SEOJK.03/2017, implementing OJK Regulation No. 56/POJK.03/2016 on the Share Ownership in Commercial Banks. This regulation requires any foreign shareholder who intends to own more than 40 per cent of a bank's shares to obtain a recommendation from the supervisory authority of their country of origin.

b. On 27 March 2017 the OJK issued OJK Regulation No. 13/POJK.03/2017 on the Use of Services Rendered by Public Accountants and Public Accounting Firms in Financial Services Activities. This regulation stipulates among others that parties conducting financial services activities are required to use the services of public accountants and public accounting firms that are registered with the OJK. The appointment of the public accountants and public accounting firms will be conducted through a general meeting of shareholders by taking into account a recommendation from the board of commissioners and audit committee.

c. On 6 April 2017 the OJK issued Circular Letter No. 16/SEOJK.03/2017 on the Submission of Information on Foreign Customers Related to Taxes in the Context of International Automatic Exchange of Information (AEoI) by using the common reporting standard (CRS). The regulation requires financial-service institutions, which include commercial banks, securities companies, custodian banks, life insurance companies and sharia life-insurance companies, to report information relating to their foreign customers to the OJK by 2018 at the latest. Foreign customers are individual or corporate customers who satisfy the following criteria: (1) existing customers that fit into the lower (below US$1 million) and upper (above US$1 million) account

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balance-value brackets; and (2) new customers, either from participating jurisdictions or passive, non-financial entities that do not operate within participating entities that do not operate within participating jurisdictions, and that have account balances above US$250,000.

d On 7 April 2017 the OJK issued OJK Regulation No. 14/POJK.03/2017 on Recovery Plan for Systemic Banks. This regulation sets the requirements for systemic banks to prepare and submit recovery plans to the OJK, or within six months after the banks being classified as systemic banks. Systemic banks are also required to have a guideline for the recovery plan, which is prepared by taking into account the governance principle to support the implementation of a recovery plan.

e On 18 April 2017 the OJK issued Circular Letter No. 18/SEOJK.02/2017 on the Information-Technology Governance and Risk Management for Information-Technology-Based Lending Services, which is the implementation of OJK regulation No. 77/POJK.01/2016 on Technology-Based Lending Services. This regulation stipulates requirements for the providers of IT-based lending services (providers) to: (1) place their data centre and disaster-recovery centre within Indonesian territory; (2) prepare an electronic system-strategic plan that supports the company's business plan; (3) prepare a disaster-recovery plan, which must be reassessed at least once a year, and submit the plan to the OJK; (4) implement proper procedures for the management of changes in the business process and electronic system; (5) employ human resources that possess sufficient IT knowledge; (6) if using outsourcing services, providers should apply the principles of prudence, sustainability, and appropriate risk management; and (7) maintain the confidentiality and availability of all personal data, transaction data, and financial data.

f On 5 May 2017, Bank Indonesia issued Regulation No. 19/7/PBI/2017 on Carrying Foreign Banknotes Through Indonesian Customs. This regulation will come into effect as of 5 March 2018. With the issuance of this regulation, as of March 2018 carrying paper banknotes through Indonesian customs within the limit of 1 billion rupiah or its equivalent may only be carried by permitted bodies, namely to banks and non-bank money changers, which have obtained a permit and approval from Bank Indonesia to carry paper banknotes, as well as rupiah processing service companies registered with Bank Indonesia.

g On 8 May 2017, the government issued Government Regulation in Lieu of Law No. 1 Year 2017 on Financial Information Access for Tax Purposes. This regulation is issued to support Indonesia's commitment through AEoI that implements the use of CRS. According to this regulation, the Directorate General of Taxation is authorised to obtain transparent access to financial information stored in financial service institutions such as banking, capital market, insurance, or other financial service institutions for the purpose of taxation.

h On 20 July 217, Indonesia's central bank issued Regulation No. 19/9/PBI/2017 on Commercial Paper Issuance and Transactions in the Money Market. Based on this Regulation, non-bank companies can issue commercial paper maturing in one year or less and trade the notes in the secondary market. The new Regulation will take effect on 4 September 2017.
II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

Formal restructurings are initiated through courts and governed by the Bankruptcy Law Number 37 of 2004 on Bankruptcy and Suspension of Payment (the Bankruptcy Law). The Bankruptcy Law provides an opportunity for borrowers to enter into debt restructuring by applying for a suspension of payment obligations, as well as the option to apply for bankruptcy.

i Payment obligations

Suspension of payment obligations

Both a borrower who has more than one lender and a lender can apply for a suspension of payment obligations. However, it should be noted that for certain lines of business (such as banks), only Bank Indonesia has the right to apply for the suspension of payment obligations. The Financial Services Authority is the only institution that may initiate suspension of payment obligations against security companies the Stock Exchange, the Clearing Guarantee Institution and the Central Securities Depository, while the Minister of Finance will be the only authority that may initiate suspension of payment obligations against insurance and reinsurance companies, pension funds and state-owned enterprises that involve the public interest.

Although there are no mandatory features of a suspension of payment obligations, as mentioned above, the approval of the lenders and the Commercial Court is required before the plan becomes effective.

Formal restructuring will be applicable in respect of both secured and unsecured lenders. Upon receipt of a petition for formal restructuring (voluntary suspension of payment obligation) submitted by a borrower or a lender, the Commercial Court will immediately issue an order for the temporary suspension of payment obligations by the borrower. Following that, the administrator will convene a meeting of lenders to vote on a proposed composition plan, or the conversion of the temporary suspension of payment obligations into a permanent suspension of payment obligations, and the duration of the suspension. The meeting of lenders must be held within 45 days from the date the Commercial Court approved the temporary suspension of payments. The lenders may supervise the implementation of the court decision by granting a permanent suspension of payments for a period that shall not exceed 270 days from the date of the court decision.

The plan must be approved by:

\( a \) more than half of the unsecured lenders present at the meeting who represent at least two-thirds of the total unsecured debts of the lenders who attend the meeting; and

\( b \) more than half of the secured lenders present at the meeting who represent at least two-thirds of the total secured debts of the lenders who attend the meeting.

In the event that the plan is not approved, or the borrower fails to comply with the provisions of an approved plan, the supervisory judge will inform the Commercial Court, which will issue a further order declaring the borrower bankrupt. There is no avenue of further appeal against such a decision.

A suspension of payment cannot be applied for with regard to:

\( a \) secured lender's receivables;
debt incurred and payable in relation to maintenance fees, supervisory fees or school fees. The supervisory judge must determine the total outstanding accounts payable that do not have preferential rights prior to the suspension of payment; and accounts payable with preferential rights.

To ensure that bankruptcy cases are handled efficiently and transparently, the supervisory judge has the authority to request information on ongoing cases from the receivers and oblige the receiver to submit a working schedule at a creditor’s meeting. If the receiver fails to provide information relating to the case after receiving two requests from the judge, or fails to adhere to the working schedule, then the supervisory judge has the authority to:

- summon and request an explanation from the receivers;
- send a written warning to the receivers with copies also being sent to the Association of Receivers and Administrators and the Minister of Law and Human Rights; and
- propose new receivers to the panel of judges in the Commercial Court.

Management during suspension of payment obligations

During a suspension of payment obligations, all corporate actions must be conducted jointly by the administrator and borrower, and liabilities incurred by the borrower without the approval of the administrator after the suspension of payment can only be imposed on the assets of the borrower as long that they have benefit over the borrower’s assets. A new loan can be obtained provided that it will increase the value of the borrower’s assets. The borrower can also impose its assets with security rights such as a mortgage, fiduciary security or pledge, provided that these assets are free of encumbrances and such action has been approved by the supervisory judge.

Informal restructuring initiatives

Informal restructuring initiatives are implemented out of court in the following forms:

- reschedule of the terms of payment;
- debt-to-equity swap;
- sale of business; and
- voluntary liquidation of a company.

Reschedule of the terms of payment

Restructuring of only the debt or equity structure is common practice in Indonesia. The general approach is for a company to reschedule debt that it can service, for example, in tranches with a grace period on principal repayment and concessional interest rates. The portion of debt that is not serviceable is normally dealt with in a number of ways, such as subordination, convertible bonds, straight equity conversion, warrants or debt forgiveness.

Rescheduling of the terms of payment is implemented by dividing the outstanding loan into tranches that are either sustainable or unsustainable. Sustainable tranches can be paid over the short term or even in cash. Unsustainable tranches can be paid over a longer period of time. Securities can also be increased to include new securities if necessary, depending on the amount of the outstanding loan.
**Debt-to-equity swap**

This option is usually taken if the borrower is not able to repay its loan but there is a possibility that it will be able to improve its financial condition in the future.

Some of the advantages of debt-to-equity swaps are that the company will be released from interest expenses and the lenders will have the opportunity to receive dividends.

Notwithstanding these advantages, the disadvantages of debt-to-equity swaps include the fact that the lender will lose its rights over the securities and its priority rights because shareholder loans are considered subordinated loans; and that shareholders cannot file a bankruptcy petition against their own company.

It should be noted that the following problems can arise in debt-to-equity swaps:

- **a** if there are restrictions under the regulations in Indonesia for foreign shareholders to hold shares in a particular line of business in accordance with the negative list of investment issued by the government, then a foreign shareholder cannot hold the shares in the company; and

- **b** if the company is a publicly listed company, and the debt-to-equity swap transaction is not approved by the shareholders because the debt-to-equity swap transaction will cause dilution of the existing shareholders.

**Sale of business**

The main objective of such restructuring is to separate or insulate the viable parts of businesses from the non-viable operations of an insolvent company or group of companies. This restructuring can be implemented in a situation where a restructuring within the same legal entity is no longer possible from the lender’s point of view.

**Voluntary liquidation of a company**

There are two types of liquidation in Indonesia: voluntary liquidation by shareholders of a company and a forced liquidation initiated by lenders.

Voluntary liquidation will be adopted by the shareholders through an extraordinary general meeting of shareholders. In a voluntary liquidation, after it is announced by the liquidator in the newspapers, the lenders may have the right to register their claims to the liquidator, and the lenders may also object to the distribution plan proposed by the liquidator. If claims or objections registered by the lenders within a period of 60 days from the date of such announcement have been rejected by the liquidator, the lenders may lodge a civil lawsuit to the relevant district court within a period of 60 days from the date of such rejection. If the lenders have not registered their claim during the liquidation process, they still may lodge their claim to the relevant district court within two years after the closing of the liquidation process, with the condition that there are still remaining assets to be distributed to the shareholders.

All of the workout arrangements explained above can be worth considering by lenders if the borrowers agree to and are cooperative about restructuring their debts, and the lenders will have the opportunity to recover their receivables after the implementation of the transaction.
iii  General issues with restructuring
The gap between the expectations of the borrower and the lender often leads to initial negotiations being slow and unproductive. This is accentuated when the borrower and lender have a history of not trusting or cooperating with each other. In this situation, both parties will often make unrealistic demands that impede useful commercial negotiations.

iv  Enforcement of security
Indonesian security consists of two types:

a  real security rights, which relate to specific assets of a borrower, such as a mortgage on land and a building or hypothec, a vessel, a pledge, a fiduciary transfer and a fiduciary assignment. Real security rights (rights in rem) are absolute rights with the following characteristics:
- they have preference (droit de preference);
- they pertain only to specific property or goods of a borrower;
- they are exercisable against any parties; and
- they follow the encumbered property of goods in the hands of whoever such property or goods may thereafter be in (droit de suite); and

b  personal security rights, which relate to a certain (individual or corporate) party that has agreed to provide security for a borrower's debts, such as in personal or corporate guarantees. Personal security rights (rights in personam) are rights that establish a direct relationship with a specific (individual or corporate) party, and therefore can only be exercised against that party and assets of that party in general. They create no preference with respect to any particular assets.

Except for a mortgage or hypothec and a fiducia security, most security documents are enforced through normal civil proceedings at court, and are preceded by three demand letters served against the grantor of such security.

Enforcement of a mortgage or hypothec and a fiducia security can be done through a public auction or private sale. The parties may choose a private sale if this method will result in the highest price benefiting all parties. A private sale must be announced in two local newspapers at the place of the assets, and the sale can only be conducted one month after such publication and provided that there is no objection from any parties to such intention.

Bankruptcy has no effect on lenders who hold a mortgage, hypothec or fiducia as security (also referred to as secured lenders), except that secured lenders are stayed from enforcing their rights for maximum period of 90 days commencing from the date of the grant of bankruptcy. Once the stay period is lifted, secured lenders are free to enforce their securities, but must do so within two months of the commencement of the state of insolvency or else they will, upon subsequent enforcement of their security, become liable to contribute to the costs of the bankruptcy. The state of insolvency is stipulated in Article 178 Paragraph 1 of the Bankruptcy Law, and will immediately commence when no composition plan has been offered, the composition plan has been rejected or its ratification has been refused by the Commercial Court. Following the state of insolvency, the receiver will distribute the bankrupt estate to the lenders.
Duties of directors of companies in financial difficulties

Indonesian Law Number 40 of 2007 (the Company Law) has made it mandatory for every Indonesian company to have three organs: a board of directors, a board of commissioners and a general meeting of shareholders.

The board of directors is responsible for the management of the company, while the board of commissioners has the duty to supervise the manner in which the board of directors manages the company in the interests of the company. The general meeting of shareholders consists of shareholders of the company, and has the right to appoint and terminate members of the board of directors and board of commissioners. In addition, there are also corporate actions that require the approval of the general meeting of shareholders.

The board of directors is required to perform the following obligations:

- submit an annual report that also contains the financial statement of the company to the general meeting of shareholders within six months after the end of the financial period. Such annual report must first be reviewed and approved by the board of commissioners;
- submit a business plan that also contains the budget plan for the next financial year prior to the commencement of the new financial year, to be approved by the board of commissioners and general meeting of shareholders;
- prepare and maintain a shareholders register and special register of shareholders that record the ownership of shares in the company and in other companies of the members of board of directors and board of commissioners, as well the ownership of shares of their immediate family members;
- maintain the resolutions of shareholders, the board of directors and the board of commissioners, and all other corporate documents;
- call a general meeting of shareholders as necessary or if based on the request of a shareholder, the board of directors or the board of commissioners;
- obtain approval from the general meeting of shareholders before conducting corporate action that requires approval from the shareholders;
- notify the Minister of Law and Human Rights of any change in the composition of the board of directors and the board of commissioners or the shareholders within 30 days from the date of the shareholders’ resolution approving the change;
- record any transfer or pledge of shares in the shareholders’ register;
- notify lenders should there be any reduction in the capital of the company, and publish such notification in at least one newspaper within seven days after the date of the shareholders’ resolution approving such reduction;
- in a merger, acquisition or consolidation, the board of directors has the obligation to prepare a transaction plan and announce the proposed transaction in newspaper; and
- in a liquidation, in addition to the announcement of such liquidation, the board of directors can also act as the liquidator of the company.

Each member of the board of directors will be jointly and severally liable for losses suffered by the company or shareholders if he or she violates the articles of association, or the prevailing laws and regulations; or if he or she fails to comply with his or her duties, or in the event the company has been declared bankrupt because of the fault or negligence of the board of directors and the assets of the company are not sufficient to cover the losses incurred in the bankruptcy.
It should be noted that a director will not be held personally liable if he or she can prove that:

a. he or she has managed the company prudently, in good faith and in accordance with the objectives and purposes of the company, the articles of association and the prevailing laws and regulations;

b. the loss suffered by the company is not a result of his or her wrongful actions or failure to comply with his or her duties, where he or she do not have any conflict of interest with the management of the company that causes the loss, and he or she has taken all necessary action to prevent such loss occurring; and

c. in the occurrence of the bankruptcy of the company, the director can prove that he or she has managed the company prudently and in good faith, and the bankruptcy has not occurred as a result of his or her negligence or fault, and he or she has taken all necessary actions to prevent the occurrence of the bankruptcy.

If a company has been declared bankrupt, the board of directors is no longer entitled to manage the company, and the authority to manage the bankruptcy estate will be assigned to a receiver designated by the Commercial Court. However, in the case of a suspension of payment obligations, the board of directors must jointly manage the company with an administrator appointed by the Commercial Court.

The board of commissioners has duties to supervise the company, and to give advice to the board of directors in the interest of the company and according to the purposes and objectives of the company. The duties of the board of commissioners include reviewing the annual report and approving the budget plan prepared by the board of directors, as well as reporting on the performance of their duties to the shareholders during the annual general meeting of shareholders.

Each member of the board of commissioners will also be jointly and severally liable for losses suffered by the company if he or she fails to perform his or her duties prudently and in good faith, except if he or she can prove that:

a. he or she has conducted the supervision of the company prudently and in good faith, and in accordance with the objectives and purposes of the company, the articles of association and the prevailing laws and regulations;

b. he or she does not have a personal interest in the management of the company that causes such loss;

c. he or she has advised the board of directors to take all necessary actions to prevent the occurrence of the loss; and

d. in the occurrence of bankruptcy, he or she can prove that the bankruptcy was not due to his or her fault or negligence, and he or she has carried out his or her supervision duties prudently and in good faith, and he or she has taken all necessary actions to prevent the occurrence of the bankruptcy.

vi Clawback actions

The Bankruptcy Law allows that certain transactions made prior to the bankruptcy that favour one lender over another can be annulled. Article 41 of the Bankruptcy Law provides that voluntary transactions (that is, transactions entered into without any contractual obligation to do so) of the borrower undertaken one year before the declaration of bankruptcy that cause
a loss to the lenders may be nullified if it can be proved that, at the time of the transaction, the borrower and the counterparty knew or should have known that the transaction would cause a loss to the lenders.

If a transaction is annulled, all assets of the borrower received by the counterparties to the transaction must be returned to the bankrupt estate.

A transaction that the borrower is contractually obliged to perform can be annulled if, at the time of the transaction, the lender knew that a bankruptcy petition was pending and that the transaction was a result of collusion between the parties.

III RECENT LEGAL DEVELOPMENTS

The Minister of Law and Human Rights issued Regulation No. 2 of 2017, which is an amendment to Regulation No. 11 of 2016 on Guidelines for Determining Fees for Receiver and Administrators. In this amended regulation, the government has reduced the amount of fees to be received by: (1) an administrator in the case of suspension of payment obligation, and (2) a receiver if a bankruptcy ends with insolvency.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

Based on data published on the website of the Commercial Court of Jakarta, during 2016 there were 140 cases of suspension of payment obligations, and from January 2017 to the end of June 2017, there were 98 applications for suspension of payment obligations at the Commercial Court of Jakarta.

In practice, suspensions of payment obligations are followed by debt restructuring, and it is common practice that the lender and borrower agree to reschedule the terms of the payment of the loan or exercise a debt-to-equity swap, or to a combination of these two options.

V INTERNATIONAL

As it is not a Member State of the EU, the EC Regulation is not applicable in Indonesia. Nor has the country adopted the UNCITRAL Model Law.

Submission to and a judgment of a foreign court will not be enforceable by the Indonesian courts unless there is a bilateral treaty between Indonesia and the country in which the judgment was rendered. To date, no bilateral treaties have been signed by Indonesia to enable the enforcement of a foreign judgment in Indonesia. A non-Indonesian judgment may, however, be given such evidentiary weight as an Indonesian court considers appropriate, and a re-examination of the issues de novo would be required before an Indonesian court to enforce a claim in Indonesia that is the subject of a foreign judgment.

However, Indonesia has ratified the 1958 New York Convention and promulgated Supreme Court Regulation No. 1 of 1990 in conjunction with Law Number 30 of 1999 on Arbitration and Alternative Dispute Resolutions, which is the implementing regulation for the recognition and enforcement of foreign arbitral awards.

Enforcement of international arbitration awards can only be handled by the Central Jakarta District Court. International arbitration awards will only be recognised and enforced in Indonesia if they fulfil the following criteria:
the international arbitration award is rendered by an arbitrator or arbitration panel in a country that is bound to Indonesia by a bilateral or multilateral treaty on the recognition and enforcement of international arbitration awards; the international arbitration awards are limited to awards that are included within the scope of commercial law under Indonesian law; international arbitration awards that may be only enforced in Indonesia are limited to those that do not conflict with public policy; an international arbitration award may be enforced in Indonesia after obtaining a writ of execution from the Chairman of the Central Jakarta District Court; and international arbitration awards that involve Indonesia as one of the parties to the dispute may only be enforced after obtaining an exequatur from the Supreme Court of the Republic of Indonesia, which will then delegate it to the Central Jakarta District Court.

No appeal or cassation to the Supreme Court may be made against a decision of the Chairman of the District Court of Central Jakarta who recognises and enforces the international arbitration award. However, a cassation to the Supreme Court may be made against a decision of the Chairman of District Court of Central Jakarta for refusing to recognise and enforce and international arbitration award.

After the Chairman of the Central Jakarta District Court has issued the writ of execution, further enforcement will be delegated to the chairman of the district court that has jurisdiction to enforce it.

VI  FUTURE DEVELOPMENTS

There is no legislation on restructuring pending in Indonesia. In view of the country’s current economic climate, it is possible that the amount of non-performing loans will increase, resulting in a rise in the amount of debt restructuring either through formal or informal procedures. This is reflected in the growing number of applications for suspension of payment obligations at the Commercial District Court during the past year.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

i Liquidity and state of the financial markets

The trend in macroeconomic terms on the Italian market continues to be positive at the beginning of 2017, although the growth of Italian productivity is lower compared to other European countries.

The very high public debt remains a heavy burden on the Italian economy and a major source of vulnerability, especially in the context of protracted weak growth.

The figures for the first quarter of 2017 relating to the public debt and presented in the Economic and Financial Document showed that public debt peaked in April 2017 up to €2.27 billion. In this scenario, government debt equates to over 132.3 per cent of GDP.

Companies’ production indicators confirm that productivity remains lower than in 2007, although slightly improved compared to 2016 figures.

Overall, companies’ financial positions have continued to strengthen gradually; bankruptcies have diminished by 16.8 per cent.

In this context, the existence of huge amounts of nonperforming loans still represent a serious concern for Italian financial markets. On this point, great attention should be paid to the innovations brought by Law Decree 14 February 2016 No. 18, which introduced a public guarantee mechanism applicable to securitisation procedure of non-performing loans, thus improving the economic value of doubtful loans granted to subjects in state of financial crisis.

ii Market trends in restructuring procedures and techniques employed during this period

The latest figures related to insolvency and bankruptcy procedures have shown a steady improvement since the previous year.

In the first quarter of 2016, 3,600 companies applied for a bankruptcy procedure – a decrease of 4.5 per cent from the previous year. The numbers of the overall insolvency proceedings have also shown encouraging results, significantly decreasing for the first time since 2008, namely by 24.5 per cent in composition proceedings, although this drop is deemed to be mainly the result of the groundbreaking changes made in the context of this proceeding.

This positive trend has also been confirmed for the first quarter of 2017. Figures show that 2,998 companies applied for a bankruptcy procedure in this period, a decrease of...
16.8 per cent from the previous year, of 20.2 per cent from 2015 and of 20.3 per cent from 2014. In the same period, the numbers of insolvency proceedings have also shown positive results, decreasing by 26 per cent from the previous year.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

The main source of Italian insolvency law is Royal Decree No. 267 of 16 March 1942 (the Insolvency Act), which has been amended and integrated from time to time by the Italian legislator.

The Insolvency Act provides for several bankruptcy and restructuring proceedings that have been amended in the last years and some of which are described below.

i Legal procedures

Bankruptcy

The bankruptcy proceeding is the most invasive procedure for a debtor. The law specifically indicates which debtors are subject to the bankruptcy procedures (not all debtors can fall bankrupt). In general, the law states that the bankruptcy procedure applies to ‘any company or individual whose main activity consists of the production or trade of goods and services’. A debtor is declared insolvent when it is no longer able to regularly meet its payment obligations. The insolvency status is per se a situation that justifies a declaration of bankruptcy by the relevant court, even where the insolvency has not been caused by the debtor’s misconduct.

The procedure is started by an order of the court having jurisdiction over the debtor’s principal place of business on the basis of a petition, which may be filed by the debtor itself (or the directors of the debtor company), a creditor, the public prosecutor, or the bankruptcy court ex officio.

The proceeding is carried out and supervised by a receiver (appointed by the court), a deputy judge, and a creditors’ committee representing all the creditors.

Upon issuance of the bankruptcy decision by the court, the debtor no longer has the legal right to manage its business and is no longer able to dispose of its assets. All legal actions taken by the creditors against the debtor are suspended.

The receiver is a public officer and is required to perform his or her duties in person. The receiver is paid through the debtor’s assets, and such remuneration ranks as ‘super-senior’ over the creditors’ claims. Law imposes certain specific duties on the receiver. In particular, the receiver manages the company’s assets and operates in the interest of the creditors. His or her main task is that of disposing of the company’s assets in order to obtain proceeds necessary to repay the creditors, who will be reimbursed according to a distribution plan on the basis of the order of claim priority established by the Italian Civil Code and by several provisions of the Insolvency Act, and certified by the court. Priorities are normally granted by pledges, mortgages or other liens voluntarily granted by, or imposed on, the debtor. Claims of Italian and foreign creditors rank equally.

Before the execution of the distribution plan, the receiver must submit a final report to the deputy judge with a full description of all the activities carried out in the assets management and in general in the business administration. Creditors may file claims against the final report. Once the motions have been decided, the deputy judge orders the implementation of the distribution plan. Creditors are always entitled to oppose the distribution plan in order to obtain payment of any unrecovered portion of their claims and of interest thereon.
Bankruptcy proceedings may also end up with a settlement accepted by the creditors, as described below.

Law No. 132/2015 made significant changes to the bankruptcy proceeding (see Section III, *infra*).

**Settlement of bankruptcy proceeding**

The Insolvency Law allows creditors and, under certain circumstances, the debtor to have recourse to a procedure within the bankruptcy proceedings. In particular, once the court has set out a timetable for the distribution of proceeds, a settlement proposal could be submitted by a creditor or the debtor, which should, in principle, guarantee repayment of the debts, either greater or quicker than the one provided for under the bankruptcy distribution.

If the court decides that the settlement proposal is in the best interests of the creditors, the court will issue a decision by ordering to notify all creditors of the proposal. For the settlement to be effective, the proposal has to be accepted by the majority of creditors.

**Composition with creditors proceeding**

While the bankruptcy procedure is highly regulated and is under the full control of the court and the receiver, the changes of law implemented in the past years have granted to the debtor a higher level of autonomy in the context of the composition with creditors proceeding.

In general, a company applies for the protection of a composition procedure (*concordato preventivo*) when it is either insolvent (but believes it is in a position to repay its creditors, at least partially) or it is suffering a crisis that has, however, not yet reached the level of insolvency.

The court, once it has admitted the company to the procedure, appoints a commissioner who acts as a public officer.

During the procedure, the assets continue to be managed by the debtor company, while the commissioner supervises the management of the company in the interest of the creditors.

The petition must be accompanied by a *concordato* plan, which, *inter alia*, shall include:

- an updated economic and financial statement of the company;
- an analysis of all the economic activities carried out by the company, including a list of all creditors and a description of the relevant credits and of any pre-emption rights;
- a list of all people having personal and property rights over the debtor properties; and
- an evaluation of goods and particular categories of creditors.

The *concordato* plan must describe the ways in which the creditors will be repaid and the relevant percentage, and shall be accompanied by a report drafted by an independent expert that will certify the correctness of the data reported and the feasibility of the plan itself. The commissioner, *inter alia*, expresses his or her opinion on the feasibility of the *concordato* plan.

As a general rule, the *concordato* plan must be approved by the majority of the non-secured creditors; to the extent that the plan provides that the secured creditors are entirely paid within 12 months from the final ‘confirmation’ of the procedure (i.e., the declaration by the judge that the procedure is properly completed), secured creditors are not admitted to vote.

The composition procedure is governed by the court, which plays a key role in terms of supervision and implementation. Although an intensive debate exists at the level of such interference, much depends on the approach of the relevant court where the procedure is
started. Another significant characteristic of the composition procedure is that, once approved by the majority of the creditors, the concordato plan proposed by the company is binding on all creditors (even those dissenting).

It is possible to submit a request to the court for admittance to the composition procedure by postponing the filing of the concordato plan and of all the other documents required by law (the pre-concordato request). The request must be accompanied, *inter alia*, by the filing of the three latest approved balance sheets and a detailed list of all the creditors. The condition for the admittance is the non-filing of a petition that has been rejected in the previous two years.

As soon as a pre-concordato request is filed, the court, subject to its positive evaluation, admits the company to the pre-concordato phase, granting the company between 60 and 120 days for filing the concordato plan and any other related documents. This is intended to allow the debtor to seek immediate protection by freezing any enforcement proceedings by creditors, but during the pre-concordato phase all extraordinary activities of the company must be authorised by the court. The court often sets thresholds of value above which such authorisation is required.

The court allows the company to decide whether a certain activity can be qualified as 'extraordinary' and oversees the company, which must provide certain information (mainly financial) during the pre-concordato phase. The court, after the publication of the pre-concordato request, may appoint a judicial officer to monitor whether the distressed company is acting for the purpose of settling all creditors. Certain periodic reporting obligations are imposed on the debtor regarding the financial management of the company during the pre-concordato phase. In the event of breach of such obligations, the court may declare the company bankrupt.

During the pre-concordato phase, not only are enforcement proceedings frozen, but interim actions are prevented.

Distressed companies often pose a risk for their partners and counterparties; in fact, in the event that the company is declared bankrupt, any payments made to suppliers or banks are at risk of being clawed back or revoked by the bankruptcy receiver. This can often result in further deterioration of the business of the company, making the crisis worse. To avoid this, and to create incentives for business partners of the debtor not to stop doing business with it and to facilitate access to credit during the period of distress, the law provides the following:

- from the day on which the request is filed with the Register of Companies (i.e., one day after it is submitted to the court), the debtor may be authorised to engage in transactions in the ordinary and extraordinary course of business (those transactions will not be subject to clawback actions);
- all credits that have arisen as a result of transactions authorised by the court (even unsecured) during the procedure take priority (within certain circumstances, even over secured claims); and
- payments made by the debtor after the request is filed with the Register of Companies are not subject to clawback action, even if the distressed company goes bankrupt.

Along the same lines, the debtor is allowed to terminate unprofitable or excessively burdensome contracts with the prior authorisation of the court. This is aimed at preserving the goodwill of the debtor and increasing the chances of its recovery.
Recently, certain groundbreaking changes have been made to this procedure. Creditors are allowed to submit their proposal or offer for the concordato, provided that certain requirements are met. Debtors are entitled to ask the court for authorisation to obtain interim financing. For more details, please refer to Section III, infra.

**Debt-restructuring agreements**

Article 182 *bis* of the Insolvency Act provides for the rules governing the debt restructuring agreement. The debt restructuring agreement can be considered a private agreement whereby the debtor and the creditors, representing at least 60 per cent of the total debt, reach an agreement on a repayment plan. Those agreements are subject to confirmation by the competent court. Restructuring agreements do not, however, bind those creditors that were not party to it.

These agreements provide the procedures and timing for the repayment of such creditors.

If debts are already due and payable at the confirmation of the agreements by the court, creditors not party to the restructuring agreements must be paid either within 120 days or 120 days after the debts become due. There are also some provisions applicable to both this proceeding and the aforementioned composition with creditors proceeding:

a. similar to ‘first-day orders’ in the US Bankruptcy Code, the debtor may submit an application to the court to obtain new debtor-in-possession (DIP) financing from banks or other sources of credit, and to pay creditors that are crucial to ensuring the continuity of the business. Such financing will rank as a super-senior priority, which is an incentive for lenders to provide financing to a distressed company;

b. there has been reinforcement of the independence requirements of third-party experts engaged to attest the feasibility of the restructuring plan, the purpose of which is to prevent cases of conflicts of interests between auditors and the debtor. Experts responsible for false statements or omission of important information in such situations are now subject to criminal liability; and

c. during the restructuring procedures, the provisions of law imposing the reintegration of corporate capital in the event of losses are not applicable. This is designed to give a distressed company time to prepare a restructuring plan without the pressure of compliance with the deadlines set by those rules and, primarily, to eliminate the need to spend money necessary to increase corporate capital after a loss (which might immediately jeopardise any attempt to re-launch and restructure), especially when the survival of the company is still in doubt.

Law No. 132/2015 introduced the new Article 182 *septies* providing for a ‘special’ debt restructuring agreement, applicable in case the majority of the total debt is towards banks or credit institutions. For further details, see Section III.vi, infra.

**Compulsory liquidation**

Compulsory liquidation is an administrative procedure controlled by state officers instead of by the courts. The procedure is used when the debtor’s business is deemed to be of public interest, such as insurance companies, banks, cooperatives and nonprofit entities, which are subject to a number of governmental controls. The purpose of this procedure is to achieve recovery of the business through a settlement or an arrangement plan. The debtor, the directors of the debtor company and any of the creditors are entitled to apply
to the court in order to start the procedure. The court is under the obligation to seek the advice of the governmental agency responsible for supervising the debtor’s enterprise. The judge may initiate the proceeding by declaring the insolvency of the debtor and appointing a liquidator. All legal actions by creditors against the debtor are then suspended, with the exception of those aimed at ascertaining the amount of the claim. The liquidator, who also acts as a public officer, is assisted by a supervisory committee consisting of a number of experts, whose number can vary from three to five and who are not required to be creditors of the debtor (even if this might be preferable). Unlike in other insolvency proceedings, there is no requirement for a judge or a commissioner to be in charge. The liquidator must review the claims and evaluate whether the settlement plan is feasible.

**Extraordinary administration**

The extraordinary administration procedure applies to big companies falling within certain specific requirements, the occurrence of which is checked by the relevant court where the request for the extraordinary administration procedure is filed. The procedure applies to companies employing at least 200 permanent workers for at least one year, and having an overall amount of debt, the value of which is no lower than two-thirds of the aggregate value of both assets and revenues. For the application of the extraordinary administration, the company must have ‘concrete chances for the recovery of the financial stability’. After consultation with the Ministry of Economic Development and the Ministry of Economy, the court issues an order declaring the insolvency of the company. The Ministry of Economy appoints an ‘extraordinary commissioner’, who proposes a plan for the disposal of the assets or a recovery plan within 60 days of his or her appointment. All legal actions initiated by creditors against the company are suspended as a consequence of the foregoing order. One of the most significant extraordinary administrations in Italy has been the *Parmalat* case in 2005. The magnitude and relevance of the * Parmalat* case – and its international implications – have resulted in several amendments to the Italian legislation on insolvency matters.

**ii Duties of directors of companies in financial difficulties**

According to the provisions of the Italian Civil Code, directors must act with a duty of care and must comply with certain rules imposed by law and by-laws relating to the fiduciary responsibilities in day-to-day management. The directors are jointly liable with the company for damages deriving from non-compliance with said duties. In all cases, the directors are jointly liable if they fail to adequately supervise the general conduct of the company’s affairs or if, being aware of prejudicial acts, they do not act in order to prevent any harmful activities, or to eliminate or reduce the harmful consequences of such activities. Liability for acts or omissions of directors does not extend to any directors that, acting without fault, express their dissent without delay, such dissent being registered in the minute book of the meetings and resolutions of the board of directors, with written notice also to the chair of the board of auditors. Again, according to the Italian Civil Code, directors are held liable to the company’s creditors for noncompliance with their duties concerning preservation of the company’s assets. The action can be brought by creditors when the company’s assets prove insufficient to satisfy their claims. In the event of bankruptcy or compulsory administrative liquidation, the action against the directors can be brought by the receiver in bankruptcy or by the commissioner. A waiver of the action by the company does not prevent the company’s creditors from exercising their legal rights against the directors.
iii Clawback actions

The suspect period has been fixed in a maximum of two years prior to the date of the bankruptcy declaration (in other cases the suspect period is 12 months and, in certain specific cases, the suspect period is reduced to six months).

In the event the bankruptcy declaration occurred after the petition of a concordato procedure, the suspect period commences on the day in which the petition is published in the company register.

The Insolvency Act states that:

*The receiver is entitled to require that the transactions carried out by the debtor to the detriment of the creditors shall be ineffective, according to the provisions of the Italian Civil Code. The action can be filed before the insolvency court against both the direct party of the contract and, if the case, its successors in title.*

Unless the other party proves that it was not aware of the insolvency status of the debtor, it is possible to clawback the following transactions:

*\(a\) non-gratuitous acts performed in the one-year period preceding the declaration of bankruptcy where the transactions carried out or the obligations assumed by the bankrupt party exceeded more than one-quarter of the paid or agreed consideration;*

*\(b\) acts extinguishing the payable and overdue pecuniary debts not made in cash or by other normal payment methods were carried out in the one-year period preceding the declaration of bankruptcy;*

*\(c\) pledges, anticresi and voluntary mortgages created by an agreement of the parties during the one-year-period preceding the declaration of bankruptcy for previous undue debts;* and

*\(d\) pledges, anticresi, voluntary and judicial mortgages (mortgages created by an order of the court) created during the six-month period preceding the declaration of bankruptcy for overdue debts.*

In the event that the receiver proves that the other party was aware of the insolvency status of the debtor, it is possible to claw back the repayments of certain overdue debts resulting from the non-gratuitous acts and those constituting a preemptive right for debts (even those incurred by third parties) if carried out in the six-month period preceding the declaration of bankruptcy.

III RECENT LEGAL DEVELOPMENTS

i Law Decree No. 83/2015 converted into Law No. 132/2015

The aim of the Law Decree is to create a system of effective measures for financial distress situations to limit the economic loss either from an entrepreneurial perspective or in the financial field. Another aim is to provide companies with appropriate measures of support for a productive recovery, with the intent to provide benefits for the employment sector and, more generally, for the national economy.

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2 Article 66 of the Royal Decree No. 267/1942 (the Insolvency Act).
3 Article 67 of the Royal Decree No. 267/1942 (Insolvency Act).
The most groundbreaking changes regarding the composition proceedings introduced: the possibility for qualified creditors to file competing proposals; the obligation to reimburse a minimum percentage of unsecured creditors; and, in the event the concordato plan provides for the transfer of the company, a going concern or key assets, a duty for the court to start a procedure to research the best offer.

**Competing proposals**

Creditors representing at least 10 per cent of the total debt are entitled to file a proposal for a concordato preventivo plan, which shall then be evaluated by the creditors alongside the one filed by the debtor. This right is not granted if the concordato plan filed by the debtor provides that at least 40 per cent of unsecured creditors are repaid (30 per cent if the plan provides for business continuity).

**The minimum percentage**

A concordato plan that does not provide for business continuity shall provide that at least 20 per cent of the unsecured creditors are repaid.

**Compulsory tendering**

The court shall start a compulsory tender for the research of the best offer in the event the concordato plan provides for the transfer of the company, a going concern or of key assets. Offers will be compared on an economic basis. The court is required to set the criteria for the tender, to be determined on a time-to-time basis depending on the specifics of the case.

**The majority principle in the approval stage**

The mechanism of silenzio assenso concerning the approval of the concordato plans has been removed (silenzio assenso means that the non-vote of a creditor in the approval stage is counted as approval in the calculation phase). This amendment, jointly considered with the new provisions on the minimum threshold of 20 per cent and on the competing proposals, makes the performance of the plan more difficult and its positive execution riskier.

**Interim financing**

A debtor who has already filed a petition for the admission to a creditor composition procedure or an application for the approval of a debt restructuring agreement can obtain new financing or continue to use existing receivables credit lines. The possibility is granted provided that:

- the new financing is required for urgent operational needs;
- the debtor is unable to obtain the financing in a different way;
- the debtor indicates the envisaged use of the financing; and
- not granting the financing would result in the disruption of business continuity.

**The debt restructuring 'special' agreement**

New Article 182 septies has been introduced in the Insolvency Act, according to which, in the event the majority of the total debt is towards the category of banks and credit institutions, the debt restructuring agreements entered into with at least 75 per cent of such category is automatically binding for the remaining 25 per cent as well, and also in the case of non-voting or absent creditors (new rules regarding the duty of correct information in favour
of the creditors have been introduced). To ensure the respect of the *par condicio creditorum* principle, Article 182 septies provides that the agreement shall be the only one entered into with the category and shall be final and binding for every creditor under the same terms and conditions.

**ii Other significant changes regarding the bankruptcy procedure**

Law No. 132/2015 introduced the following new provisions regarding the appointment and the revocation of the receiver, the liquidation phase and the maximum duration of the procedure:

- *a* litigation procedures that are related to the bankruptcy proceeding are treated as a priority by courts;
- *b* the receiver shall provide a liquidation plan within 60 days from the draft of the inventory and in any case no later than 180 days from the bankruptcy declaration. The law provides for the revocation of the receiver in case of nonfulfilment of these obligations;
- *c* payment of liquidated assets prices can be made by instalments;
- *d* the liquidation procedure can be completed notwithstanding litigation procedures are still pending. Further incomes will be distributed according to the court resolution for the approval of the distribution plan; and
- *e* the completion of the liquidation procedure shall occur within two years from the bankruptcy declaration. Time extensions can be granted subject to specific needs.

**iii The Law Decree No. 69, dated 3 May 2016**

A further cause of revocation of the receiver has been introduced by the Law Decree No. 69, dated 3 May 2016 in the event of non-submission of the periodical report for the income distribution. The revocation cause applies provided that the liquidation procedure has generated income to be distributed.

Further amendments have been introduced with the intent to facilitate the obtainment of financing by entrepreneurs in the course of their business activity.

Entrepreneurs can grant pledges on moveable assets (excluding registered moveable assets) to guarantee their debts. The pledge shall be executed in writing and shall describe the parties, the assets, the credit and the maximum amount guaranteed. The guarantee becomes effective with the filing in the registry of non-possession pledges held by the Italian Revenue Agency. In the event of enforcement of the guarantee, the sale is carried out by the creditor on the basis of a competitive procedure and according to the value appraisal. Parties can provide for the possibility to lease the assets; in this case the instalments will be accounted for up to the full reimbursement of the debt. In case of bankruptcy, the sale is only admitted provided that the creditor is ranked as privileged.

To assist financing with guarantees, entrepreneurs can also transfer properties in favour of banks or credit institutions. The effectiveness of such transfers is subject to the condition precedent of non-payment for a period of six months after the expiry of at least three nonconsecutive instalments unpaid.

Furthermore, the Decree provides for two amendments in the section regarding the performance of the creditors’ meeting by way of electronic devices:

- *a* the court, considering the number of creditors and the total amount of the debt, may decide the creditors’ meeting to be held with the support of electronic devices, provided that said devices can effectively ensure the correctness of the meeting; and
in the event the court decide for creditors’ meeting by way of electronic devices, the
discussion on the proposal of the debtor, and eventually on the competing proposals,
is regulated by way of the decree issued by the court at least 10 days prior to the date
scheduled for the meeting.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST
ACTIVE INDUSTRIES

Despite the weak but steady growth observed in the last two years, Italian companies are
still suffering the negative consequences of the contraction of domestic demand following a
weakening of foreign demand.

Top-ranking Italian businesses are still living within the context of financial difficulties,
which in the worst cases have required companies, depending on the seriousness of such
situations, to resort either to bankruptcy proceedings or insolvency proceedings.

It is also worth mentioning that when dealing with distressed companies, either
as an investor, debtor or creditor, special attention must be paid to Law Decree No.
231 of 8 June 2001 (Law 231), which concerns the administrative liability of legal entities,
companies and associations without legal capacities, and the consequences of its violation by
the company.

In particular, the application of Law 231 becomes more important when the distressed
situation of the relevant company is a consequence of (or simply occurs in the context of) the
commission by the entrepreneur (or by the board of directors) of specific crimes.

The commission of those crimes can trigger the submission of the company itself to
certain sanctions, including the confiscation of the company’s properties, if the company
did not create a system capable of protecting itself from the negative consequences of the
commission of those crimes by physical individuals operating in the name or on behalf
of the company. Therefore, in evaluating a business opportunity, the investor has to take
into account any possible consequences in the event that a violation of Law 231 has been
charged to the company. In fact, the creditor’s right to be satisfied by the company’s assets
or the company’s right to recover from the distressed situation (sometimes) thanks to the
intervention of a third-party investor could be overridden by the state’s interest in confiscating
all (or part of) the assets of the company, to the detriment of creditors and all other interested
parties. According to a recent decision of the Supreme Court, this principle, according to
which the interest of the state has priority over the interests of the creditors, has been slightly
overridden, to the benefit of the creditors and the company. This decision is quite important
and it would be suitable for a provision of law to be implemented to confirm these principles.

V INTERNATIONAL

On 20 May 2015, the European Parliament issued the new Regulation (EU) 2015/848 (the
Regulation) on insolvency proceedings, which becomes effective on 26 June 2017 and will

It is worth mentioning that different dates of effectiveness have been set for the
following Articles of the Regulation:

a Article 24, Paragraph 1 on the set-up of a national insolvency database will apply from
26 June 2018;
Article 25 on the interconnection between national insolvency databases will apply from 26 June 2019; and

Article 86 on information regarding national and European insolvency proceedings has started to be applied from 26 June 2016.

The new Regulation has been developed in the context of a new awareness of insolvency. The aim of the Regulation is no longer the sale of the company assets to achieve the reimbursement of the creditors, but is mainly the saving of the business and the company’s productivity.

The following changes, inter alia, have been included:

a) a broadened field of application of the Regulation has been introduced: Article 1 provides that the Regulation applies to ‘public collective proceedings, including interim proceedings’, aiming at the rescue, the completion of a debt restructuring agreement, the company reorganisation or the company assets liquidation;

b) the rules regulating the applicable jurisdiction and the centre of main interest are now defined by the Regulation as ‘the place where the debtor conducts the administration of its interests on a regular basis and which is ascertainable by third parties’ and the national courts are now allowed to claim the jurisdiction in the event ‘the company’s actual centre of management and supervision and of the management of its interests is located’ within its territory, and ascertain ex officio the correctness of the jurisdiction;

c) it is now possible to suspend or refuse secondary insolvency proceedings in the event of contrast with a connected insolvency procedure dealt by another Member State;

d) an international network for the insolvency databases has been created, provided for by Article 24 of the Regulation; and

e) a duty of cooperation between different Member State courts has been introduced in case of insolvency proceedings regarding two or more companies part of the same group.

The Regulation will apply from 26 June 2017, with a few exceptions among Member States.

VI FUTURE DEVELOPMENTS

As stated above, since the Parmalat case in 2005, the Italian legal framework on restructuring has been made more effective than ever thanks to a series of interventions aimed at granting more protection to all those entities involved from a creditor’s perspective.

In February 2016, the Council of Ministers approved the law bill consisting of 15 articles, drafted by the Rordorf Commission, for the delegation to the government for the drafting of a consolidated act for company crisis and insolvency.

Should the law bill be converted in the formulation approved by the Council of Minister, it shall have a revolutionary effect on the sector. It is worth noting that the law bill, inter alia, has provided for the removal of the word ‘bankruptcy’ in the consolidated act, given the negative meaning and effects that are related to this word. The aim is, therefore, not only the merging, but also the enactment of a full ‘restyling’ of the rules governing bankruptcy and restructuring procedures, also taking into account the experiences accomplished by the practice in foreign countries.

The main goal is a simplification of current legislation to make it more intelligible, also in the interest of nonprofessionals, and a noteworthy reduction of the costs related to the
proceedings. Particular attention has been paid to the category of the debtors, who, in most cases, are people with a low or absent degree of juridical and economic knowledge and are particularly exposed to the debt growth risk.

The delegation, *inter alia*, regards several aspects related to:

- company groups;
- alert and mediation procedures;
- debt-restructuring agreements and repayment plans;
- creditor-composition proceedings;
- restructuring programmes;
- over-indebtedness procedures;
- guarantees; and
- extraordinary administration.

The legislative process is currently pending for final approval. Following the approval of the Italian Chamber of Deputies, the law bill is pending before the Italian Senate of the Republic.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

Under ‘Abenomics’, the economic policy introduced under Prime Minister Shinzo Abe’s administration, monetary policy led to the weakening of the yen against major world currencies and an increase in Japanese stock market prices.

In these circumstances, because financial institutions continue to accept changing payment terms, the number of insolvency cases has declined over the past several years. According to statistics from the Supreme Court, the number of bankruptcy cases in 2015 was 71,533 (down approximately 2.5 per cent from the previous year); civil rehabilitation cases were 158 (down approximately 3.7 per cent from the previous year) and corporate reorganisation cases were 42 (39 of which are group companies of Rams Corporation). There was no bankruptcy of listed companies in 2016.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Informal and consensual restructuring framework

Overview

A distressed debtor commonly seeks to reach a negotiated agreement with its creditors outside the court to avoid statutory insolvency proceedings. An out-of-court restructuring or workout can preserve a debtor’s going-concern value and avoid administrative costs associated with statutory insolvency proceedings. It is generally perceived by restructuring practitioners that an out-of-court restructuring is preferable to statutory insolvency proceedings to preserve a debtor’s going-concern value and reduce the costs for restructuring.

There are no specific rules on out-of-court restructurings, with the exception of several out-of-court restructuring schemes that have been developed. These exceptions, which provide guidelines and some level of certainty for out-of-court workout proceedings, include the Guidelines for Out-of-Court Workouts published by a study group in 2001, the Turnaround Alternative Dispute Resolution (Turnaround ADR) established in 2007, the Regional Economy Vitalisation Corporation of Japan (REVIC) scheme and the SME Business Rehabilitation Support Co-operative scheme. The following are, among the developed guidelines and schemes, outlines of Turnaround ADR and REVIC, which have recently been utilised often.

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**Turnaround ADR**

Turnaround ADR was created through an amendment to the Act on Special Measures for Industrial Revitalisation and Innovation in 2007, to support turnaround of the debtor outside the court at an earlier stage. Turnaround ADR is designed to help facilitate negotiations between a distressed debtor and its financial creditors under independent mediators licensed by the Ministry of Economy, Trade and Industry and the Ministry of Justice. The Japan Association of Turnaround Professionals (JATP) is the only licensed organisation that can mediate Turnaround ADR cases thus far. Two or three mediators from the JATP who have long been seen as restructuring professionals preside over Turnaround ADR cases. Medium- or large-sized companies are supposed to employ Turnaround ADR. The creditors expected to participate in Turnaround ADR proceedings are generally financial institutions, while trade creditors generally do not participate in Turnaround ADR. The proceedings are not disclosed to the public. There have been approximately 50 cases that employed Turnaround ADR as of November 2015.

**The REVIC scheme**

REVIC was established in 2013 as a limited-term organisation to succeed the role of the Enterprise Turnaround Initiative Corporation of Japan (ETIC), which was established in 2009 to help turnaround of small and medium-sized enterprises (SMEs) in financial distress. ETIC also succeeded the role of the Industrial Revitalisation Corporation of Japan, which was established in 2003, modelled on Securum in Sweden.

REVIC is a restructuring advisory firm with the function of debt and equity investment, owned by the Japanese government and private financial institutions. The purpose of REVIC is to support vitalisation of SMEs with excessive debts, even though they have their worthwhile management resources. The REVIC scheme provides many measures with qualifying debtors, including, among other things, purchasing the debts from financial institutions other than the ‘main bank’ and making a new equity investment in the debtor. If it purchases the debts or invests in the debtor, REVIC is expected to sell them within five years. REVIC then develops a turnaround plan and sends restructuring professionals to the debtor.

**ii Statutory insolvency proceedings**

**Overview**

Under Japanese law, there are three major types of insolvency proceedings: civil rehabilitation proceedings, corporate reorganisation proceedings and bankruptcy proceedings. Each can be categorised into one of two general types, depending on whether the aim of the proceedings is to restructure the company as an ongoing concern or to liquidate the company. Civil rehabilitation proceedings are roughly parallel to those under Chapter 11 of the Code; bankruptcy proceedings are roughly parallel to those under Chapter 7 of the US Bankruptcy Code.

Civil rehabilitation proceedings are restructuring-type proceedings, which were introduced on 1 April 2000, and which apply to all types of companies, including corporations, partnerships and limited liability companies. Civil rehabilitation proceedings are often referred to as debtor-in-possession (DIP) proceedings. Generally, the management of a debtor, as a debtor-in-possession, will continue to operate the debtor’s business, being overseen by a supervisor appointed by the court.
Corporate reorganisation proceedings are also restructuring-type proceedings. Unlike in civil rehabilitation proceedings, they apply only to corporations. A reorganisation trustee will be appointed by the court to operate and administer the debtor’s business and property. Corporate reorganisation proceedings are typically accompanied by a recapitalisation of the debtor, which commonly involves a 100 per cent capital reduction, coupled with capital increases by a plan sponsor.

Bankruptcy proceedings are liquidation-type proceedings. A bankruptcy trustee, who represents the interests of all creditors, is appointed by the court to liquidate the debtor’s assets into cash and then distribute the cash to the creditors in a fair and equitable manner (in principle, on a pro rata basis).

**Filing of proceedings**

All three insolvency proceedings can be filed either voluntarily or involuntarily. Generally, no one, including a debtor or any of its creditors, is obligated to file a petition to commence insolvency proceedings under Japanese law. Unlike in some other jurisdictions, such as the United States, insolvency proceedings in Japan do not automatically commence with the filing of the motion. The court instead issues an order to commence the proceedings, if it confirms that there exists a basis for the proceedings to commence and no cause for which it may dismiss the motion (e.g., a motion filed in bad faith).

Unlike in some other jurisdictions, such as the United States, there is no automatic stay granted by the court following the filing of a petition. A stay is granted only upon the debtor filing another petition for temporary preservation of the debtor’s assets.

In civil rehabilitation proceedings, the court, simultaneously with the grant of a temporary restraining order, also orders that a supervisor be retained. In order to retain a supervisor, the court lists the debtor’s activities that need to be approved by the supervisor, which include disposal of the debtor’s assets (including creating a security interest on the debtor’s assets) and DIP financing. The purpose of retaining a supervisor, together with obtaining a temporary restraining order, is to prevent the debtor’s assets from being lost or collected by any creditor.

In corporate reorganisation proceedings, the court also appoints a provisional administrator. A court order exclusively entrusts management of the debtor’s business and administration of the debtor’s assets to the provisional administrator. Consequently, the debtor’s pre-commencement management loses these rights. The court typically enumerates the debtor’s activities that will be managed by the provisional administrator, including payment of debts, disposal of the debtor’s assets and borrowing.

Contrary to civil rehabilitation proceedings and corporate reorganisation proceedings, in bankruptcy proceedings a temporary restraining order is not necessary because the period from the filing of a motion to commence bankruptcy proceedings until the court’s order to commence bankruptcy proceedings is typically relatively short.

**Commencement of proceedings**

Upon commencement of civil rehabilitation proceedings, in general, the pre-commencement management of a debtor does not lose their power to operate the debtor’s business or to administer and dispose of the debtor’s assets. The pre-commencement directors are responsible for turning around the debtor’s business under the supervision of a court-appointed supervisor.

On the other hand, upon commencement of corporate reorganisation proceedings, the power to administer and dispose of the debtor’s assets and to operate the debtor’s business is
exclusively vested in a court-appointed reorganisation trustee. The provisional administrator appointed by the court upon the filing motion usually becomes a reorganisation trustee upon commencement of corporate reorganisation proceedings.

Upon commencement of bankruptcy proceedings, the debtor company that is subject to the bankruptcy proceedings (the bankrupt company) loses the power to administer and dispose of its assets.

**Filing proof of claims**

In civil rehabilitation proceedings and corporate reorganisation proceedings, any creditor who has claims other than those classified as common benefit claims is required to file with the court a proof of claim within the filing period, as determined by the court, to be entitled to the voting right over a rehabilitation plan or reorganisation plan and other rights, including the right to repayment or refund under the plan. The procedures for filing a proof of claim in bankruptcy proceedings are almost the same as those in civil rehabilitation proceedings and corporate reorganisation proceedings.

In civil rehabilitation proceedings and bankruptcy proceedings, secured creditors whose claims are not fully covered by their security interests also need to file a proof of claim identifying the expected amount of the claims to be unsecured by the fair value of the collateral to make the amount treated as a general unsecured claim under a rehabilitation plan.

In contrast to the other two proceedings, in corporate reorganisation proceedings, secured creditors need to file both the amount of the secured claim that is covered by the fair value of the collateral and any remaining balance of the unsecured claim, because secured creditors are prohibited from exercising their security interest under corporate reorganisation proceedings.

In a bankruptcy proceeding, a filed proof of claim will be incorporated into a list of creditors. Distribution will be made pursuant to the creditors’ list after the amount of the filed claims is determined in accordance with the claim determination procedure as explained below. In general, a creditor who fails to file a proof of claim within the filing period may lose its right to distribution from the bankruptcy estate. Secured creditors whose claims are not fully covered by their security interest are also required to file the expected amount of claims to be unsecured by the fair value of the collateral.

In all three proceedings, a creditor may assign its claim to another party at any time during the proceedings. The change in the creditor needs to be filed if a creditor assigns its claim after filing a proof of claim.

**Determination of claims**

Any proof of claim duly filed will be assessed and decided whether to admit or not admit each proof of claim by the debtor-in-possession, reorganisation trustee or bankruptcy trustee during the investigation period as designated by the court. A creditor is also entitled to object to a specific proof of claim during the investigation period. A claim that is admitted by the debtor-in-possession, reorganisation trustee or bankruptcy trustee and that is not objected to by any creditor is determined as set forth in the filed proof of claim. If the debtor-in-possession, reorganisation trustee or bankruptcy trustee or any creditor objects to the validity or the amount of a specific proof of claim, such claim will be determined by the court upon
the filing of a petition for the court’s determination by the creditor against whose claim an objection is made. A party can appeal to the bankruptcy court’s order to determine the amount of the claim.

Rehabilitation plan and reorganisation plan/distribution
Based on the amount of the pre-commencement claims determined through the process mentioned above, the debtor-in-possession or reorganisation trustee is obligated to propose a rehabilitation plan in civil rehabilitation proceedings or a reorganisation plan in corporate reorganisation proceedings and file it with the court within the period prescribed by the court. Any creditor who has filed a proof of claim (and any shareholder in corporate reorganisation proceedings) is entitled to do so within the period designated by the court.

Both a rehabilitation plan and a reorganisation plan may provide for the amendment of the pre-commencement claims and other items that are allowed under the relevant law to restructure the debtor’s business. As to the amendment to the pre-commencement claims, a rehabilitation plan and reorganisation plan needs to provide a general standard that is applicable to all claims in the same class, including the recovery rate, the payment schedule and a debt-for-equity swap. Any amendment to the pre-commencement claims needs to meet the principle of ensuring the liquidation value, referred to as the ‘best interests of creditors test’ in the US. This principle requires that the recovery rates in civil rehabilitation proceedings or corporate reorganisation proceedings be higher than those in bankruptcy proceedings.

After the filing of a rehabilitation plan or a reorganisation plan, the court will issue an order to hold a creditors’ meeting to put the proposed plan to a vote. In civil rehabilitation proceedings, a proposed rehabilitation plan is approved at the creditors’ meeting with an affirmative vote by a majority of the creditors in attendance (or by way of a written vote) and an affirmative vote by holders of at least half of the total amount of the claims held by such creditors. In corporate reorganisation proceedings, a proposed reorganisation plan is approved at the meeting by each class of interested persons, and the requirements for approval by each class of interested persons are different as follows: for the class of secured claims, an affirmative vote by the secured creditors holding at least two-thirds the total amount of the secured claims is required; in general, for the class of unsecured claims, an affirmative vote by the creditors holding claims for a majority of the total amount of the unsecured claims is required; and for the class of shareholders, the shareholders have no right to vote in the event that the debtor’s debts exceeds its assets at the time of commencement of corporate reorganisation proceedings.

When the proposed rehabilitation plan or reorganisation plan is approved at a creditors’ meeting, the court issues an order to confirm the approved plan, unless it finds, among other things, that the plan is unlikely to be completed or that the plan is contrary to law, including the principle of equal treatment and the principle of ensuring the liquidation value. The approved and confirmed rehabilitation plan or reorganisation plan becomes effective upon the confirmation order becoming final and binding, and the debtor will be released from the pre-commencement debts as provided for in the plan. The creditors may exercise their rights pursuant to the provisions of the plan.

On the other hand, given that the purpose of bankruptcy proceedings is to liquidate a debtor to repay the debts, the bankruptcy trustee sells and disposes of all property belonging to the bankruptcy estate and distributes the cash to the creditors. Such distribution of funds is prorated to the amount of the claims determined through the claim-determination
process as described above. Any balance of the claims after final distribution upon selling and disposing of all property belonging to the bankruptcy estate will be discharged. After the final distribution of proceeds from the bankruptcy estate, the court will order the conclusion of bankruptcy proceedings.

**Conclusion of civil rehabilitation proceedings and corporate reorganisation proceedings**

A debtor-in-possession can emerge from civil rehabilitation proceedings, among other things, when the rehabilitation plan has been successfully implemented or when three years have passed since the court’s confirmation of the plan. Conversely, the court issues an order to discontinue civil rehabilitation proceedings, with or without a motion from a debtor-in-possession or a court-appointed supervisor, if it becomes obvious that the rehabilitation plan is unlikely to be completed. Any creditor holding claims of at least one-tenth of the total amount of all unpaid claims provided for in the rehabilitation plan may move to revoke the rehabilitation plan if all or part of its claims are or is not paid, as the case may be. Once civil rehabilitation proceedings are discontinued or the rehabilitation plan is revoked, the proceedings will be converted into bankruptcy proceedings.

A reorganised company can emerge from corporate reorganisation proceedings when: (1) the reorganisation plan has been successfully implemented; (2) the reorganisation plan has thus far been, and is likely to continue to be, performed without default, and at least two-thirds the claims under the reorganisation plan have been paid; or (3) it is certain that the reorganisation plan will be implemented even if all the requirements of (2) have not been met. Conversely, the court may issue an order to discontinue corporate reorganisation proceedings, with or without a motion from the reorganisation trustee, if it becomes obvious that the reorganisation plan is unlikely to be completed. In such case, the court will convert corporate reorganisation proceedings to bankruptcy proceedings.

**Disposal of the debtor’s assets outside the plan**

Similar to Section 363 sales in the United States, an increasing trend in Japan is for substantially all of a debtor’s assets to be sold to a buyer prior to the proposal of a rehabilitation plan or reorganisation plan. With the court’s permission, a debtor-in-possession in civil rehabilitation proceedings and a reorganisation trustee in corporate reorganisation proceedings may execute the sale of substantially all of the debtor’s assets. A buyer will obtain the debtor’s assets sold, but with liens on them, if any. Under Japanese law, creditors may not credit bid for the debtor’s assets.

In civil rehabilitation proceedings, cases have sometimes been seen in which a debtor files a motion to commence the proceedings along with an arrangement with a buyer under which the debtor will sell its business to the buyer prior to the proposal of a rehabilitation plan. This is called ‘pre-arranged’ civil rehabilitation proceedings. This type of pre-arranged filing, however, has not yet gained popularity because the break-up fee agreed on pre-commencement is classified as a general unsecured claim under Japanese law. A buyer needs to get around this issue by signing an agreement immediately upon commencement of civil rehabilitation proceedings.
Creditors’ rights and waterfalls

Classification of claims

Claims are classified depending on their nature and receive different treatment. Some classes are not subject to discharge or change in amount under insolvency proceedings, while other classes are. It is essential to understand which class a particular claim comes under in each insolvency proceeding. The following discussion explains the general nature of each class and its treatment in insolvency proceedings.

Administrative expenses

Similarly to how administrative expenses are treated under the US Bankruptcy Code, certain types of claims incurred to preserve a debtor’s going-concern value or bankruptcy estate are classified as a ‘common benefit claim’ in civil rehabilitation proceedings and corporate reorganisation proceedings or an ‘estate claim’ in bankruptcy proceedings. All amounts of such claims are paid from the debtor’s property or the bankruptcy estate from time to time when they are due and payable. Consequently, a creditor who has a common-benefit claim or estate claim is accorded priority over any other type of claim.

Secured claims

Generally, a secured claim that is treated as a right to separate satisfaction or a secured reorganisation claim is a claim secured by a mortgage, a pledge, a special type of lien or a special type of right of retention on certain property of the estate of the debtor, and remains secured at the commencement of insolvency proceedings. Further, a claim secured by such security interest will be treated as a ‘secured claim’ only to the extent of the sale price (in civil rehabilitation proceedings and bankruptcy proceedings) or the fair value (in corporate reorganisation proceedings) of the collateral. If the amount of the creditor’s claim exceeds the sale price or fair value of the collateral, the remaining balance after a foreclosure or sale of the collateral (in civil rehabilitation proceedings and bankruptcy proceedings) or the unsecured amount of the claim (in corporate reorganisation proceedings) is treated as a general unsecured claim.

In civil rehabilitation proceedings and bankruptcy proceedings, a secured creditor is treated as a creditor who holds a ‘right to separate satisfaction’. A secured creditor is entitled to foreclose on or sell the collateral outside of bankruptcy proceedings or civil rehabilitation proceedings, receiving repayment from the proceeds of the collateral. In this sense, a secured creditor has the priority on repayment from the value of the collateral; however, any unpaid amount of the claim through such foreclosure or sale will be treated as a general unsecured claim.

In corporate reorganisation proceedings, a secured creditor holds a secured reorganisation claim. Contrary to civil rehabilitation proceedings and bankruptcy proceedings, a secured creditor in corporate reorganisation proceedings may not foreclose on the collateral outside of the corporate reorganisation proceedings. Furthermore, the full amount of the claim corresponding to its security interest is not necessarily treated as a secured reorganisation claim; only the amount of the claim that is covered by the fair value of the collateral at the time of commencement of the corporate reorganisation proceedings is treated as a secured reorganisation claim, and the remaining amount that is unsecured by the collateral is treated
as a reorganisation claim (general unsecured claim). To evaluate the fair value of the collateral has a great significance, which will be conducted through the claim determination process, as discussed above.

**Preferred unsecured claims**

A claim that results from grounds or causes that existed before the commencement of insolvency proceedings and is secured by a general statutory lien or accorded any other priority under the relevant law is treated as a preferred unsecured claim in insolvency proceedings. A typical example of this claim is wages of employees and certain tax claims, because the relevant law accords priority on these claims.

In bankruptcy proceedings and corporate reorganisation proceedings, a creditor with such preferred unsecured claims may not exercise its rights outside the proceedings. Such creditor has a right to distribution from the bankruptcy estate in bankruptcy proceedings or a right in accordance with the reorganisation plan in corporate reorganisation proceedings, with priority over general unsecured claims.

On the contrary, a preferred general claim in civil rehabilitation proceedings is generally not subject to restriction on exercising rights under civil rehabilitation proceedings. A creditor with such claim may collect from the debtor from time to time when debts are due, outside of the proceedings, unless the court orders otherwise.

**General unsecured claims**

A claim that results from grounds or causes that existed before the commencement of insolvency proceedings and does not fall within any other class of claim is classified as a general unsecured claim. A general unsecured claim is subordinate to a preferred unsecured claim. A creditor with such general unsecured claims may not exercise its rights outside the insolvency proceedings, only being given a right to distribution from a bankruptcy estate or a right in accordance with a rehabilitation plan or reorganisation plan.

**iv Creditors’ committee**

Unlike some other jurisdictions, such as the United States, it is not mandatory for a creditors’ committee to be formed in Japan. The statutes of civil rehabilitation proceedings and corporate reorganisation proceedings, however, entitle the court to approve the participation of the creditors’ committee in the proceedings under certain circumstances, if any creditors have formed a creditors’ committee. The court-approved creditors’ committee is entitled to be actively involved in the restructuring of a debtor’s business. For example, the creditors’ committee may request a debtor or reorganisation trustee to make a status report on the restructuring of the debtor’s business. The expense for the creditors’ committee is reimbursed if the court finds that the committee contributed to ensuring the turnaround of the debtor. Nonetheless, it is quite rare for the creditors’ committee to be formed, although an increasing trend towards formation of the creditors’ committee can be seen in corporate reorganisation proceedings. This would be partly because the court oversees the whole proceedings, and thus, a debtor or reorganisation trustee is not allowed to control the proceedings ignoring the interests of the creditors.
v Information available to creditors

Any creditor may inspect or copy documents submitted by a debtor or trustee to the court so as to obtain information. The court may, however, restrict the inspection or copying by a creditor if the debtor or trustee demonstrates with prima facie evidence that a document contains information that would likely be significantly detrimental to the turnaround of the debtor’s business or would cause serious damage to the debtor’s property if it were to be inspected or copied by a creditor.

In addition, as a practical matter, a debtor-in-possession or reorganisation trustee in civil rehabilitation proceedings or corporate reorganisation proceedings voluntarily shares information of the debtor’s business and property with major creditors from time to time to provide a rationale on whether to vote for a rehabilitation plan or reorganisation plan proposed by the debtor or reorganisation trustee.

In bankruptcy proceedings, at a creditors’ meeting the bankruptcy trustee reports on the current status of liquidating the debtor’s assets.

vi Exceptional remedy for small claims and trade claims

Upon commencement of the proceedings, a debtor is afforded the protection of being able to suspend payment of their debts. During the period from the filing of a motion until commencement of the proceedings, a temporary restraining order affords a debtor such protection.

Trade creditors, however, will consider repudiating performance of their obligations out of strong negative concerns about collecting their future claims. A debtor’s going-concern value will rapidly deteriorate if a significant portion of the commercial trades necessary to run the debtor’s business is suspended in this manner. In civil rehabilitation proceedings or corporate reorganisation proceedings, the court, therefore, may exempt payment of small debts or certain trade claims from prohibition, taking into account the necessity to do so, the debtor’s business size, equitable treatment of other general unsecured claims and other factors.

vii Transactions that may be set aside

Japanese law grants a supervisor, a reorganisation trustee and a bankruptcy trustee powers to set aside certain transactions to preserve the debtor’s business as a going concern or to maximise the liquidation of the debtor’s assets. Outlined below are pre-commencement transactions that will typically be examined and reviewed upon commencement of insolvency proceedings; avoidance and bilateral executory contract.

Avoidance

A court-appointed supervisor in civil rehabilitation proceedings, a reorganisation trustee in corporate reorganisation proceedings and a bankruptcy trustee in bankruptcy proceedings may exercise the right of avoidance should an act be found to have been conducted that was prejudicial to creditors or granted a preference to a specific creditor. Contrary to some jurisdictions abroad, a creditor committee, an individual creditor or a shareholder has no standing (even derivative standing) to bring a motion before the court to exercise the right of avoidance.
The avoidance under Japanese insolvency proceedings is categorised into two major types: avoidance of acts prejudicial to creditors and avoidance of acts that grant a preference to a specific creditor.

In addition, any preference not obligated by the debtor in terms of the act itself or the time of the act may also be avoided if such act was conducted within 30 days before the debtor became unable to pay debts and if the creditor knew, at the time of the act, the fact that it would prejudice other creditors.

**Executory contract**

Upon commencement of insolvency proceedings, a debtor or trustee is authorised to choose to terminate or to continue the debtor’s ‘bilateral executory contracts’. Bilateral executory contracts are those in which the debtor and the counterparty obligate themselves reciprocally, so that the obligations of the debtor are correlative to the obligations of the counterparty and all or part of the obligations of both the debtor and the counterparty have yet to be performed at the time of the commencement of insolvency proceedings.

If a debtor or trustee chooses to continue a bilateral executory contract, the counterparty shall perform its obligations under the contract, and any right of the counterparty under the contract is treated as a common benefit claim or estate claim, and the counterparty is entitled to prior payment or refund for such claim.

If a debtor or trustee chooses to terminate a bilateral executory contract, the debtor or trustee is required to return any assets transferred if the counterparty is obligated under the contract to transfer such assets and if such assets are actually retained by the debtor or trustee, or compensate the counterparty if the counterparty is obligated under the contract to render services other than transferring assets or if the debtor or trustee does not actually retain the assets transferred by the counterparty. Any right of the counterparty to a refund of the price for its performance of obligations upon such termination is treated as a common benefit claim or estate claim, and the counterparty is entitled to a prior refund from the debtor’s assets or bankruptcy estate.

**III RECENT LEGAL DEVELOPMENTS**

i **Developments of turnaround ADR**

With regard to out-of-court workouts in Japan, Turnaround ADR is the most common framework for consensual out-of-court restructuring for medium- or large-sized companies in which a debtor may seek to reach an agreement with its financial creditors out of court with independent experts’ support, while continuing their business transactions. On the other hand, financial creditors can reduce their tax burden occurring because of the debt waiver through this procedure. In 2012, there were several developments of this procedure, because, in spite of certain positive reviews, it was not used for many cases (only about 50 cases filed from its establishment in 2007 to 2015). For ease of use, an ordinance of the Ministry of Economy, Trade and Industry revised it to mitigate the qualifications to be a procedure mediator, the restriction of the number of expert mediators for small cases with less than ¥1 billion of total liabilities, and the requirement to set the DIP financing in such proceeding.
ii Industrial Competitiveness Enhancement Act

The Industrial Competitiveness Enhancement Act (ICEA) seems to have had a major impact on the restructuring market. The ICEA was enacted on 4 December 2013, for the purpose of implementing the measures that were incorporated in the Japan Revitalisation Strategy, which was approved by the Cabinet on 14 June 2013, as the third arrow of Abenomics to strengthen the industrial competitiveness of Japan. To do this, the ICEA has taken several actions to deal with three major distortions of the Japanese economy: excessive regulation, underinvestment and delay in consolidation. Concerning the restructuring market, the ICEA aims to create an environment to promote early business rehabilitation by facilitating out-of-court workouts and enhancing support for local SMEs to start and rehabilitate businesses, which has aimed to create and foster a business environment to promote business restructuring that tries to significantly increase profits and promote venture businesses.

The ICEA provides important articles regarding out-of-court workouts regarding the reduction of the principal of corporate bonds under Turnaround ADR (Sections 56 and 57 ICEA). These articles provide a procedure under which the procedure mediators may confirm the necessity and reasonableness of the deduction of the principal of corporate bonds, and the court will consider such confirmation in the approval of the resolution at the Bondholders’ Meeting for such reduction. These seem to favour debtors that have issued corporate bonds to file Turnaround ADR, since whether the principal of corporate bonds may be reduced under such proceedings was not clear before such legislation was enacted.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

Although the overall number of statutory insolvency cases has been declining, analysis of the cases filed in 2015 shows that insolvency cases has primarily been arising from compliance violations and economic fluctuations occurring in other countries.

i Restructuring caused by compliance violations

In recent years, compliance violations, such as window-dressing financial statements, violation of industry law, cartels, mislabelling of food, false contracts and fabricated earthquake-resistance on buildings have caused financial difficulty in several restructuring cases, and have come to be recognised as serious risks to companies. Even though the compliance violations may relate to a certain product that represents a relatively small portion of a company’s sales, because of the bad impression that the public may form of that company, compliance violations may lead to scandals arising, which may lead to top management taking responsibility for the violations, or at worst, insolvency of the company.

The prevailing view is that the increased importance that has been placed on the corporate social responsibility (CSR) of companies is one of the reasons that there is an increasing risk of compliance violations. Today, a widely supported idea is that companies should not only maximise profit but should also take into consideration the interests of various stakeholders, and provide safe products and services that comply with laws and regulations. The greater the emphasis placed on CSR, the more likely it is that compliance violations will arise, and the extent and severity of public sanctions are also likely to be significantly greater. Thus, the generally held view is that top management is tasked with continuing to improve crisis management and risk control.
Restructuring caused by economic fluctuation of other countries

Another recent trend of restructuring cases is that the economic fluctuation in other countries has resulted in companies facing financial difficulties. In pursuit of low labour costs or to realise market potential, many companies produce and sell in foreign countries, and Asian countries, especially China, have deep economic ties to Japan. Recent research by Tokyo Shoko Research Ltd in 2015 has revealed that approximately 20 per cent of listed companies (694 of 3613 companies) in Japan have mentioned issues related to China, such as economy, politics or social policies, as business-related risks in their annual securities reports.

When looking at the recently filed cases in 2016, the number of insolvency cases caused by issues related to China has increased approximately 8.9 per cent year-on-year, and the common reasons are rising labour or procurement costs, fluctuations in foreign exchange and financial difficulties faced by their suppliers and customers that resulted from the impact of the economic slowdown, which was in turn caused by the economic situation arising from the tightening of monetary policy in China.

INTERNATIONAL

Recognition and assistance

Following the ratification by the Japanese government of UNCITRAL Model Law on Cross-Border Insolvency, the Act Concerning Recognition and Assistance for Foreign Insolvency Proceedings (the Act) was enacted on 1 April 2001, to coordinate the liquidation and rehabilitation of debtors that are engaged in international business activities and subject to insolvency proceedings commenced in jurisdictions other than Japan. Under the Act, where a debtor has an address, domicile, place of business or office in a foreign jurisdiction and an insolvency proceeding similar to bankruptcy proceedings, civil rehabilitation proceedings or corporate reorganisation proceedings in Japan has been commenced against the debtor in that foreign jurisdiction, the trustee (or the debtor, where no trustee has been appointed) who is authorised in the foreign insolvency proceeding to administer or dispose of the debtor's assets may file with the Tokyo District Court an application to recognise the foreign insolvency proceeding. The Act prescribes the circumstances where the court is required to dismiss such an application, such as where recognition of the foreign insolvency proceedings would be against the public policy of Japan or where a Japanese statutory insolvency proceeding has already commenced in Japan against the debtor.

Where the court has ordered recognition of the foreign insolvency proceeding, upon application by an interested person or at the court's own discretion, the court may also order:

a. the suspension (or revocation, if necessary) of a court or administrative proceeding, or a procedure for compulsory execution, provisional attachment or provisional disposition (collectively, 'execution procedures') with respect to any of the debtor's assets in Japan;

b. a general prohibition of execution procedures against any of the debtor's assets;

c. preservative measures (such as prohibition of the debtor's right to dispose of any portion of its business or any of its assets in Japan or the debtor's right to make certain payments); or

d. in limited circumstances, suspension of the enforcement of secured claims against assets of the debtor in Japan.
The court may also require that the debtor obtain the court’s approval to dispose of any of the debtor’s assets in Japan, to transfer its assets to a foreign jurisdiction, or to perform or engage in any other acts designated by the court. Any act by the debtor in violation of a court’s orders will be null and void and subject the debtor to criminal sanctions.

ii Amendment to the insolvency law

In response to the enactment of the Act, an amendment to Japanese insolvency law was also made to coordinate cross-border insolvency between more than two jurisdictions. For example, a Japanese trustee may ask a foreign trustee to cooperate and provide such information as is required to properly carry out the insolvency proceeding, and vice versa.

iii Treatment of foreign creditors

In principal, foreign creditors are treated in the same way as domestic creditors. Having said that, the ‘hotchpot’ rule, designed to ensure all creditors in the same class are equally treated, applies to a foreign creditor who is paid in a foreign jurisdiction. Under the rule, a foreign creditor, by claiming in a foreign proceeding, will not receive more than the proportion of payment that is received by other domestic creditors of the same class.

VI FUTURE DEVELOPMENTS

To ensure the smooth progression in out-of-court workouts, the possible ways of conducting debt-workouts under out-of-court workout proceedings by majority votes have been recently studied. A study group convened 12 times from March 2014 to March 2015. Although the study group was not made public, its members are believed to be renowned experts, and professors and representatives from the Ministry of Economy, Trade and Industry, Financial Services Agency, Ministry of Justice, Supreme Court and Bank of Japan participated as observers. This study group published a report in March 2015, and in it, several models that should be examined when the legislative amendment is considered were proposed. This report also includes a model to enable debt restructuring with dissenting creditors by the court approval, improve the operation of the simplified rehabilitation procedure and newly create the prompt reorganisation procedure. It seems likely that this report will lead to the reform of the platform for out-of-court workout procedures, making it much easier to use.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

Situated at the crossroads between Belgium, France and Germany, Luxembourg is a highly stable country and has registered consistent growth rates in the last two years with a GDP growth of 4.2 per cent in 2016 (compared to 4 per cent in 2015). Economists also forecast a GDP growth rate of 4.2 per cent in 2017.2

In Luxembourg, bankruptcy proceedings are currently the most common insolvency proceedings, while reorganisation proceedings remain rarely used in practice or are often used too late to avoid bankruptcy. In 2016 bankruptcy proceedings increased with a total of 1039 judgments (compared to 912 in 2015).3 In contrast, approximately 400 bankruptcy proceedings were opened by the Luxembourg District Court during the first half of 2017, thus reflecting a slight downward trend in 2017.

In this context, the business sector most affected by the high bankruptcy ratio is the services sector.4 These figures reflect the structure of Luxembourg’s economy, which is still led by the banking and financial sector. Around 150 credit institutions are established in Luxembourg. Some multinational companies, such as ArcelorMittal, Goodyear, DuPont, SES or Ferrero have chosen to successfully establish their European headquarters in Luxembourg. In recent years, multinational companies active in the high-tech and e-commerce industries have also decided to set up their European or international headquarters in Luxembourg.

Regarding Luxembourg reorganisation proceedings, few were opened in 2016. Two controlled management proceedings were opened in 2016, one of which was followed by a bankruptcy proceeding.

After the 2007–2008 crisis, proceedings were opened against several credit institutions with established subsidiaries or branches in Luxembourg, including among others some Icelandic banks (Kaupthing, Glitnir Bank, Landsbanki) as well as Lehman Brothers and Espirito Santo.

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1 Grégory Minne is a partner and Clara Mara-Marhuenda is counsel at Arendt & Medernach.
4 www.lequotidien.lu, 4 January 2017 quoting an analysis made by Creditreform.
II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

The Luxembourg legislative framework makes a distinction between proceedings involving the winding up of the debtor (bankruptcy proceedings), and proceedings aiming at the reorganisation of the debtor: controlled management, composition with creditors to avoid bankruptcy and suspension of payments.

Of the above, controlled management is the most-used reorganisation proceeding. Suspension of payments and composition with creditors have rarely been used successfully in the past decades.

It must be added that specific insolvency regimes govern credit institutions, insurance undertakings and investment funds, for example:

- the amended law of 18 December 2015 on the resolution, reorganisation and winding-up measures of credit institutions and certain investment firms;
- the amended law of 7 December 2015 on the insurance sector;
- the amended law of 17 December 2010 relating to undertakings for collective investment (UCIs);
- the amended law of 13 February 2007 on specialised investment funds;
- the amended law of 12 July 2013 on alternative investment fund managers;
- the law of 23 July 2016 on reserved alternative investment funds; and
- the amended law of 15 June 2004 relating to the investment company in risk capital (SICAR).

i Winding-up proceedings

Bankruptcy

Conditions for opening

Debtors who carry out commercial activities and who make a profession out of these activities may be declared bankrupt.

Two conditions have to be met cumulatively for a trader to be considered bankrupt: (1) he or she can no longer pay debts as they fall due (i.e., he or she is in a situation known as cessation of payments); and (2) he or she is no longer being granted credit.

The cessation of payments means the debtor is unable to meet his or her commitments. It implies that unpaid debts are certain, liquid and have fallen due on the day on which the bankruptcy judgment is delivered. It is not necessary that the debtor has ceased all his or her payments. The only relevant issue is to establish whether the default in payment to certain creditors is temporary or permanent. In the latter case, the existence of a single debt may lead to the cessation of payments. Inversely, temporary financial difficulties would not be sufficient.

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5 Articles 437 ff. of the Commercial Code.
6 Grand Ducal Decree of 24 May 1935 on controlled management.
7 Law of 14 April 1886 on composition with creditors, as amended.
8 Articles 593 ff. of the Commercial Code.
9 Article 437 of the Commercial Code.
10 Novelles, Droit commercial, T.IV, No. 203, p. 72.
11 Court of Appeal, 5 December 2012, docket no. 38410.
12 District Court of Luxembourg, 14 May 2004, docket no. 75935.
13 Court of Appeal, 20 February 1934, Pas. 13, p. 268.
The loss of creditworthiness may result from the inability to raise credit or from the creditors' refusal to accept any further delay in paying back the debt.  

**Procedure**

The district court with jurisdiction may declare the debtor bankrupt upon the request of: (1) one or more creditors; (2) the public prosecutor; (3) upon the declaration of the cessation of payment by the debtor himself or herself; or (4) *ex officio* by the court.

The proceeding is carried out by a receiver under the supervision of a bankruptcy judge, who are both appointed in the bankruptcy judgment. The receiver will have the judgment published in summary in the newspapers designated by the court.

The receiver represents both the debtor and the body of creditors.

The receiver prepares an inventory of all of the debtor's assets. If it appears that the assets are insufficient to cover the costs of the bankruptcy proceeding, the court may upon request of the receiver decide to end the proceeding immediately.

All creditors have to lodge a proof of their claim with the district court. The receiver decides together with the bankruptcy judge whether the declared claims have to be accepted or not. Creditors whose claims have been rejected may refer to the district court for judgment.

All assets of the debtor are realised either by private contract or by public auction as ordered by the court. The receiver seeks to obtain payment of all outstanding claims of the debtor.

The receiver administers and realises the debtor's assets and distributes the proceeds among the creditors on the basis of their rank and after the administrative costs and fees of the receiver are paid.

After all proceeds have been distributed among the creditors, the receiver submits a detailed report about the bankruptcy proceeding.

**Effects**

Upon the bankruptcy judgment, the debtor is no longer entitled to administer his or her assets or dispose of them. Any legal actions taken by unsecured creditors against the debtor are suspended. Certain preferential creditors are allowed to continue the proceedings they have initiated.

The district court determines a hardening period, (or suspect period), which covers the situation where the debtor, before having been declared bankrupt, was unable to meet its financial obligations and during which 'abnormal' transactions performed by the debtor may be declared void. Such clawback actions will be discussed below. In practice, the Court usually sets the hardening period to the legal maximum of six months prior to the bankruptcy judgment.

Agreements entered into by the debtor are not automatically terminated, with the exception of *intuitu personae* agreements, employment agreements and those including an insolvency termination clause. Generally any business activity of the debtor is stopped but in certain cases the receiver may decide to continue the business temporarily.

After bankruptcy proceedings have started, the debtor can propose a composition to its creditors. Proposals of composition after bankruptcy proceedings have started are, however, exceptional.

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14 Court of Appeal, 12 November 2014, Pas. 37, p. 340.
ii Reorganisation proceedings

Composition with creditors to avoid bankruptcy

Conditions

Composition with creditors is a protective measure that allows debtors in financial difficulties to avoid the declaration of bankruptcy, through the approval by the district court of an arrangement with its creditors for the settlement of their claims. As in bankruptcy matters, only traders may benefit from the composition with creditors proceedings, provided that they are considered honest but unfortunate.

Procedure

The debtor files the request before the district court with jurisdiction. The petition contains, among others: (1) a description of the events that have led to the financial difficulties; (2) a detailed evaluation of the debtor's assets; (3) a list indicating the names of his or her acknowledged or alleged creditors, their address and the amount of their claims; and (4) the composition proposal.

Subject to the request's admissibility, the district court appoints a delegated judge to establish a report of the situation of the debtor. However, should the court consider that the procedure is hopeless, it may order the bankruptcy _ex officio_. If the court approves the composition proposal, it sets a date for a meeting of creditors. The debtor must deposit a sum to cover the costs to be incurred for the publication of the notice to attend the meeting of creditors.

At the meeting of creditors, the delegated judge reports on the state of the affairs of the debtor and the debtor proposes an arrangement to his or her creditors. The composition can only be approved with the approval of the majority of the creditors (representing 75 per cent of the total claims accepted definitely or provisionally). Creditors whose claims are secured by a lien, a pledge or mortgage are not entitled to vote with regard to their claims unless they waive their lien, pledge or mortgage. Following the meeting with creditors, the court convenes a hearing for the final approval of the arrangement.

The judgment approving the composition (or not) is issued and, within three days, it is posted in the auditorium of the court and published in summary form in the designated newspapers.

Effects

Once approved, all enforcement measures are temporarily suspended subject to financial collateral arrangements (see Section II.iv, _infra_). The arrangement is binding upon all creditors but only applies to liabilities incurred or commitments made before such arrangement.

An appeal or objection by the creditors or the debtor against the judgment approving the composition (or not) has no suspensive effect.

Suspension of payments

Conditions

Suspension of payments\textsuperscript{15} may be granted to the debtor, who has suffered temporary liquidity problems, allowing him or her to suspend payments to creditors for a given period of time.

\textsuperscript{15} Articles 593 ff. of the Commercial Code.
It may be granted either: (1) if the debtor, due to exceptional and unforeseen events, has to temporarily cease his or her payments but the verification of the balance sheet shows that he or she has sufficient assets or income to satisfy the creditors in principal or interest; or (2) if the debtor is currently in deficit but there are strong indications that he or she may rebalance his or her assets and liabilities (i.e., return to solvency).

**Procedure**

The request, accompanied by a description of the events on which the request is based, a list of the creditors and a detailed estimate of the debtor’s assets and liabilities, is filed by the debtor simultaneously before the district court and the Supreme Court.

The district court appoints one or more experts to examine the affairs of the debtor and a judge to supervise the operations.

The judge will hand down his report in the presence of the creditors convened on the date (within 15 days of the request) set by the president of the district court. On such date, the creditors are heard, they declare the amount of their claims and decide whether they approve or reject the request for suspension of payments.

The suspension of payments may only be granted with the approval of the majority of creditors representing three-quarters of the aggregate debt.

After the meeting of the creditors, the district court hands down its opinion, which is transmitted, together with the relevant documents, to the attorney general of the Supreme Court.

The Supreme Court hands down its decision within eight days. If the Supreme Court grants a suspension of payments, it determines its duration and appoints one or more commissioners.

**Effects**

The management body of the debtor stays in place during the suspension of payments but acts under the supervision of a commissioner. The creditors’ rights are suspended for the duration of the proceeding. The suspension of payments only applies to the commitments entered into before such suspension of payments was granted.

**Controlled management**

**Conditions**

A trader who is either: (1) not able to raise additional credit; or (2) has difficulties meeting his or her commitments may apply to the district court for an order for controlled management, under which the management of the debtor is placed under the control of one or more commissioners designated by the court. A debtor cannot avail himself or herself of the controlled management regime if he or she is already considered bankrupt, (i.e., if the two conditions for bankruptcy referred to above are met).

**Procedure**

The application for controlled management, accompanied by a list of the creditors and evidence that the prospects for reorganisation (or orderly liquidation) are realistic, is filed *ex parte* by the debtor before the district court. Only the debtor has standing to seek controlled management and such proceeding may not be initiated by a third party (e.g., a creditor or a shareholder).
The purpose of controlled management is to allow either a reorganisation or an orderly winding up of the debtor through the realisation and distribution of his or her assets.

Upon the filing of the application, unless the financial situation of the debtor appears to be hopeless, the district court issues a first judgment including the appointment of a judge delegated to examine the debtor’s affairs and to report to the court. If the debtor’s prospects for reorganisation (or orderly liquidation) are not realistic, bankruptcy will be the only alternative.

If the court comes to the conclusion that a reorganisation (or orderly liquidation) is possible, it will grant the application for controlled management and appoint one or more commissioners who have to submit a reorganisation plan or a plan regarding the realisation and distribution of the debtor’s assets.

The judgment of the court is issued from the delegated judge’s report, after having heard the debtor (excluding the creditors). The court’s judgment will be published in summary form for the information of all creditors.

The commissioners will report to the court and submit a reorganisation (or a liquidation) plan, depending on the financial capacities of the debtor. The plan shall determine:

a whether unsecured creditors’ claims will be paid in full or in part, with or without further rescheduling; and

b whether interest accruing after the date of the judgment delegating a judge or the controlled management decree will be due.

The contents of the commissioners’ proposal is individually notified to the debtor’s creditors and also published in the Luxembourg Official Gazette.

The creditors shall vote within 15 days of the notification and the publication on the reorganisation or liquidation plan, which, upon approval of a majority of creditors representing more than half of the debtor’s aggregate debt, and the court’s consent, will be binding upon the debtor and all creditors. The debtor or his or her creditors may appeal against the court’s judgment to accept or reject the plan agreed to by a majority of the creditors. The court’s judgment approving the plan is, however, provisionally enforceable pending the outcome of the proceedings in the Court of Appeal.

Creditors may submit observations to the court before it takes its decision to accept or reject the plan. Creditors abstaining from the vote are deemed to have voted in favour.

Once the plan has received final approval, its content is applicable and binding upon the debtor and all his or her creditors, whether in agreement or not. If, however, the plan is rejected by the creditors or by the court, the court either pronounces bankruptcy or allots further time to the commissioner for the submission of an alternative plan.

All debts of the debtor originating before the date of designation of a delegated judge by the first judgment of the district court are taken into consideration. Further debts, duly authorised by the judge and, afterwards, by the commissioner, which are incurred during the mission of the delegated judge and of the commissioner, may also be taken into consideration in the plan.

If the plan is approved by the creditors and the court, the debtor in principle regains control over his affairs. Otherwise, bankruptcy proceedings will normally be instituted.

Effects

The commissioner does not replace the debtor’s management but supervises it. The decisions taken by the debtor’s management must be approved by the commissioner or should be
otherwise voidable. In addition, the commissioner may initiate proceedings to void any ‘abnormal’ transactions (such as preferential payments) made by the debtor within a period of up to six months and 10 days prior to the application for controlled management. They may also initiate liability actions for mismanagement against the directors.

As from the court’s judgment, enforcement rights of the creditors against the debtor’s assets are suspended and any voluntary payments from the debtor require the prior authorisation of the delegated judge.

Creditors’ enforcement rights remain suspended for the duration of the controlled management. Depending upon the wording of the court’s judgment, they may have to submit their proof of claim.

iii Informal (out-of-court) restructuring
There is currently no legal framework in Luxembourg for an out-of-court debt restructuring. However the debtor may enter into out-of-court arrangements with his creditors.

iv Specific topics
Taking and enforcing security
The amended law of 5 August 2005 on financial collateral arrangements (the Collateral Law), implementing Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements, provides exceptional protection to collateral takers in the case of reorganisation or winding-up of the collateral giver. In substance, where a security interest is subject to the Collateral Law, Luxembourg insolvency provisions (where the collateral giver is in Luxembourg) or foreign law insolvency provisions (where the collateral giver is not in Luxembourg) are not applicable, thus enabling the collateral taker to enforce its security interest notwithstanding the reorganisation or winding up of the collateral giver.16

Under the Collateral Law, netting agreements (under which the parties agree to set off their mutual obligations) with respect to claims or financial instruments are also enforceable notwithstanding the existence of Luxembourg or foreign reorganisation or winding-up proceedings initiated against the defaulting party.

Duties of directors of companies in financial difficulties
General principle
As a general principle, the directors of a Luxembourg company are not liable for the debts incurred by that company.17 However, the directors’ general duty is to perform their duties in the best interest of the company and they may be held liable if they failed to act in a prudent and diligent way and caused damages to the company (contractual liability) or to third parties (tort liability). In case of bankruptcy, the receiver, who represents both the company and the body of creditors, may initiate liability actions against the directors.18

16 Article 20(4) of the Collateral Law.
17 Article 58 of the Companies Law.
18 Article 59, Section 1 of the Companies Law provides for the personal and individual liability of a director towards the company for management errors. Article 59, Section 2 provides that a director shall be liable to the company and third parties in the event that the company or third parties suffer a loss due to a breach of either the law on commercial companies or the company’s articles of incorporation.
Specific provisions
The amended law of 10 August 1915 on commercial companies (the Companies Law) includes specific provisions on the duties of directors of Luxembourg companies in financial difficulties.

If as a result of a loss, the net assets of a company are reduced to an amount that is less than half of its share capital, the board of directors shall convene a shareholders’ general meeting to deliberate on the possible dissolution of the company.19 In the event of a breach of this provision, the directors may be declared personally jointly and severally liable towards the company for all or part of the increase in the loss.

The Companies Law provides for specific criminal offences, such as the failure to publish the balance sheets and compulsory reports20 or the payment of fictitious dividends.21

The main legal provisions dealing with the personal liabilities of directors in case of bankruptcy are laid down in the Commercial Code.

The directors must file for bankruptcy within one month from the date that the company has ceased its payments.22 Failing that, they may be criminally liable for negligent or fraudulent bankruptcy.23

If a director has contributed by a serious offence to the bankruptcy of the company, the court may declare that such director shall be prohibited from exercising directly or indirectly any commercial activity as well as any function of director, manager, auditor or any function implying the power to undertake obligations on behalf of a company.24

Any director may be declared personally bankrupt in case of bankruptcy of a company, if he or she has used the company to act in his or her personal interest; has used the company’s assets as if they were his or her own; or has carried on, in his or her personal interest, any loss-making activity that would inevitably lead the company into bankruptcy.25 It makes no difference whether the director has been lawfully appointed by the company or has acted in such capacity.

The court may decide that the directors of a company are liable for the outstanding debts of that company, if gross negligence by the directors has contributed to the bankruptcy and if the assets of the company do not allow the payment of all the company’s creditors. Such gross negligence is appreciated in concreto by the court.

The same liability applies in cases where one or several directors have misused their authority in order to continue any loss-making activity of the company, for their own personal benefit and without taking reasonable measures to avoid bankruptcy.

The above rule does not only apply to directors who are in office at the moment the company is declared bankrupt but may also apply to any directors that have in the past contributed to the bankruptcy through their actions, to lawfully appointed or to de facto directors.

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19 Article 100 of the Companies Law.
20 Article 163 of the Companies Law.
21 Article 167 of the Companies Law.
22 Article 440 of the Commercial Code.
23 Articles 573 ff. of the Commercial Code.
24 Article 444-1 of the Commercial Code.
Clawback actions

Any payments made or transactions concluded by the management of the debtor, but not by the receiver, during the bankruptcy proceedings, are null and void.

Moreover, the Commercial Code provides for specific rules applicable to transactions entered into by a debtor who has been declared bankrupt during the hardening period or made to defraud the rights of creditors, regardless of the hardening period. These rules do not apply to financial collateral arrangements subject to the Collateral Law (e.g., pledges or transfer of title for security purposes).

Transactions concluded during the hardening period

The following transactions are automatically null and void if concluded by the debtor during the hardening period or during the 10 days preceding the hardening period: any transaction pertaining to the transfer of assets without consideration or where the consideration received by the debtor is notably insufficient; any payment made in respect of debts that have not yet matured; any payment made by any other means than cash or trade bills in respect of matured debts; the creation of any contractual or judicial mortgage and the granting of any pledge on any asset of the debtor in order to secure pre-existing debts.26

Any other payment made by the debtor for any matured debt and any transaction for consideration entered into during the hardening period may be declared null and void if the counterparty of the debtor had due knowledge of the fact that such debtor was in cessation of payments at that time.27

The action seeking a declaration of invalidity or annulment of a transaction by the court may only be brought by the receiver, who represents the body of creditors.28

Transactions made in violation of the rights of creditors, regardless of the hardening period

Any transaction or payment made to defraud the rights of the creditors of a debtor is null and void, irrespective of the date on which it occurs.29

The receiver may challenge any fraudulent payments and transactions made prior to the bankruptcy, regardless of the hardening period, subject to proof that the creditors suffered a loss and that the transaction was made by the debtor to defraud the rights of his or her creditors.

III RECENT LEGAL DEVELOPMENTS


27 Article 446 of the Commercial Code.
28 Luxembourg District Court, 28 May 1925, Pas. 11, p. 206.
29 Article 448 of the Commercial Code.
The law provides for measures for early intervention and the resolution of credit institutions and some investment firms, either on an individual or a group basis, and designates the Luxembourg financial regulator as the resolution authority for Luxembourg. The main resolution tools granted to the resolution council are: (1) the sale of businesses by competent authorities without shareholder consent; (2) the creation of a bridge institution; (3) an asset segregation allowing for a transfer of toxic assets to a ‘bad institution’; and (4) a bail-in.

The law also provides for the reorganisation and winding up of credit institutions, investment firms and other professionals of the financial sector.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

As set out in the introductory section, 2016 saw a 12.6 per cent increase in the number of bankruptcies in comparison with 2015. The sector most affected by bankruptcies was the services sector.30

In September 2016, Telecom Luxembourg Private Operator was placed under controlled management and avoided bankruptcy through its acquisition by the French NomoTech Group, through its Luxembourg subsidiary LuxNetwork SA.31

V INTERNATIONAL

In the context of cross-border insolvency proceedings, Regulation 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (the New Insolvency Regulation) applies to insolvency proceedings opened as from 26 June 2017.

The New Insolvency Regulation replaces the Regulation 1346/2000 of the Council of 29 May 2000 on insolvency proceedings (the Old Insolvency Regulation) as from 26 June 2017. The Old Insolvency Regulation continues to apply to insolvency proceedings that have been opened before 26 June 2017.

Without going so far as to completely change legislation that has already proved its worth, the New Insolvency Regulation contains substantial innovations intended to make up for the deficiencies of the Old Insolvency Regulation and to take into account the development of international insolvency law.32

Like the Old Insolvency Regulation, the New Insolvency Regulation defines a legal framework for cross-border insolvency proceedings as it governs in particular issues linked to jurisdictional competence, the recognition of insolvency proceedings and applicable law.

The New Insolvency Regulation also takes into account recent developments in the domain of insolvency by introducing substantial innovations, such as the extension of the scope of the rules to proceedings intended to rescue distressed debtors, the clarification of the notion of ‘centre of main interests’ (COMI) and the measures intended to combat

forum shopping, the strengthening of relations between the main proceedings and secondary proceedings, the improvement of the treatment of creditors and the establishment of a regime for the treatment of the insolvency of groups of companies.\textsuperscript{33}

The Luxembourg insolvency proceedings referred to in the New Insolvency Regulation are as follows:

a  bankruptcy proceedings;  
b  controlled management;  
c  composition with creditors;  
d  special winding-up regime applicable to notaries; and  
e  procedures applicable to collective debt settlement in the context of over-indebtedness.

Suspension of payments is excluded from the above list of Luxembourg insolvency proceedings.

\section*{VI \hspace{4ex} FUTURE DEVELOPMENTS}

\subsection*{\textit{i} Directive}

A proposal from the European Commission 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\textsuperscript{34} was released by the end of 2016. The proposal aims to reduce significant barriers to the free flow of capital stemming from differences in the restructuring and insolvency frameworks of the Member States that should have in place key principles on effective restructuring and second chance frameworks, and measures to make insolvency proceedings more efficient by reducing their length and associated costs and improving their quality.

\subsection*{\textit{ii} Future insolvency reform}

A reform of insolvency legislation is expected in the future. Its purpose is to improve the reorganisation of debtors and to implement new restructuring tools. A draft bill is pending and currently subject to amendment.\textsuperscript{35}

\begin{flushright}
\footnotesize
\textsuperscript{33} Ibid.  
\textsuperscript{35} No 6539 on business preservation and modernisation of bankruptcy law.
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I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

Restructuring practice in Mexico in regard to corporations of any considerable size, measured by sales or assets, continues to focus on consensual, out-of-court workouts. Indeed, through the decades, since the 1980s, Mexico has been a jurisdiction of highly successful negotiated solutions, with the development and participation of highly sophisticated and experienced lawyers, bankers and financial advisers.

Perhaps no more than 20 material cases (involving liabilities over a US$100 million threshold) have gone through a formal insolvency proceeding (concurso mercantil) since the Law on Commercial Insolvency was passed in 2000. Notably, in the past two years, the three main homebuilders, with Corporación Geo being the largest to date, having restructured US$2.9 billion, were among the most recent cases. Obviously, with such a small volume of corporate cases, the federal judiciary has not found a need to actually develop specialised courts in insolvency matters.

In the past year, it has become fairly evident that Mexico as a jurisdiction has significantly failed in advancing the efficient development of a fair, equitable, transparent, reliable and predictable restructuring process through a court-supervised concurso mercantil.

There have been a number of court rulings that have fed the notion that concurso proceedings may be derailed with the use of excessive procedural manoeuvres, given a continuing emphasis on compliance with extreme formalities and an unfortunate use of rather inoperable formats developed for very small family-owned company restructurings. Several controversial rulings have placed a question mark on the very existence of a rule of law, and the prevalent use of procedural delaying tactics based upon extended notions of due process and ‘respect of human rights’ have added to the ambiguity of what is otherwise clearly intended to be a reliable procedure aimed at conserving productive enterprises as ongoing concerns.

Not only do critical supporting factors remain dubious, such as the access to DIP financing, but a number of isolated decisions have led to extended procedures and a general and evident lack of adherence to the strict time frames provided for by the Concurso Law.

Among the more notorious decisions are: (1) the Third and Ninth Court of Appeals in Civil Matters of the First Circuit have put into question the effectiveness of well-established structured financing transactions, whereby through a trust a company has sold future receivables or guaranteed payment obligations with such future receivables, in favour of a financial institution, by holding that if the debtor enters concurso, other provisions of ‘public

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order’ come into play protecting broader interests replacing commercial considerations and laws, and thus all future receivables will become a part of the estate, ‘true sales’ notwithstanding (cases arising in the concurso of Oceanografía); (2) the Third of Appeals, two years after the exit from concurso of Corporación Geo, ruled, based on a provision of the Law found in the chapter of liquidation, that a company cannot exit concurso with a plan, even if approved by an overwhelming majority, if there are any appeals pending (appeals may well take years to be concluded), which criteria, if generalised, will mean the return to endless and obscure procedures; and (3) in a case involving Abengoa, the Sixth Federal Court in Civil Matters of Mexico City ruled, that notwithstanding that a duly approved auditor confirmed that the company did not fall under the parameters and definitions of insolvency established in the Concurso Law, there are other higher interests that should be protected, and then proceeded to involuntarily declare the company in concurso as insolvent. There were other recent rulings principally sustained on arguments of protection of the ‘human right to due process,’ which have added to the uncertainly as to the outcome and reliability of formal in court insolvency procedures.

Nevertheless, the decisions have been isolated and are being contested or have been overturned. Moreover, in a publicised matter, the Council of the Federal Judiciary took disciplinary action against a judge known for his creativity.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

The Concurso Law was published in May of 2000 and has been amended twice, in December 2007, with the introduction of the Mexican version of a pre-pack, and in January 2014, with the more significant amendments summarised in Section III supra.

The Concurso Law is a complex statute, which will require continued careful application and interpretation by the federal courts, which have exclusive jurisdiction over insolvency proceedings. (although the concept has been legally challenged recently, it has been done so unsuccessfully up until now). Nevertheless, the relatively few cases that have been filed under the Concurso Law have mostly continued to fail in following strict adherence to the time-sensitive provisions of the Law, and certainty as to a final outcome continues to be clouded, although a handful cross-border cases have been true successes. In any event, there seems to be improvement when compared to the prior statute of 1943 (for example, the proceeding of Altos Hornos de México took over 17 years to get to the approval of an exit plan that is to be implemented in future years).

The following subsections present the principal aspects of the Concurso Law.

i One proceeding

The Concurso Law provides for one sole insolvency proceeding (concurso mercantil), encompassing two successive phases: a conciliatory phase of mediation among creditors and debtor, and bankruptcy. The objective of the conciliatory phase is to conserve the business enterprise as an ongoing concern through a restructuring agreement. On the other hand, the stated purpose of bankruptcy is to liquidate the business. Prior to a debtor being placed in concurso, the process includes a preliminary visit stage to verify whether the commencement standards have been met, unless a pre-pack is filed. Unfortunately, IFECOM formats relating to the visit seem to be designed for an audit of the company and not for a two-week review of the balance sheet, leading to delays and confusion.
ii  Procedural terms
An important part of the Concurso Law involves measures to expedite the handling of mechanical aspects of insolvency. Procedural terms in legal proceedings are relatively short, yet most courts fail to abide by them.

Provisions in the law as to procedural exceptions in legal proceedings should no longer result in the automatic suspension of the conciliatory proceeding, as was the case under the prior law, yet federal judges continue to apply measures that have, in fact, halted concurso proceedings.

The conciliatory stage is designed to be completed in 185 calendar days in the best of cases, although two 90-day extensions may be granted if a qualified majority of creditors so approves. The Concurso Law clearly underlines that in no event may the conciliatory stage be extended beyond 365 days, whereupon bankruptcy and liquidation of assets are, in theory, to begin immediately. In practice, this is not the case.

iii  Petition for commercial insolvency
A business enterprise that is generally in default with respect to its payment obligations will be declared commercially insolvent. The debtor, any creditor or the Office of the Attorney General may file for insolvency.

The Concurso Law establishes precise rules that determine when a debtor is ‘generally in default’. The principal indications are the failure by a debtor to comply with its payment obligations in respect of two or more creditors, and the existence of the following two conditions: 35 per cent or more of its liabilities outstanding are 30 days past due; and the debtor fails to have liquid assets and receivables, which are specifically defined, to support at least 80 per cent of its obligations, which are due and payable.

Specific instances, such as insufficiency of assets available for attachment or a payment default with respect to two or more creditors, are considered by the Concurso Law to be facts that by themselves will result in a presumption of insolvency.

In theory, the 2014 amendments allow the debtor to file for concurso if it can be anticipated that it will be generally be in default with respect to its payment obligations or falling within one or more of the presumptions of insolvency within 90 days from the petition filing. Involuntary filings have been largely unsuccessful because of the many formalities that must be met.

iv  Jurisdiction
The federal courts have jurisdiction over concursos. While it is a fact that district judges are overburdened with constitutional challenges (amparos) and have little practice in regard to mercantile matters, the selection process, supervision, continued education and preparation of federal judges have been substantially improved in the recent past. Salaries have been materially increased, and there has been a greater impartiality. Nevertheless, the courts have been reluctant to accept insolvency cases given their considerable workload, among other reasons, and when they have accepted a major matter, the mere size and thousands, if not millions, of pages involved have made it a huge task to address and preside over these proceedings efficiently.
v Experts

The Concurso Law provides for the use and training of experts in the field of insolvency with IFECOM as an entity to coordinate their efforts and provide continuing education.

The specialists who have a role in proceedings under the Concurso Law are:

- **a** the auditor, whose duties are to determine whether the debtor complies with the commencement standards and who participates in the proceeding up to the judge’s declaration of insolvency;\(^2\)
- **b** the conciliator, who is appointed in such declaration and who has broad powers to mediate, to take steps to protect the enterprise as an ongoing concern or to immediately begin bankruptcy and who takes on the significant responsibilities in a concurso; and
- **c** the receiver, who may or may not be the conciliator and whose principal function is to proceed with the sale of assets and payment of claims.

The judge also has a principal role, although the function of the mediator or conciliador is substantial (including the authority to approve DIP financing).

Those who wish to act as auditor, conciliador or receiver must ask IFECOM to register them in the special registry maintained by IFECOM. It is unfortunate that the registry, especially for complex cases, has not been opened for the large accounting or insolvency advisory firms, only for individuals.

There are numerous restrictions prohibiting conflict-of-interest relationships. The appointment procedure is to be based on random, electronic selection from the classes and ranges of experience pertaining to the experts registered with IFECOM, classes that vary in accordance with the complexity and asset size of the business enterprise in question.

A qualified majority of creditors may replace or appoint a professional as conciliador or receiver even if the professional is not registered with IFECOM. In cases involving the insolvency of a company operating under a federal concession, the conciliador may be appointed at the request of the corresponding authority, such as the Ministry of Communications in the case of corporations in the telecommunications industry, as was the case with the SATMEX proceeding.

vi Related companies

Insolvency proceedings of two or more entities are not joined, although controlling and controlled companies’ proceedings will be joined, but will be handled in separate records. A petition must be filed individually by each group member; nevertheless, the 2014 amendments introduced provisions to allow for the joint petition by multiple group members (untested as of today). Mexico does not, however, recognise substantive consolidation.

vii Identification of creditors and declaration of insolvency

The debtor that requests a judgment of declaration of concurso mercantil must furnish detailed lists of creditors and debtors, with a description of the nature of the debts. The amendments

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2 Although the 2014 amendments introduced the possibility of avoiding the ‘visitation stage’ in pre-packed filings, thus saving weeks of bureaucracy, the author is of the view that there is a benefit of having an auditor complete the many complex IFECOM formats that have proven to be indispensable in the ongoing proceeding.
introduced a few relevant additions to the petition request: a copy of the corporate resolutions that approved the filing, a proposed reorganisation plan and enterprise conservation plan, which were intended to include DIP financing terms.

Absent a pre-pack, the day after the judge admits the petition, he or she must send a copy to IFECOM, ordering it to designate a visitor in five days. The judge will order the visit and immediately notify the debtor. The visitor will review the books and records of the debtor. The visitor will prepare minutes of the visit, which must also include a list of all creditors in IFECOM formats. The visitor may request that the judge issue precautionary measures needed to preserve the assets of the debtor. The visitor will render a report to the judge that will be sent to the debtor and the creditors for their respective comments, if any.

Within a maximum term of 83 days as of the initial filing, the Law provides that the judge must render a judgment of mercantile insolvency, which, among other things, must contain:

a an order to IFECOM to appoint a conciliator;
b a declaration of the opening of the conciliatory stage unless the debtor has requested bankruptcy;
c an order to the debtor to deliver all books and records to the conciliator;
d an order to the debtor to suspend the payment of its pre-petition indebtedness, other than those that are deemed to be essential for the continuation of the business enterprise;
e an order to freeze all asset foreclosure and attachment proceedings; and
f an order to publish a notice to all creditors (a filing proof of claim), so that they may appear in the proceeding, although this requirement is no longer mandatory.

The extensive participation of the conciliator in the proceedings should also be noted. The conciliator is also responsible for proposing the creditors who should be recognised and is mandated to proceed with notices and publications pursuant to provisions that are very specific as to terms. Formalities are always a major issue and creditors must be aware of tactics delaying the publications that may lead to material delays and uncertainty.

viii Effects of a declaration of insolvency

Once the initial judgment declares the debtor in a stage of *concurso mercantil*, attachment or foreclosure of assets is suspended during the conciliatory stage, with the sole exception of labour-related obligations; tax-related attachments or liquidations under specific provisions of the Concurso Law are specifically stayed.

The debtor maintains the administration during the conciliatory stage, although the conciliator may request the court removal of the administration. With the express purpose of conserving the enterprise as a going concern within the conciliatory stage, the conciliator is given broad powers to decide on the acceptance or rejection of contracts (within certain parameters), the contracting of new loans - although most litigators insist that the judge must approve - and the sale of non-essential assets. In all cases, the conciliator must constantly report to the court every 72 hours – which is obviously burdensome in major filings – of each and every payment to any supplier or person, irrespective of the amount.

ix Debts in foreign currency

The Concurso Law clearly attempts to correct prior judicial practice, which converted foreign currency debt to pesos early on in the proceeding. The Law establishes provisions that are
designed to protect the monetary value of creditor loans. All peso-denominated obligations are converted into inflation-linked units known as UDIs; foreign currency-denominated obligations are converted into pesos at the prevailing rate of exchange on the date the insolvency judgment is rendered and then converted into UDIs. Only claims with a perfected security interest (mortgages or pledges – but not in regard to guarantee trusts) will be maintained in their original currency or unit of account, and will continue to accrue interest, but only to the extent of the value of the collateral.

x Fraudulent conveyances

The Concurso Law provides for a general rule as to the period when insolvency is presumed to have begun, which is of 270 calendar days prior to the judgment declaring insolvency (the ‘retroactive period’). Nevertheless, upon the reasoned request of the conciliador, the interventors, who may be appointed by the creditors to oversee the process, or any creditor, the judge may determine a longer period (at most, three years). Conveyances that are not arm’s-length or commercially sound, and the creation or increase of security interests within the retroactive period will be presumed fraudulent to creditors and will not be recognised.

xi Netting

The general concept of netting is recognised by the Concurso Law, which specifies that netting is mandatory for parties to a transaction recognised by the Law, pursuant to terms agreed upon in the relevant contract, on the date of the declaration of insolvency, in respect of liabilities and rights arising from master or specific agreements entered into in connection with financial derivative transactions, reportos (Mexican law-governed repurchase transactions), securities lending transactions and other equivalent transactions.

Mandatory netting is also recognised by the Law as an exception to the ‘cherry-picking’ powers given to the conciliador (i.e., mandatory netting applies, regardless of whether the conciliador decides to assume or reject the relevant executory contract).

Under the Concurso Law, the effects of a netted transaction are deemed to survive, even if the transaction was netted during the insolvency retroactivity period (as mentioned previously, generally 270 days). This provision constitutes another development that should give financial institutions certainty when netting, on a bona fide basis, financial derivative transactions.

Obviously, as a prerequisite to netting, the Concurso Law accepts the principle of early termination. It establishes that financial derivative transactions and reportos transactions, maturing after the date of the declaration of insolvency, shall be deemed terminated precisely on that date.

In connection with financial derivative transactions, the Concurso Law provides that, if the relevant agreement does not specify the terms pursuant to which a transaction is to be closed-out and netted, the value of the underlying assets and liabilities is to be determined on the basis of their market value on the date of the declaration of insolvency; if such market value is not available or cannot be demonstrated, the conciliador may request an experienced third party to determine such value.

The general concept of netting reflected in the Concurso Law should be broad enough to encompass transactions such as New York or English law-governed repurchase transactions, securities loan agreements and any other transactions that may be expressed in other currencies. However, the broad terms of the relevant provisions in the Concurso Law, may result in abuses that would seem to go beyond the intent of the drafters of the
Law (i.e., creditors claiming that transactions that are not financial derivative transactions, and, therefore, not benefiting from netting provisions, be considered as derivatives, by virtue of the manner through which such transactions were documented). It is also expected that complex derivatives will be challenged as invalid, based on arguments of *ultra vires*, lack of authority, disproportional elements and the like, specifically in times of unforeseen volatility. While such issues have been addressed by US courts (principally in New York) in favour of creditor banks in matters where Mexican companies were plaintiffs, the subject of complex derivatives is far from settled in Mexico.

Under the Concurso Law, once obligations are netted, if a liability by the insolvent debtor results, the relevant creditor would need to claim it in the bankruptcy proceedings; if a liability by the relevant creditor results, such creditor would need to satisfy its obligations with the conciliator within 30 days of the date of the declaration of insolvency.

**Restructuring plan; pre-packaged insolvency**

To become effective, a restructuring plan must be subscribed to by the debtor and recognised creditors representing more than 50 per cent of the sum of the total recognised amount corresponding to unsecured creditors and the total recognised amount corresponding to secured or privileged creditors subscribing the plan. For acceptance, the favourable vote of 75 per cent of third-party unsecured claims if unsecured inter-company claims account for more than 25 per cent of unsecured claims must be obtained. Any such plan, with the validation of the court, would become binding on all creditors and the insolvency proceeding will be considered as final and concluded.

The Concurso Law provides that the insolvency procedure can begin at the conciliation stage (i.e., avoiding the visit) if the debtor, together with creditors representing at least 50 per cent of the credits so requests, accompanying a proposed restructure plan signed off by the debtor and such creditors.

The problem with the statute is that there are no provisions allowing qualified majorities to impose a plan on any recalcitrant participant in regard to secured creditors, although there are different untested theories as to how such imposition may be accomplished.

**Key procedural events**

The key procedural events, in summary, are as follows (approximate terms as they should work are in parenthesis).

**Conciliatory stage**

- filing;
- acceptance of filing (by day 10);
- appointment of a visitor (by day 21);
- judgment declaring insolvency (by day 80);
- appointment of conciliator (by day 85);
- judgment recognising creditors and establishing preferences (by day 145); and
- restructuring agreement (by day 365); if not, bankruptcy is declared (on day 365, at the latest).
Bankruptcy stage
The bankruptcy stage may begin earlier, if requested at any time by the debtor or if the conciliador determines that it will be impossible to reach agreement in respect of a restructuring agreement. Creditors may demand that the concurso begin at the bankruptcy stage, but it is extremely unlikely any such demand will actually prevail. Once the bankruptcy stage is declared, a receiver is appointed, which may be the same person who acted as conciliator (by day five of the declaration); the receiver takes over possession of the enterprise and its management (by day 20); the receiver prepares and delivers liquidation balance sheets and inventories (by day 75); the individual assets or the enterprise as a whole are slated for the sale and notices are sent out to potential bidders (by day 135); asset sales begin (general rule is to conclude liquidation by day 180); and payment to recognised creditors, subject to the preference of labour and, thereafter, secured creditors and taxing authorities, will begin as soon as practicable. In practice, the very few cases that have reached this stage, and save for only one case, have all failed to adhere to the time frames set forth by the Law, missing the mark by years.

xiv Other provisions
The 2014 amendments overhauled the whole bank resolution regime, and expunged it from the Concurso Law so that it is governed solely by the Credit Institutions Law. It also includes a chapter that refers to international cooperation in insolvency proceedings (in a similar fashion as Chapter 15 in the US but with substantial changes that make it inoperative). Finally, it also refers to conducts and liabilities that will be considered criminal in nature, and refers to specific prison terms that may be applied to administrators and directors committing criminal conduct.

t XV Duties of directors
The Concurso Law includes a regime for director liability for all business entities, which could have a significant impact on the manner in which directors behave in the imminence of insolvency and the way in which these issues are addressed by the courts.

Disinterested directors are protected from liability under ‘business judgement’ provisions, based on the presumption that directors have acted on an informed, good faith basis, on the belief that the action taken was an adequate alternative, if based upon reliance on management and the advice of the corporation’s external auditors or legal and financial advisers.

It is the view of the author that as a legal matter, directors and officers must manage an insolvent company and maximise its value for the benefit of all of its stakeholders. The focus should be maximising the value of the enterprise, rather than attempting to maximise recoveries for any particular constituency.

III AMENDMENTS AND DEVELOPMENTS TO CONCURSO MERCANTIL
The latest amendments to the Concurso Law were enacted by Congress in 2014. The principal objectives of the reform focused on the goals of a more expedient and efficient procedure, greater transparency and a reasoned intent to formally introduce DIP financing – certainly bold intentions.

The most relevant provisions introduced by Congress were:

a the judge was prohibited from extending the periods set forth in the Concurso Law;
b the consolidation of *concurso mercantil* proceedings of companies that are part of the same corporate group, the concept of which now includes companies that have the capability to make decisions with respect to another company, regardless of the actual shareholdings;

c the ability of a debtor to request the *concurso mercantil* status prior to being generally in default with respect to its payment obligations, when such situation is expected to occur inevitably within the following 90 days;

d the possibility of requesting a *concurso mercantil* directly in the stage of bankruptcy (liquidation);

e permitting common representatives to file credit recognition claims on behalf of a group of creditors and the addition of certain rules for the subscription of the debt restructuring agreement in the case of collective credits through their individualisation;

f allowing for the use of standardised forms to voluntary request or involuntary demand *concurso mercantil*;

g the prospect of filing petitions and other communications electronically;

h an emphasis on transparency;

i provisions permitting debtors to obtain DIP financing as necessary to maintain the ongoing business of the company and the essential liquidity during the *concurso*, the financing of which will be considered privileged in ranking (with a preference over all secured creditors) for purposes of the preference of the payment thereof in the event of a liquidation;

j the recognition of subordinated creditors, including inter-company creditors in accordance with certain rules, which, among others, establish that such inter-company creditors will not be allowed to vote for the approval of the debt restructuring agreement when such inter-company creditors represent 25 per cent or more of the total amount of recognised credits, unless such creditors consent to the agreement adopted by the rest of the recognised creditors of the same class; and

k the broadening of the retroactivity period applicable for the review of fraudulent conveyances with respect to transactions entered into with inter-company or related creditors.

The Concurso Law now also clarifies that the netting or realisation of assets provided as collateral of derivative contracts, repo and securities lending transactions will be allowed when such agreements provide that the ownership of such collateral has been transferred to the creditor.

With respect to the *concurso mercantil* proceeding with pre-packaged plan, the Concurso Law permits the appointment of a conciliator who is not registered with the Federal Institute of Bankruptcy Specialists or IFECOM, by the agreement of the debtor and creditors representing at least the majority of the total amount of debt. Likewise, the percentage required for filing a petition for *concurso mercantil* with a pre-pack plan was increased to provide that creditors representing at least a majority of the total amount of the abilities of the company must subscribe to the pre-pack plan.

To avoid abuses in respect of an insolvent debtor, the amendments to the Concurso Law also included a new set of provisions that refer to the potential liability of the debtor’s management and relevant employees for damages caused to the debtor company if:

a acting with a conflict of interest;

b favouring one or more shareholders and causing damages to other shareholders;
c obtaining economic benefits for themselves or for others;
d knowingly making, providing, disseminating, publishing or ordering false information;
e ordering or causing the accounting registries, related documentation or conditions in a contract to be altered, modified or destroyed;
f failing to register transactions or causing false information to be registered, or causing nonexistent transactions or expenses to be registered, or real transactions or expenses are exaggerated, or otherwise carrying out any act or transaction that is illegal or prohibited by law, causing a damage to the bankrupt debtor and obtaining an economic benefit, directly or indirectly; and

g in general carrying out any wilful or illegal act or acting with bad faith pursuant to the Concurso Law or other laws.

Although the Concurso Law adopted the business judgment rule contained in the Securities Law applicable to the members of the board of publicly traded companies and allows such directors and relevant employees to obtain insurance, guaranty or bonds to cover the amount of the indemnification for losses and damages caused, except for wilful misconduct, acts of bad faith, the Concurso Law expressly prohibits any agreement, or provisions in the by-laws with respect to any type of consideration, benefit or exemption that may limit, release, substitute or redeem the liabilities of such members of the board and relevant employees of a bankrupt debtor in the event of wilful misconduct or bad faith.

IV  SIGNIFICANT LEGAL DEVELOPMENTS

i  Practical implementation of the reform

Recent cases, including those summarised in Section I, supra, have underlined material limitations in regard to concurso proceedings.

Although the Law allows creditors and debtor companies in a pre-pack concurso to appoint a conciliator who is not a member of IFECOM, understandably IFECOM has been a zealous protector of its oversight responsibility, placing a stringent scrutiny on any such conciliator, especially with respect to formalities that seem to go well beyond the Law. There continues to be a marked emphasis on the use of cumbersome IFECOM formats and computer programs, which are not designed for large corporations, in all stages of the procedure. The procedure and requirements that have been imposed by IFECOM in regard to the recognition of creditors, places an emphasis on physical delivery of original documents that in practice has meant that the conciliator may not rely on the audited financial statements of the company but on empirical evidence of debt, which may lead to months of otherwise inexplicable delay. Other practical issues have included the attempted imposition of the criteria that in the recognition of creditors secured by guarantees structured through trusts, they should only be recognised as common creditors, based upon the notion that such creditors have the potential of detaching assets in their trust from the estate, a proposition that, in fact, may take years to separate. In addition, in regard to individual bondholder recognitions, the compulsory IFECOM formats have referred to ‘assignment of credits’ where in legal terms there were none, as the concept is the individualisation of a collective credit – the bond issue – and not an assignment.

Substantial formalities imposed on the judicial procedure have led to little transparency. The Federal Judiciary has failed to implement electronic filings of any sort, which leads to a considerable administrative burden on the courts themselves, not to mention a colossal waste
of paper and natural resources. Reviewing all the documents actually filed as a consequence is a task of gargantuan proportions, which of course affects the timing of the concurso – the ‘strict’ time periods in the Law have been extended more often than not – and moreover, create a perfect setting for many appalling delaying tactics, which do not merit a serious comment, although their existence is undeniable.

As to DIP financing, Mexican companies have not been aided by debtor-in-possession financing from Mexican banks or institutional sources, and foreign entities have failed to be persuaded to fund any such facilities until now, given continuing procedural uncertainties resulting in questions as to preference. Banking regulations governing mandatory reserves, default measurements and other relevant topics to potential DIP lending were only addressed recently to some extent. In any event, the demands by lenders once a concurso is in process for security over and above the statutory priority, have severely limited DIP financing.

As to the ranking of claims, only registered mortgages and pledges have been given statutory preference on a clearly reliable basis, given a literal reading of the Concurso Law. Creditors holding security rights under trusts or escrows have been recognised in most cases as common creditors only, although they are given the ‘privilege’ of separating assets in trust from those of the company in question, a concept that makes little sense in view of the stated objective of the Law: to keep the corporation as an ongoing concern during the workout or conciliatory stage of the concurso. Breaking up operating assets is inconsistent with this objective. My view is that such creditors should be recognised as creditors with a stated contractual privilege to specific assets or flow of funds, irrespective of any procedure of separation.

As to expenses, formal cases have brought about a debate both at IFECOM and among a number of judges, as to which concepts will actually be recognised as reimbursable expenses in a concurso proceeding. Professional fees, legal and those of financial advisers, have often been considered as substantially onerous and have thus been reduced significantly. In the extreme, the professional fees of a conciliador in a major case, were turned down by the judge as unnecessary.

Among the more alarming points of view generally shared by the litigation bar, is that, to the extent a capitalisation of debt becomes part of an exit plan, even if voted upon and approved by overwhelming majorities of every class of creditor, shareholders do in fact have a veto power over a plan if they disagree. I do not share this perspective, even though my view is by no means widely accepted, as it is contrary to the notion of absolute priority, and because the Concurso Law empowers the judge to impose the capitalisation, although most judges are and will be reluctant to do so.

As a final point, most companies (notably service providers in the energy sector) have opted to stay away from concurso and have successfully restructured substantial liabilities. The construction and homebuilder sectors have turned to concurso with varying degrees of success.

V INTERNATIONAL

The Concurso Law embraces, in form, the UNCITRAL Model Law on cross-border insolvency and international judicial cooperation. Mexican courts have sporadically recognised and given limited judicial assistance to foreign insolvency proceedings (provided that such proceedings do not contradict Mexican law or general principles of law), although there have been less than a handful of such cases. It is noted that the Concurso Law includes
substantial changes to the UNCITRAL Model Law that make the process defective as it focuses on channelling procedures through a conciliator, and thus basically imposes the need to file a *concurso* proceeding in regard to any significant assets in Mexico.

Related to this topic, it has been more frequent for Mexican companies to file for protection in the bankruptcy courts of the US (mainly in the Southern District of New York) under Chapter 15, after initiation of a *concurso* in Mexico, and certainly such courts have responded efficiently, recognising the *concurso* as the main proceeding. In the *Vitro* case, however, the US Bankruptcy Court for the Northern District of Texas ruled against the acceptance of Vitro’s formerly approved *concurso* plan as manifestly contrary to US public policy. Courts in the US have stated that this public policy exception must be narrowly construed and is limited to the most fundamental policies of the US. The US Bankruptcy Court’s decision was upheld in appeal, although, the matter was finally settled before the case could have been heard by the US Supreme Court.

**VI FUTURE DEVELOPMENTS**

*Concurso mercantil* filings have been understandably few and sporadic, although there are benefits from a tax and other perspectives, specially when there are substantial liabilities from capital market placements. Indeed, *concurso* may be the only vehicle to achieve a successful restructuring and a cramdown. It is, in any event, a complex and expensive process which requires precise financial planning.

The *Concurso* Law itself may and should be revised and there is obvious room for improvement, although amendments are not expected anytime soon. Nevertheless, the principal concern relates to the inconsistency in the application of the Law. It is expected that IFECOM will continue to update its policies, its criteria and its function as the entity providing support to the Federal Judiciary for a more efficient and transparent procedure.

The Supreme Court and the Council of the Judiciary must place a higher scrutiny on improving filing systems, addressing the many delaying tactics arising from ‘unique’ theories of human rights and due process that could well extinguish entire enterprises, and, most importantly, support the training and selection of judges that are versed on commercial and banking law, with a minimum degree of knowledge in accounting and essential finance.

One of Latin America’s leading construction and engineering concerns, the iconic Empresas ICA, has been reported to be preparing its pre-packed filing under the *Concurso* Law during the second half of the year. Billions of US dollars of liabilities are expected to be restructured under a pre-approved plan. The banking and financial community in Mexico and internationally, will be attentive to the *concurso* proceedings.

The reliability of *concurso mercantil* and ultimately, the recognition of Mexico as a jurisdiction in which the role of law is upheld, will be at stake. The financial and legal communities remain confident that transparency, adherence to time sensitive milestones and efficiency will in due course prevail, thus allowing the conservation of thousands of jobs and maintaining value for all stakeholders, which will ultimately benefit the continuing development of a vibrant Mexico.
Chapter 20

NETHERLANDS

Paul Kuipers1

I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

i Liquidity and state of the financial markets
Quantitative easing by the European Central Bank and others has resulted in high liquidity levels and low funding costs for Dutch borrowers. Dutch corporates have also had good access to financing throughout 2016 because foreign financiers and investors have been showing an increasing appetite for Dutch assets. Notably, in the real-estate market, German Pfandbrief banks are becoming lenders of choice, while in the market for leveraged financing, the prime sponsors can dictate the terms of their ‘covenant lite’ deals. Economic recovery and increased liquidity levels have, in some cases, resulted in stressed credits becoming bankable again. For corporate borrowers, 2016 was mainly a year to pursue repricings of older loans. Volumes for acquisition financing were lower, despite an upturn in the acquisitions themselves. Strategic purchasers could often fund the acquisition price out of their own funds, with a bridge facility being merely sought as a tool to present certainty of funding.

ii Impact of specific regional or global events
The political shocks of the Brexit referendum and the election of Donald Trump as US president, including the uncertainty in the lead-up to the referendum and the US elections, resulted in a reduction in M&A activity that was reflected in the financing market. However, the Brexit referendum also resulted in increased activity in the Dutch real-estate market, with a number of international investors choosing to invest in the Netherlands partially as a result of uncertainty about the prospects for UK real estate and sterling.

In consumer-facing sectors, fierce competition of low-budget competitors and online shops, and short-term liquidity problems, continues to drive changes in the retail sector.

iii Market trends in restructuring procedures and techniques employed during this period
Pre-packaged insolvencies (pre-packs) remain an area of focus in the Netherlands. In order to ensure continuity of a stressed business, a debtor, sponsor, their advisers and key creditors (notably secured lenders and key suppliers) prepare a deal, following which the court appoints a liquidator to assess the proposed restructuring as a transaction that might be implemented on the first day of an actual bankruptcy. While the Dutch legislator continues to work on a broader statutory platform for pre-packs (see Section VI.ii, infra), employee rights have taken centre stage with arguments having been raised that a pre-pack constitutes a transfer

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of undertaking that is not exempt from protections of the workforce (known as TUPE rules, under which employees effectively transfer to the transferee business). Following the recent judgment of the European Court of Justice (ECJ) concerning the Estro pre-pack (see Section VI.ii, infra), pre-packs can no longer be used as a tool to make part of the workforce redundant, at least not without making severance payments. It has now also been clarified that, if a company that is trying to restructure via insolvency has a works council, that works council, in principle, has advisory rights in respect of the restructuring.

Finally, 2015 saw a number of big insolvencies in the retail sector that resulted in the courts giving important practical guidance in the course of 2016 regarding the position of suppliers that retained their title and creditors having security over stock. During a (retail) insolvency, there is the option to ask for a stay of enforcement for a period of up to four months. During that period, the retail operation can be kept a going concern, even where that includes selling stock supplied under retention of title or pledged in favour of secured creditors. The insolvency administrator will subsequently need to account to the supplier or secured creditor for the value of the assets so sold. That turnover will, however, not necessarily be at retail prices and attention will be paid to the costs of the estate in selling for the benefit of others and what would otherwise have been recoverable in a more classic enforcement sale.

In retail insolvencies, one enforcement method that is regularly used includes a liquidation sale conducted by the liquidator under a mandate granted by the secured creditor. Any cash and electronic payments made by customers in respect of encumbered property are deemed to constitute enforcement proceeds available for distribution to the secured creditor.

iv Number of formal procedures entered into or exited during 2016

According to details made available by the Central Bureau of Statistics of the Netherlands (CBS), the total number of corporate bankruptcy proceedings commenced in 2016 amounts to 4,396 new cases (excluding sole proprietors and traders). This represents a decrease of almost 17 per cent compared with the number of new filings in 2015, and is the lowest number since 2009. The decrease in the number of new bankruptcy cases is linked to the recovery of the Dutch economy in 2016.

Similar to 2015, most new bankruptcies have been recorded in the wholesale and retail sector. A total number of 449 new cases were opened in the wholesale sector and 425 new cases in the retail sector. A significant number of bankruptcy proceedings were entered into in the financial services sector (758 new cases). The sharpest drop in new bankruptcy cases concerned the construction industry (a reduction of 33 per cent in new cases).

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Available insolvency and restructuring procedures

The Bankruptcy Code provides for three main proceedings: bankruptcy, suspension of payments and debt adjustment for natural persons.

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Bankruptcy proceedings have been primarily designed as liquidation proceedings, but in practice, can function as a restructuring tool (e.g., through a composition scheme or by means of a going-concern sale of the debtor’s viable business parts). The primary objective of suspension of payments proceedings is the reorganisation and continuation of the debtor’s business, but the limited scope of the proceedings (confined to unsecured, non-preferential, insolvency claims) and continued application of transfer of undertaking protection rules render it ineffective for many restructurings. The main purpose of debt adjustment for natural persons is to provide heavily indebted natural persons with a fresh start. Considering the focus of this chapter on large corporate debtors, debt adjustment for natural persons will not be further dealt with.

Special emergency proceedings for financial undertakings have been enacted in the Financial Supervision Act. Such proceedings contain elements of both liquidation and restructuring proceedings. Furthermore, the Bank Recovery and Resolution Directive (the BRRD) and the Single Resolution Mechanism Regulation (the SRM Regulation) provide for a European approach towards the recovery and resolution of banks and large investment firms (and certain affiliated entities) in distress. To facilitate a timely intervention in respect of such institutions, national legislation implementing the BRRD and the SRM Regulation grants certain intervention powers to competent resolution authorities. Beyond the scope of the BRRD and the SRM Regulation, the Dutch Central Bank has powers to procure that a bank in serious financial problems is transferred, in whole or in part, to a third party. Furthermore, the Dutch Minister of Finance holds powers to intervene in the affairs of banks, investment firms and (managers and custodians of) investment institutions (all as defined in the Financial Supervision Act), including the power to expropriate their shares or capital instruments and some or all of their assets (e.g., as applied to the nationalisation of SNS REAAL NV and SNS Bank NV in February 2013), where this is necessary to safeguard the stability of the Dutch financial system.

Restructurings often occur beyond the setting of formal insolvency proceedings (e.g., through security enforcement, new or amended financing arrangements, contractual composition schemes or foreign restructuring routes). The main disadvantages of such informal restructurings often include the lack of a stay on individual recourse rights of creditors and the absence of a cramdown mechanism in relation to dissenting and non-participating creditors, beyond those mechanisms agreed between creditors. Changes to the statutory framework are pending to enhance attempts to restructure financially distressed companies outside formal insolvency proceedings (see further in Section VI, supra).

3 Article 232 of the Bankruptcy Code, Article 7:663 and Article 7:666 of the Civil Code.
4 See Part 3.5.5 of the Financial Supervision Act.
ii The taking and enforcement of security

Loans granted to a corporate debtor can be secured over the company's assets. Creation requirements of security rights are governed by general rules of property law and depend on the relevant type of collateral. All-embracing security can be obtained by a combination of pledges and mortgages over assets comprising the debtor's business.

An important effect of the commencement of bankruptcy proceedings is the divestment of the debtor (i.e., the debtor loses the power to dispose of and administer the assets included in the insolvent estate). Pledges granted in advance over future property can no longer crystallise after the debtor's divestment. During the course of bankruptcy proceedings, the liquidator is exclusively entitled to dispose of and administer the insolvent estate.

The secured creditor in Dutch insolvency proceedings can enforce its rights as if the proceedings had not been opened. Enforcement of security can only be temporarily stayed by the order of a moratorium at the time of the bankruptcy adjudication or subsequently by the supervisory judge. Such a moratorium can last for a maximum period of four months (including extensions). The liquidator has powers to expedite enforcement of security by demanding that the secured creditor realise the collateral within a reasonable period of time. Failure to enforce within that time period will result in a loss of enforcement rights and an obligation to share in the general realisation costs of the proceedings. A final limitation on the position of the secured creditor is that it cannot enforce its security in respect of all claims that might arise after the opening of insolvency proceedings.

In practice, the secured creditor and the liquidator often agree on the realisation of the secured asset by the latter against the deduction of a nominal fee from the realisation proceeds.

iii Duties of directors of companies in financial difficulties

No statutory obligation exists for directors of a financially distressed company to file for insolvency proceedings. Nevertheless, governance of the company may be placed under increased scrutiny by third parties and continued trading may give rise to director's liability.

In essence, directors would face liability if their behaviour was negligent towards a third party and constituted serious personal wrongdoing. A prominent ground for personal liability is when directors allowed the debtor to carry out a transaction with a third party while they knew (or should have known) that the debtor would be unable to meet its obligations under that transaction and that the deprived counterparty would not have sufficient recourse.

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7 Article 23 of the Bankruptcy Code.
8 Mortgages cannot be granted in advance over future immoveable assets, registered ships and registered aircraft. See Article 3:97 (1) and 3:98 of the Civil Code.
9 Article 23 and 35 (2) of the Bankruptcy Code.
10 Article 68 (1) of the Bankruptcy Code.
11 Article 57 (1) of the Bankruptcy Code.
12 Article 63a of the Bankruptcy Code.
13 Article 58 (1) of the Bankruptcy Code.
14 Article 58 (1) and Article 182 of the Bankruptcy Code.
15 It follows from Article 132 (2) of the Bankruptcy Code and Article 483e of the Civil Procedure Code that security can only be enforced during insolvency proceedings for (i) pre-commencement secured claims; and (ii) post-commencement secured claims which originate from a pre-commencement legal relationship. Cf. also Supreme Court 16 October 2015, JOR 2016/20 (DLL/Van Logtestijn).
16 Article 6:162 of the Civil Code.
for its damages. Director’s liability can also result from actions that resulted in default and non-recoverability of damages, as well as selective payments (e.g., non-payment to a particular creditor based solely on unwillingness of the director to allow such payment to be made).

Each director can also be held personally liable for the entire deficit of the bankrupt estate if their improper management caused the bankruptcy. By statute, improper management is established if books and records of the bankrupt company have not been properly maintained or if directors failed to meet obligations regarding the company's annual accounts. Subject to proof to the contrary, that improper management is also assumed to have caused the bankruptcy.

Directors can also be held liable by the company for improper performance of management tasks allocated to them by law or the articles of association. Examples of circumstances in which directors can be held liable include violation of the law or articles of association, procuring reckless and irresponsible financial behaviour of the company and utilising assets of the company for personal benefit.

iv  Clawback actions

During bankruptcy proceedings, a liquidator may invoke the actio Pauliana in order to invalidate antecedent transactions that are detrimental to the insolvent estate. Clawback generally prerequires prejudice, which will materialise in the event creditors receive a lower distribution on their claims as a result of a transaction.

Prejudice would typically be the result of a reduction in the total value of the debtor’s estate as a result of a transaction (transactions at undervalue) or as a result of a disturbance of the statutory waterfall of priorities when a company is already insolvent (preferences). The liquidator should look at the entire transaction (including beneficial aspects of the transaction) and, therefore, has no right to cherry-pick by only looking at one particular

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17 Supreme Court 6 October 1989, NJ 1990, 286 (Beklamel).
19 For example, Supreme Court 26 March 2010, JOR 2010/127; NJ 2010, 189 (Zandvliet/ING).
20 Article 2:138 (1) and Article 2:248 (1) of the Civil Code. Such improper management must have occurred within three years of the commencement of the bankruptcy proceedings. See Article 2:138 (6) and Article 2:248 (6) of the Bankruptcy Code. The scope of the provision is extended to shadow directors pursuant to Article 2:138 (7) and Article 2:248 (7) of the Civil Code. A new Bill on management and supervision of legal entities seeks to apply similar rules regarding all corporate entities by implementing Article 2:9c in the Civil Code.
21 Article 2:10 of the Civil Code.
22 Article 2:9 (1) of the Civil Code and the proposed new Article 2:9b of the Civil Code.
23 Other circumstances that may be relevant include the nature of the company's activities and corresponding risks, the allocation of tasks within the board of directors, possible guidelines applicable to management, the information available to directors at the time of scrutinised actions and decisions, and the knowledge and prudence which may generally be expected of a director which is sufficiently prepared and performs his task in a diligent manner. See Supreme Court 10 January 1997, JOR 1997/29; NJ 1997, 360 (Staleman/Van de Ven).
provision of a document as a clause that has a negative impact on the recourse position of the joint creditors. If the disputed act was part of a set of transactions, the positive or negative effects of the combined set should be regarded as well.24

Where prejudice has been established, the right to challenge the prejudicial action depends on further circumstances. The avoidance of an act entered into without a preexisting obligation to perform the relevant act requires that the debtor (and in the case of a transaction against consideration, also the counterparty) knew or should reasonably have known that such prejudice would materialise.25

Knowledge of a mere chance that prejudice may occur is insufficient to invoke the actio Pauliana. Knowledge must relate to a reasonable degree of likeliness that insolvency proceedings will be opened and that the insolvent estate contains a deficit.26 In certain cases, the onus of proof regarding knowledge of prejudice is reversed by law (e.g., in the event of certain transactions executed between related parties within a period of one year prior to the bankruptcy date).27

A compulsory or involuntary legal act, on the other hand, can only be avoided either in the event that the transaction occurred at a time on which the counterparty knew or ought to have known that a petition was submitted for the commencement of insolvency proceedings against the debtor,28 or in the event of a concerted action by the debtor and the creditor aimed at facilitating preferential treatment of the latter (collusion).29

Finally, it should be noted that set-off effected in the period immediately prior to the commencement of insolvency proceedings could be clawed back if the creditor effecting the set-off acted in bad faith when acquiring its claim or debt on which it relied when setting off.30 Bad faith is, notably, given when the creditor knew or should have known that the insolvency could reasonably be expected.31

### III RECENT LEGAL DEVELOPMENTS

#### i Conditional ownership as eligible collateral

As described above, an important effect of the commencement of insolvency proceedings concerns the divestment of the debtor (see Section II.ii, supra). Any property acquired by the debtor after the commencement of the proceedings (including future property that has been pledged or transferred in advance to a third party) belongs unencumbered to the insolvent estate.

In an important Supreme Court case, it has been held that assets supplied under a retention of title arrangement constitute immediate (albeit conditional) ownership rights in

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25 Article 42 of the Bankruptcy Code.
27 Article 43 of the Bankruptcy Code.
28 Knowledge of the mere likelihood that insolvency proceedings may be opened is insufficient to meet this requirement. See Supreme Court 16 June 2000, NJ 2000, 578 (Van Dooren qq/ABN AMRO Bank I).
29 Supreme Court 24 March 1995, NJ 1995, 628 (Gispen qq/IFN) and Supreme Court 20 November 1998, JOR 1999/19; NJ 1999, 611 (Verkerk/Tietheoff qq).
30 Article 54 (1) of the Bankruptcy Code.
31 Supreme Court 7 October 1988, NJ 1989, 449 (AMRO/THB).
favour of both the supplier and the buyer: an ownership right under a condition subsequent of payment of the purchase price of the former and ownership under a condition precedent of payment of the purchase price of the latter. Both conditional ownership rights can be immediately transferred or encumbered for the benefit of a third party. For example, in the event that a buyer grants a pledge over its conditional ownership of supplied property under a retention of title arrangement, the pledgee acquires an immediate right of pledge on such conditional ownership rights. This right remains unaffected in the event that insolvency proceedings are opened against the supplier. Moreover, the payment of the purchase price during such insolvency proceedings converts the proprietary entitlement of the buyer of the pledged asset into an unconditional ownership right.32

ii Illegitimate frustration of right of pledge by liquidator
In the event that a liquidator illegitimately collects a pledged claim,33 the claim – and correspondingly the right of pledge – ceases to exist. The (former) pledgee can claim the remittance of the collected amount as a claim against the estate and invoke priority similar to that which was awarded to its frustrated right of pledge. However, in case the insolvent estate comprises insufficient funds to discharge all claims against the estate in full, the salary of the liquidator is awarded senior ranking over the claim of the (former) pledgee. This rule follows from recent (controversial) case law of the Supreme Court.34 The frustration of the right of pledge may trigger the personal liability of the liquidator against the (former) pledgee.35

iii Ranking of secured post-commencement claims with regard to unsecured (preferential) insolvency claims
It has been established in case law that a secured creditor is entitled to enforce security for post-commencement secured liabilities, provided that such liabilities originate out of a legal relationship already existing at the time at which the bankruptcy proceedings have been opened.36 This rule also applies to post-commencement claims, which are awarded the status of claims against the estate pursuant to an express statutory provision. Claims against the estate (including those secured by a pre-commencement right of pledge) must be discharged in full before a distribution can be made to the holder of any unsecured insolvency claim (including preferential insolvency claims).37

32 Cf. Supreme Court 3 June 2016, JOR 2016/287 (Rabobank/Reuser).
33 For example, the liquidator is not entitled to actively pursue the collection of pledged claims during a reasonable time period (generally two weeks). This rule is endorsed in Supreme Court 22 June 2006, NJ 2007, 520 (ING/Verdonk qq) and enables the pledgee to notify account debtors of the pledged claim. Upon such notification, the pledgee is exclusively entitled to collect the claim pursuant to Article 3:246 (1) of the Civil Code and Article 57 (1) of the Bankruptcy Code.
34 Supreme Court 30 October 2009, JOR 2009/341 (Hamm qq/ABN AMRO) and Supreme Court 5 February 2016, JOR 2016/83 (Rabobank/Verdonk qq).
35 Cf. e.g., Supreme Court 19 April 1996, NJ 1996, 727 (Maclou) and Supreme Court 16 December 2011, NJ 2012, 515 (Prakke/Gips).
36 See Supreme Court 16 October 2015, JOR 2016/20 (DLL/Van Logtestijn). This view is based on Article 132 (2) of the Bankruptcy Code and Article 483e of the Civil Procedure Code.
37 Cf. 15 April 2016, JOR 2016/215 (Van der Maas qq/Heineken).
iv Status of post-commencement interest claims

In a landmark Supreme Court decision it was held that (in principle) post-commencement claims which originate from a pre-commencement legal relationship are admissible in the proceedings as insolvency claims. An exception to this rule is provided for by law which renders (unsecured) post-commencement interest claims inadmissible in the proceedings. A recent case confirms that the duration of the insolvency proceedings should be ignored concerning the timing of a possible future prescription of such interest claims.

v Opening of debtor’s books and records

During insolvency proceedings, creditors can request the opening of the debtor’s books and records if they have a direct and sufficiently significant interest. In this respect it must be demonstrated by the relevant creditor that information is needed to determine its relationship with the debtor (e.g., regarding the amount, nature or substance of its claim). No such opening of the books and records can be demanded to examine possibilities to initiate legal action against third parties (e.g., (former) directors of an insolvent debtor company). Access to the debtor’s books and records should be distinguished from the opening of the books and records of the liquidator concerning the administration of the insolvent estate (as addressed in earlier case law).

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

As a summary, below is a selection of key insolvencies and restructurings carried out in 2016, sorted by procedure used:

- **Liquidation in bankruptcy:**
  - Vroom & Dreesmann (V&D), retail;

- **(Partial) going-concern sale in bankruptcy:**
  - Macintosh, retail (including its Scapino, Dolcis and Manfield brands);
  - McGregor, retail;
  - MS Mode, retail;
  - Unlimited Sports Group, retail;

- **Share deal:**
  - Propertize B.V., a nationalised Dutch bad bank sold to NPL investors; and

- **Scheme of arrangement:**
  - Metinvest B.V., a Dutch finance vehicle in an Ukrainian based iron ore and steel conglomerate.
  - Indah Kiat International Finance Company B.V., a Dutch finance vehicle related to the APP Group, which is primarily engaged in manufacturing paper pulp.

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38 Supreme Court 19 March 2013, JOR 2013/224 (Koot/Tideman).
39 Article 128 of the Bankruptcy Code.
40 Supreme Court 24 June 2016, JOR 2016/290 (BSM/Van Galen qq).
41 Article 3:15j (d) of the Civil Code.
42 Supreme Court 8 April 2016, JOR 2016/180 (Schmitz qq/Aerts Europa).
V INTERNATIONAL

i General cross-border insolvency framework

The general legal framework pertaining to cross-border insolvency proceedings is primarily of European origin. Dutch courts recognise foreign insolvency proceedings that fall within the ambit of the Recast European Insolvency Regulation (Recast EIR)\(^{44}\) and the Winding-Up Directives concerning credit institutions and insurance undertakings.\(^{45}\) To date, the Netherlands has not adopted the UNCITRAL Model Law on Cross-Border Insolvency.

In the absence of binding international rules on recognition of foreign insolvency proceedings, other than the said EU law instruments, the fallback position under Dutch law is based on case law only. Under that case law, foreign proceedings outside of the scope of EU law instruments are merely granted territorial effect in the following ways:

\(a\) Assets of a debtor that are situated in the Netherlands are excluded from the scope of a general attachment and a general stay under the lex concursus.

\(b\) Any legal effects of the commencement of insolvency proceedings applicable under the lex concursus cannot be invoked in the Netherlands to the extent that this would prevent the debtor’s creditors from taking recourse against assets situated in the Netherlands during or upon the conclusion of the proceedings.

\(c\) The application of the territoriality principle does not prevent any other legal effects from being invoked in the Netherlands. For example, a liquidator is entitled to administer and dispose of the debtor’s assets situated in the Netherlands, provided that such rights are conferred to him under the lex concursus and any attachments levied by an execution creditor prior to such acts by the liquidator are respected.\(^{46}\)

ii Recognition of UK schemes of arrangement

Dutch companies have increasingly been using English law-governed schemes of arrangement as a means of implementing debt restructurings. The first case involving a Dutch company in which recognition issues have been considered is \(\text{Re NEF Telecom Company BV}\).\(^{47}\) Another example entails the scheme offered by Magyar Telecom, which was a Dutch borrower.\(^{48}\) More recent examples are mentioned in Section IV,(d), supra.


\(^{46}\) See Supreme Court 2 June 1967, NJ 1968, 16 (Hiret/Chiotakis); Supreme Court 31 May 1996, JOR 1996/75; NJ 1998, 108 (Coppooole/De Vleesmeesters); Supreme Court 24 October 1997, JOR 1997/7146; NJ 1999, 316 (Gustafson qq/Mod); Supreme Court 19 December 2008, JOR 2009/94; NJ 2009, 456 (Yukos I) and Supreme Court 13 September 2013, JOR 2014/50; NJ 2012, 424 (Yukos IV).

\(^{47}\) [2012] EWHC 2944 (Comm); recognition issues do not appear to have been raised in a prior case of a Dutch company proposing a scheme, \(\text{Re DAP Holding NV}\) [2005] EWHC 2092 (Ch).

\(^{48}\) \(\text{Re Magyar Telecom}\) [2013] 3800 (Ch).
The prevailing view in legal literature and practice is that Dutch courts will probably recognise an English court order. There is guidance that a scheme of arrangement is within the scope of the Brussels Ibis Regulation,\(^49\) so that the Dutch court is generally not entitled to dispute the English court’s jurisdiction and could refuse recognition of the scheme.

Should schemes of arrangement be outside the scope of the Brussels Ibis Regulation, then alternative grounds for recognition have been identified, including:

\[a\] the Rome I Regulation;\(^50\)

\[b\] the Convention providing for the Reciprocal Recognition and Enforcement of Judgments in Civil Matters (concluded on a bilateral basis between the Netherlands and the United Kingdom on 17 November 1967); and

\[c\] general Dutch private international law.

**VI FUTURE DEVELOPMENTS**

**i Proposal for EU Insolvency Directive**

On Tuesday, the European Commission issued a proposal for a Directive on ‘preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures’ (the Directive). If implemented, it would significantly close the gap between Member States’ existing restructuring and insolvency frameworks, placing a greater emphasis on corporate rescue and significantly reducing the ability of shareholders and ‘out of the money’ creditors to block a viable restructuring proposal.

The Directive does not attempt to harmonise core aspects of formal insolvency procedures such as the conditions for opening insolvency proceedings, definitions of insolvency or the ranking of claims. This is unsurprising, as deciding, for example, which creditor claims should be prioritised depends on balancing a range of cultural, economic, social and political considerations, with the final balance struck varying considerably between jurisdictions. Instead, the Directive focuses, as far as corporate debtors are concerned, on ensuring that a statutory framework is put in place in each Member State that maximises the chances of a company with a viable business being able to restructure its debts before it is forced into liquidation. The five main elements of the European proposals, which would not be available to credit institutions or insurance undertakings, relate to: (1) the framework for a restructuring plan; (2) the cramdown of ‘out of the money’ creditors; (3) limitation of shareholder leverage; (4) the availability of a preventative restructuring procedure; and (5) the protection for new financing, interim financing and other restructuring-related transactions.

**ii Future reform of Dutch law**

It is currently clear that no full revision of the statutory regime will occur in the foreseeable future. Various proposals are currently pending or being prepared to improve specific parts of the current regime. Main themes of reform include:


combating insolvency fraud through the introduction of director disqualification rules, revision of criminal law aspects of insolvency proceedings and other powers;
b the promotion of corporate rescue through the Business Continuity Acts described below; and
c the modernisation of insolvency proceedings by enhancing electronic communication modes, abolishing physical claims admission meetings, adding flexibility in the composition of the creditors’ committee and other tools.

Specific attention should be drawn to the proposed Business Continuity Acts, which are expected to be enacted in three tranches, numbered I to III. These Acts purport to promote the rescue of financially distressed companies at an early stage.

A proposed amendment of the current regime under the Business Continuity Act I includes the debtor’s right to request a court appointment of a silent administrator prior to the commencement of formal insolvency proceedings. The silent administrator will, in principle, be appointed as liquidator in subsequent formal insolvency proceedings. The silent administrator can declare:
a that it can be reasonably expected that certain pre-commencement transactions to be conducted in the ordinary course of business or to discharge outstanding liabilities will not be avoided by the liquidator pursuant to the Dutch clawback rules in subsequent insolvency proceedings;
b the circumstances under which it can be reasonably expected that the liquidator will sell goods after the commencement of bankruptcy proceedings; and
c the preparations that can be made in order to accelerate the administration of possible bankruptcy proceedings.

The future of the Business Continuity Act I is somewhat uncertain in the wake of the recent ECJ judgment concerning the Estro pre-pack. In essence, the ECJ ruled that TUPE rules (see above Section I.iii, infra) apply to pre-packaged going concern sales implemented upon (or soon after) the commencement of bankruptcy proceedings. Although bankruptcy proceedings are designed by the legislator as winding-up proceedings and generally benefit from a statutory liquidation carve out from the TUPE rules, a pre-pack aimed at ensuring the continuation of the debtor’s business cannot be considered to be a liquidation for the purposes of such carve out (regardless of whether the pre-pack is technically implemented during bankruptcy proceedings). Employment contracts and accrued liabilities will thus automatically transfer to the transferee of the debtor’s business. Where many of the companies that used Dutch pre-packs had done so as a tool to reduce (the costs associated with) their workforce, without having to make severance payments, this incentive for a pre-pack has now been effectively blocked by the ECJ. A pre-pack could still be useful to, for example, restructure other liabilities of a financially distressed debtor or to procure a going concern sale of viable parts of the debtor’s business, but the ECJ ruling may cause the tool to be reconsidered in its entirety.

The Business Continuity Act II purports to introduce a statutory regime governing composition plans outside formal insolvency proceedings. The proposed regime provides for cramdown in relation to creditors and shareholders dissenting to a debt restructuring supported by a majority of creditors and shareholders in the relevant class of creditors. A composition plan can be offered to individual classes.
Among the measures currently contemplated for the Business Continuity Act III is the introduction of a prohibition on *ipso facto* clauses in contracts that provide for the supply of essential goods and services.

Other measures currently considered to enhance the speed and efficiency and to reduce the costs of insolvency proceedings include:

- *a* enhanced possibilities to use digital and electronic communication means (e.g., to conduct creditor meetings and to circulate information);
- *b* measures to accelerate the proceedings (e.g., introduction of a bar date for the admission of claims);
- *c* tailored solutions for complex proceedings (e.g., the proactive admission of claims in case of insolvency proceedings opened against an issuer of complex financial products traded on the international capital markets); and
- *d* enhanced insolvency expertise of the legislator and judiciary (e.g., by the appointment of an Insolvency Council as a new advisory body).
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

The Norwegian economy has experienced severe challenges over the last couple of years, owing to the drastic drop in and continuously low oil prices from late 2014. Before November 2014, a barrel of crude oil cost more than US$100. As of mid-June 2017, a barrel costs approximately US$45, which is more than the low point in 2015 of approximately US$30, however, still considered to be challengingly low for oil industry companies. A number of large Norwegian businesses within the oil and oil services industries have carried out downsizing and cost-reduction measures over the past few years, and several companies, especially within these sectors, have carried out restructuring processes or gone bankrupt. Further, the Norwegian currency has been weaker over the last few years than prior to the drop in oil prices, and especially against the US dollar, the euro and the British pound.

According to the Financial Supervisory Authority of Norway (FSA), Norwegian banks have a high profitability, and much higher than the average for European banks. However, Norwegian banks’ profit decreased somewhat in 2016 due to a higher loss on offshore industry loans, and the larger banks suffered the most. A significant amount of the banks’ offshore customers has or will carry out restructurings.3

The key policy rate has not been changed since December 2015, and remains historically low at 0.5 per cent as of June 2017. Norges Bank indicates that the key policy rate will remain low until 2019, from when it will gradually increase.4

The perceived market trend related to distressed companies is that banks and other lenders are more willing than only a few years ago to negotiate solutions in cases of breached economic covenants or payment default by providing waivers, extensions of payment, etc. These measures seem to have reduced the need for statutory restructuring and insolvency proceedings; however it appears that the number of out-of-court restructuring proceedings is rising as more and more companies, especially in the oil and oil service industries, are facing payment problems due to the continuously low oil prices.

The total number of winding-up proceedings and forced liquidations in Norway in 2016 was 5,865, which was approximately the same as in 2015. As per 19 June, the total number for 2017 is 3,024, which is an increase of approximately 7.3 per cent compared to

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the same period in 2016. Although the total number of bankruptcies is high, most of these cases still concern smaller companies and private persons, as has been the case for several years.

There are no new trends when it comes to restructuring methods under Norwegian law, and the majority of restructurings are still handled outside of the courts. Several Norwegian companies have initiated such out-of-court restructurings over the past few years, and many of these are still trying to see through a plan. See, however, Section VI, infra, regarding a current review of the judicial restructuring scheme in Norway.

Only very few judicial restructuring proceedings are opened each year. In 2016, eight judicial debt negotiation proceedings were opened in Norway; all of which have ended in winding-up proceedings. Thus, none were successful. So far in 2017, two judicial debt negotiation proceedings have been opened, of which one has already ended in winding-up proceedings. The other is ongoing as of the end of June 2016.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

There are two main categories of statutory bankruptcy proceedings in Norway: winding-up proceedings and judicial debt negotiation proceedings. Judicial debt negotiation proceedings can be either voluntary or compulsory, each regulated by slightly different legislation. Both winding-up proceedings and judicial debt negotiation proceedings are regulated by the Bankruptcy Act of 8 June 1984 No. 58.7

A company must be illiquid to file for judicial debt negotiation proceedings (i.e., in a position where it cannot meet its financial obligations as they fall due). It is not, however, a requirement that the company is insolvent (i.e., both illiquid and with negative net assets). Thus, judicial debt negotiation proceedings may be opened even though the debtor has positive net assets. Insolvency is, however, an absolute requirement to open winding-up proceedings.

Only the debtor may deliver a petition for judicial debt negotiation proceedings, while a petition for winding-up proceedings may be filed either by the debtor or by a creditor with an unsecured (or only partly secured) claim against the debtor.

After judicial debt negotiation proceedings have been opened, the debtor shall suggest a reorganisation plan to the creditors. Such a reorganisation plan may consist of various elements. In voluntary judicial debt negotiation proceedings, the suggested plan must be accepted by all creditors. In compulsory judicial debt negotiation proceedings, however, the minority voters are crammed down by the majority voters. The plan must provide a minimum dividend payment of 25 per cent to all unsecured creditors with claims not ranking in priority, and the reorganisation plan requires a majority both in number of creditors and of the total amount of all claims filed in order to be binding on all creditors (‘double majority’).

5 All numbers are from the Register of Bankruptcies.

6 As per 19 June 2017.

7 Other judicial insolvency proceedings include public administration for banks regulated by the Act on guarantee schemes for banks and public administration, etc., of financial institutions of 6 December 1996, and forced liquidation or dissolution proceedings regulated by the Limited Liability Companies Act of 1997 Sections 16-15 through 16–18.
The voting requirements for reaching a double majority in a compulsory composition are (the numbers referring to creditors and claims that are granted voting rights):

a) if the dividend payment is at least 50 per cent, the plan must be accepted by at least three-fifths of the creditors holding at least three-fifths of the total debt; or

b) if the dividend payment is less than 50 per cent (but not below 25 per cent), the plan must be accepted by at least three-quarters of the creditors holding at least three-quarters of the total debt.

Claims ranking in priority shall be paid in full, and will therefore not entitle the respective priority creditors a right to vote. Nor will secured claims give grounds for voting rights, as far as they would have received payment if the secured assets were to be sold. Finally, closely related parties to the debtor do not have the right to vote.

If the legal requirements for completing a successful composition with the creditors are not met, the judicial debt negotiation proceedings will come to an end, and winding-up proceedings will be opened by the court. Thus, there is ‘no return’ from a judicial debt negotiation proceeding: either the company succeeds or it is liquidated.

i) Taking and enforcement of security

When winding-up proceedings are opened in Norway, a bankruptcy estate is established as a separate legal entity from the debtor. Subject to the Satisfaction of Claims Act of 8 June 1984 No. 59, the bankruptcy estate has automatic seizure of all the debtor’s assets, with only few exceptions. This means that the estate can sell, use or dispose of in any other way all the debtor’s assets, claims and rights, with certain limitations. All profits from the realisation of assets and collection of claims belong to the estate, which in turn make dividend payments to the creditors based on, inter alia, the claims’ security and priority.

The common situation in Norway is that the creditors – usually the debtor’s bank – have established securities in most of the debtor’s assets, including inventory and stock, machinery and plant and trade receivables, as well as registered motor vehicles, real property, ships, etc. If the security right is validly established with legal protection, such securities will prevail over the bankruptcy estate’s seizure, in the sense that those assets might not be of any real value to the bankruptcy estate since any sales profit shall ultimately be paid to the security holder. The rules on validity, legal protection and a number of other issues related to security interests may be found in the Mortgage Act of 8 February 1980 No. 2, with a few lex specialis rules in other acts, such as the Financial Collateral Act of 26 March 2004 (see below). Most assets that may be posed as security are registered in national registers, in which case the security interest (lien, pledge, etc.) normally has to be registered in the relevant register to obtain legal protection. The registration costs are low, and the process of registering the security interest usually takes from a few days to one or two weeks.

Prior to the filing of a petition for any bankruptcy proceeding, a creditor with an unsettled and due claim against the debtor may seek to establish an execution lien in nearly any asset belonging to the debtor. However, if a petition for winding-up proceedings or judicial debt negotiation proceedings is filed less than three months after the execution lien was established, the execution lien will have no legal effect towards the bankruptcy estate.

Once the execution lien is established, the creditor may initiate a forced sale of the encumbered asset, subject to the mandatory rules of the Enforcement Act of 26 June 1992 No.
The opening of a bankruptcy proceeding will, however, impose an automatic stay on enforcement proceedings against the debtor, including a creditor’s attempt to establish an execution lien in any of the debtor’s assets. The stay lasts for six months.

After a petition for judicial debt negotiation proceedings has been filed, there is a three-month automatic stay of any petitions for winding-up proceedings based on debt incurred prior to the opening of the judicial debt negotiation proceedings. The stay may be prolonged at the discretion of the court upon a motion from the debtor. If compulsory judicial debt negotiation proceedings are opened, the automatic stay lasts throughout the proceedings.

The stay is not effective against a petition for winding-up proceedings filed by at least three creditors with voting rights whose claims in sum represent at least two-fifths of all claims entitled to dividend payment.

If voluntary or compulsory judicial debt negotiation proceedings are opened, the business of the illiquid company will continue more or less as usual, while the court-appointed administrator and creditors’ committee cooperate with the board of directors and management of the debtor to restructure the company and work out a reorganisation or composition plan, or both, to propose to the creditors. Any due debt established prior to the opening of the proceedings will be ‘frozen’, while the debtor must continue to pay running costs as well as instalments of secured debt, lease agreements, etc., for the time period after proceedings are opened. The creditors’ committee shall supervise the company and suggest a plan to uphold the security holders’ interests during the proceedings.

If winding-up proceedings are opened, it is common in Norway that the secured assets are realised by the estate in cooperation with the security holder (usually a bank or other financial institution). The security holder pays any and all costs related to such work, since it is the security holder who has the economic interest in the realisation of secured assets.

The Financial Collateral Act of 26 March 2004 (implementing the EU Financial Collateral Directive 2002/47/EU) regulates financial collateral arrangements that secure obligations a corporate body has towards a financial institution. Subject to the rules of this statute, the parties may agree in writing to deviate from the otherwise mandatory rules of the Enforcement Act with regard to how and when a security interest in financial collateral may be enforced. Further, the statute provides exemptions from the main rules on set-off of security interests, allowing financial institutions to net outstanding amounts or apply netting in certain situations where set-off would otherwise be prohibited. Finally, if one were to adapt a strict interpretation of the provision on the six-month automatic stay period in the Bankruptcy Act, cf. above, the automatic stay will not be effective for financial collateral governed by the Financial Collateral Act.

ii Duties of directors of companies in financial difficulties

Provisions in the Limited Liability Companies Act of 13 June 1997 regulate the duties of directors of limited liability companies, as well as detailing in which situations such directors may be held liable for damages or criminally liable. Corresponding provisions for other common company structures can be found in the Partnerships Act of 27 June 1986 and the Public Limited Liability Companies Act of 13 June 1997, but the rules on liability for members of the board of directors and for the general manager of businesses have mainly evolved through case law over the past few decades.
Directors of companies in financial difficulty must ensure that all of the company's creditors are treated equally and fairly, and that the company does not incur any debt that it cannot pay unless the respective creditor is familiar with, or informed of, the company's financial situation and the risk involved upon providing credit.

Furthermore, the directors must act promptly if the company's equity is considered insufficient compared with the size and risk of the business operations, or if the company's equity is less than half of the share capital. Such actions include measures to improve the company's financial situation, convene a shareholders' meeting to provide information on the situation, and ultimately to file for bankruptcy proceedings, if it is unlikely that the financial difficulties can be resolved in the immediate future.

After judicial debt negotiation proceedings are opened, the directors maintain the same roles and duties as before such proceedings were opened, but they must act in compliance with the administrator's and creditors' committee's decisions and the legal framework regulating the proceedings.

When winding-up proceedings are opened, the directors maintain their positions, but have no authority over the company or its assets and rights. They no longer have any managerial duties, but must assist the administrator of the bankruptcy estate in obtaining information and documentation.

### iii Clawback actions

Transactions made by the debtor prior to the opening of either winding-up proceedings or compulsory judicial debt negotiation proceedings may in certain circumstances be subject to clawback. The main objective of the clawback rules is to treat creditors equally, meaning that one or more creditors shall not benefit at the expense of other creditors. The rules on clawback do not apply to voluntary debt negotiation proceedings.

Transactions carried out within three months prior to the day when the court received the petition for bankruptcy proceedings may be subject to clawback if they fulfil certain criteria set out in various provisions in Chapter 5 of the Satisfaction of Claims Act. Such transactions include 'extraordinary' payments of debt, gifts, security for 'old debt' and certain cases of set-off, to mention a few.

Some transactions may be subject to clawback even if they were carried out more than three months prior to the filing of the bankruptcy petition. Gifts may generally be subject to clawback if given within a period of one year prior to the filing of the petition. Furthermore, the time bar in most clawback provisions is extended to two years if the transaction in question benefits a party closely related to the debtor. Unfair transactions beneficial to the receiving party at a time when the receiving party is deemed not to have been acting in good faith, and at a time when the debtor's economic situation was weak or was severely weakened by the transaction, may be subject to clawback if carried out within a 10-year period prior to the filing of the bankruptcy petition.

If there are grounds for a clawback claim and it is executed, the receiving party of the transaction must return to the estate what was received from the debtor. If the receiving party was deemed to have been in bad faith, the estate may claim that the receiving party indemnifies the estate for the loss it has suffered as a result of the avoidable transaction.

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8 Sections 3–4 and 3–5 of the Limited Liability Companies Act.
9 Subject to provisions in Chapter 5 in the Satisfaction of Claims Act.
The estate must usually take legal action to collect the clawback claim within one year after the opening of the bankruptcy proceedings.

III RECENT LEGAL DEVELOPMENTS

See Section VI, infra, regarding a current evaluation of the Norwegian rules on judicial debt restructuring proceedings as well as changes to the Bankruptcy Act regarding cross-border matters.

Two Supreme Court decisions from the past year are especially relevant to the insolvency field: HR-2017-33-A regarding legal protection for a non-registered transfer of real estate; and HR-2017-370-A regarding a bankruptcy estate’s assessment of possible clawback claims.

In the first case, a real property transaction had been carried out by way of a demerger instead of a sale-and-transfer agreement, in order to avoid having to pay stamp duty. Hence, the change of ownership was not registered in the Land Registry. When the transferring company went bankrupt years later, its bankruptcy estate held that the transfer did not have legal protection and consequently that the property could be seized by the estate. The Supreme Court agreed with the estate, and thereby confirmed that a transfer of real property must be registered in the Land Registry to obtain legal protection, and thus clarifying a much debated legal question and establishing a wider protection against transactions seeking to bypass formal requirements.

In the second case, the Supreme Court implied in an obiter dictum that when an estate assesses whether or not a payment or transaction is sufficiently substantial for clawback (see Section II. iii), supra), payments or transactions to two or more recipients may be summarised and viewed together, establishing a broader clawback possibility. The court emphasised that such an approach might be applied only on exception and only if the recipients have a close financial relationship or can be seen as a group. An obiter dictum is a statement in a court verdict that is not essential to or necessarily based on the facts in a case, and is not considered as precedence.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

Over the past few years, as mentioned in Section I, supra, the oil and oil service industries have suffered due to the low oil prices, and there have been substantial lay-offs and other cost-reducing measures. In November 2016, it was estimated that more than 40,000 jobs had been lost because of the oil crisis. Since then, the market seems to have stabilized, as the unemployment rate is now reported to be slowly decreasing.

Furthermore, rig market prices and freight rates in shipping and the seismic industry have been low for some time. Several companies operating in these markets are currently financed through high-yield obligation loans that will expire during the next couple of years, and will probably be forced to seek alternative financing, which may lead to more bankruptcies if such financing cannot be obtained. The Norwegian bond market has experienced record growth in the number of corporate bonds listed since the financial crisis of 2008-2009, and

includes both medium-sized and large businesses.\textsuperscript{11} The Oslo Stock Exchange and the Nordic Alternative Bond Market combined held the third-largest market place for high-yield bonds in the world in 2014.\textsuperscript{12}

The Nordic mining industry has been suffering for a while, and in December 2014, the iron ore mining company group Northland Resources, with operations in several of the Nordic countries, decided to file for bankruptcy proceedings in a number of the group companies. In May 2015, the government decided to fund the mining company ‘Store Norske’ with 500 million Norwegian kroner after the company announced that it was in desperate need of funding to keep its operations going. The company runs three coal mines on Spitsbergen that together employ approximately 320 employees (Spitsbergen has only 2,670 inhabitants). Further, in November 2015, Sydvaranger Gruve AS, which operated mines in Finnmark, Norway and had between 350–400 employees, filed for bankruptcy.

Recent larger bankruptcies emerging from the current oil crisis include the listed company Dolphin Group ASA and its subsidiary Dolphin Geophysical AS, which were taken under bankruptcy proceedings in December 2015, and the oil service company Atlantic Offshore AS, which filed for bankruptcy in April 2016. Dolphin Geophysical AS was a global supplier of marine geophysical services, operating seismic vessels and performing surveys, multiclient projects and processing services.\textsuperscript{13} One of the main reasons for the bankruptcy was said to be reduced revenues as a result of the oil crisis. Atlantic Offshore AS operated several oil service vessels and experienced economic difficulties because of (according to the debtor) a lower demand for services from the oil industry. The company filed for bankruptcy proceedings following lengthy restructuring attempts, as it was no longer able to meet terms and conditions of its bond loans.

\section*{V INTERNATIONAL}

Norway has not implemented the EC Insolvency Regulation; nor has it adopted the UNCITRAL Model Law.

The Nordic Convention on Bankruptcy between Norway, Denmark, Finland, Iceland and Sweden has been in place since 1933. This Convention includes regulations on how the Member States should handle debtors’ assets located in the respective states when bankruptcy proceedings are opened in one of the other states. Further, the Convention establishes which country’s law should be applied in various situations, and provides rules on recognition and enforcement.

There is very limited Norwegian case law on international insolvency cases. However, a decision of the Supreme Court of Norway from 2013 is worth mentioning. The Court addressed the question of whether an established execution lien in a Spanish debtor's assets in Norway could be clawed back or set aside by the Spanish bankruptcy estate, and whether the debtor’s assets in Norway were protected by a stay on creditor enforcement actions because of the Spanish insolvency proceedings, thus giving the opening of insolvency proceedings in Spain legal effect with regards to the Spanish debtor’s assets in Norway. The Court ruled that the insolvency proceedings in Spain did not prevent separate debt recovery proceedings.

\textsuperscript{11} See Oslo Børs and Nordic ABM: ‘Issuing corporate bonds in Oslo – an efficient, flexible and mature market for raising debt capital’.
\textsuperscript{12} See Erik Lind and Klaus Henrik Wiese-Hansen ‘Norway: A transformed bond marker’. IFLR.
\textsuperscript{13} See www.dolphingeo.com/about/company-overview.
against the debtor’s assets in Norway, that is, stating that a clawback claim from the Spanish bankruptcy estate would not be recognised, and allowing creditors to enforce execution liens established in the debtor’s assets in Norway while the debtor was under insolvency proceedings in Spain. The Court stated that acknowledgement of insolvency proceedings in another state must primarily be based on mutual agreements between states or international legislation, and that no such agreement or legislation existed involving Spain.

VI FUTURE DEVELOPMENTS

There have been written hearings and opinions on whether Norway should implement the EC Insolvency Regulation, but there is still no such legislative proposal. The Regulation will likely not be ratified in Norway for several years (if indeed at all). However, in April 2016, the Ministry of Justice and Public Security published a legislative proposal to add a chapter with new provisions on cross-border insolvency matters. The chapter, which has not yet entered into force, was added to the 1984 Bankruptcy Act by an amending act dated 17 June 2016. The chapter includes provisions on both territorial and factual jurisdiction, choice of law rules, as well as recognition of foreign insolvency proceedings and the impact foreign proceedings shall have in Norway. Some of these legal principles appear to resemble certain provisions of the EC Insolvency Regulation. As of end June 2017, no date has been set for when the new chapter will enter into force.

The judicial restructuring scheme in Norway is under review, subject to a mandate given by the Ministry of Justice to Judge Leif Villars-Dahl with the Oslo Court of Probate and Enforcement. His mandate included, inter alia, to evaluate whether the current rules should be amended to facilitate a more flexible restructuring scheme with the aim of saving more businesses and preserving more jobs. Judge Villars-Dahl submitted his evaluation report to the Ministry of Justice on 1 March 2016, and the report has since been circulated for comments. The Ministry of Justice appointed a group of three lawyers and one economist to support him in his work; attorney Knut Ro, attorney Staale Gjengseth, attorney Stine D Snertingdalen and Professor Nils-Henrik von der Fehr.
Chapter 22

PORTUGAL

David Sequeira Dinis and Nair Maurício Cordas

I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

The events of the past few years have had a significant impact on the Portuguese economy and, consequently, on restructuring and insolvency activities. The deteriorating economic conditions caused by the financial crisis and felt in Portugal led the government to request external assistance from the International Monetary Fund, the European Commission and the European Central Bank (i.e., the Troika) in April 2011. As a result, a memorandum of understanding on specific economic policy was entered into between the Portuguese state and the Troika on 3 May 2011, according to which the quarterly disbursement of financial assistance to Portugal would depend on the implementation of a series of structural reforms by the government, inter alia, amendments to the Portuguese Insolvency and Restructuring Code, with a view to facilitate an effective restructuring of viable companies.

The overall financial difficulties felt by companies in Portugal – namely, due to the shortage of liquidity and access to financing for their activities – aggravated by the reforms imposed by the Troika, led to a considerable rise in insolvency and restructuring procedures as of 2008. In accordance with official data from the Portuguese Ministry of Justice, the overall increase of new insolvency proceedings filed between the fourth quarter of 2007 and the fourth quarter of 2013 corresponded to approximately 358.5 per cent.

Although the financial crisis is not considered to be over, and its effects are still very much felt by all market participants, 2014 appeared to have been a turning point for the Portuguese economy and the country’s restructuring and insolvency activities. It was the year that the Troika ‘left’ Portugal and, in accordance with a study performed by Cosec, the number of insolvency proceedings filed in 2014 decreased 33 per cent when compared with the number of proceedings filed in the previous year, corresponding to a total of 4,019 filings.

The most recent data shows that this positive trend was maintained throughout the last year. Indeed, in accordance with the study Economic Insight 2016–17: Tectonic shifts and risk of local tremors, although the year 2016 ended with an increase of 1 per cent in insolvencies world-wide, the number of insolvency proceedings filed Portugal that year decreased 18 per cent.

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In addition, as of the closing of the first quarter of 2017, and in accordance with a study performed by Cosec, 839 companies were declared insolvent, which represents a fall in 20 per cent in the number of new proceedings when compared with the first quarter of 2016.5

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Insolvency and restructuring procedures

The insolvency and restructuring procedures available in Portugal are governed by the Portuguese Insolvency and Restructuring Code approved by Decree-Law No. 53/2004, of 18 March, as amended (CIRE) and by Decree-Law No. 178/2012 of 3 August, recently amended by Decree-Law No. 79/2017 of 30 June.

Portuguese law currently establishes four different insolvency and restructuring procedures: an insolvency procedure, a special revitalisation procedure, a special payment agreement procedure and a system of extrajudicial recovery of undertakings.

CIRE provides for a single main insolvency proceeding (called processo de insolvência), the main purpose of which is to obtain payment for the insolvent’s creditors through the implementation of an insolvency plan or, should that prove to not be possible, through the liquidation of the insolvent’s estate and subsequent distribution of the proceeds among the creditors.

In general, a debtor is deemed to be insolvent when it is unable to perform its overall obligations as they fall due or when its liabilities significantly exceed its assets (over-indebted balance sheet). Insolvency proceedings may, thus, be initiated, inter alia, in the following circumstances:

a dissipation of the debtor’s assets;
b the debtor’s failure to pay, within a six-month period prior to the filing for involuntary insolvency, its tax liabilities, social security obligations, wages, or any rent, lease or instalment relating to the purchase or loan obtained to acquire the company’s premises;
c if the debtor is a company and its liabilities clearly exceed the company’s assets, in reference to the last approved balance sheet (the above-mentioned over-indebted balance sheet); or
d when there is a delay of at least nine months in approving the company’s annual financial statements.

Insolvency proceedings may be filed by the debtor, any of its creditors (regardless of the nature of the credit), any person who is responsible for the debtor’s liabilities or the public prosecutor. In this respect, it should be noted that the directors of a company have the legal duty to file for insolvency within 30 days from the date on which they become aware of, or should have become aware of, an insolvency situation, as further explained below.

The commencement of insolvency proceedings has an impact on the debtor, pending legal procedures, and the ongoing business and credits owned by the insolvent. As of the declaration by the court of the insolvency of a debtor, the insolvent will be controlled by an insolvency administrator appointed by the court who, as a general rule, will be responsible for managing the insolvent’s estate, and will be entitled to carry out any acts and be involved

in any transactions within the ordinary course of business, with the exception of specific acts of material relevance, which require the creditors’ prior consent. In addition, although the directors of the company remain in office, and must cooperate with the insolvency administrator, the creditors’ general meeting, the creditors’ committee and the court, they do so with limited powers and without receiving any compensation for the performance of their duties, and may resign upon submission of the annual financial statements of the company. Notwithstanding, in specific cases, the directors of the insolvent company may continue to exercise active management functions under the insolvency administrator’s supervision.

On the other hand, from the moment of the declaration of insolvency, creditors may only satisfy their credit within the scope and by means of the insolvency proceedings by lodging their claim with the insolvency administrator within the specific term set by the court for this purpose (up to 30 days); thus, the filing or continuation of any enforcement proceedings filed by insolvency creditors against the insolvent are halted, and the insolvent’s obligations are accelerated to maturity.

It should also be noted that Portuguese law establishes specific rules with regard to the classes of credits and the ranking of claims:

a. claims over the insolvent’s estate (for instance, court fees, the insolvency administrator’s fees, the costs and expenses of the insolvent estate’s management or liquidation, or both, and debts or claims resulting from obligations incurred under contracts entered into by the insolvent company after the declaration of insolvency), which are ranked above any other and are to be paid first, usually, with the proceeds resulting from the insolvency administrator’s activity;

b. secured claims, which comprise secured credits (typically by a mortgage or pledge) and claims for credits with special legal privileges (e.g., certain employee and tax claims), which have priority over the proceeds of the sale of the assets to which they are linked;

c. privileged claims (i.e., claims protected by general legal privileges, which are usually granted to ensure tax and social security collection, and have priority over common and subordinated claims);

d. common claims (i.e., unsecured, unprivileged and unsubordinated credits, which are satisfied on a pro rata basis once those claims referred to above have been paid); and

e. subordinated claims, which are only paid after all other creditors have been satisfied in full (namely, credits of creditors with a special relationship with the debtor, e.g., directors, shareholders, and interest due after the declaration of insolvency).

The Portuguese Supreme Court recently rendered two important decisions with direct impact to the ranking of claims, having harmonised its case law with regard to employees and promissory buyers’ secured credits.

On the one hand, the Portuguese Supreme Court recently decided that the properties built by a construction company within its commercial activity (i.e., the intent to sell it) are excluded from the special legal privilege over the employer’s property granted to labour credits under Portuguese labour law. Said credits will not, therefore, be ranked as secured claims.6

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6 Decision dated 23 February 2016, proceedings No. 1444/08.5TBAMT-A.P1.S1-A.
On the other hand, the Portuguese Supreme Court decided that the retention right over the promised property granted to promissory buyers – that prevails over mortgages registered beforehand – is only granted to promissory buyers that are consumers.7

As referred to above, the insolvency proceedings’ main purpose is to obtain payment for the insolvent’s creditors through the implementation of an insolvency plan. Thus, in the course of the proceedings, the creditors’ general meeting may resolve on the approval of an insolvency plan that, upon approval by the court, binds all creditors, including those who have voted against it or who have not attended the meeting. In order for the insolvency plan to be approved, the following quorums must be met: at least one-third of the creditors with voting rights must attend (or be duly represented in) the relevant meeting; more than two-thirds of the votes cast therein must endorse the approval of the plan; and more than half of the votes cast must be issued by unsubordinated creditors. Once approved by the creditors, the plan needs to be affirmed by the court before producing effects over all creditors.

In this regard, CIRE does not contain specific provisions on which measures may be set out in an insolvency plan, and thus the creditors are free to choose any such measures. Accordingly, the plan may, for instance, set out a reduction or waiver of debts; condition the satisfaction of the debts on the insolvent’s availability; impose the granting of securities by the insolvent company; and determine the sale of assets to creditors. In addition, unless otherwise provided for in the insolvency plan, the rights arising from securities in rem or credit privileges are not affected by the insolvency plan, subordinated credits are deemed waived and, upon fulfilment of the insolvency plan, the insolvent company is deemed discharged of its residual obligations.

If, however, the approval of an insolvency plan is not feasible, the payment of the insolvent’s creditors will be assured through the full liquidation of the insolvent’s estate and subsequent distribution of the proceeds among them.

The closing of the insolvency proceeding will be ordered by the court, inter alia, in the following cases:

a after the final allotment of assets, upon registration of which the company will cease to exist;
b when the court ruling that affirmed the insolvency plan has the force of res judicata (unless if otherwise provided therein);
c upon request of the insolvent, when the insolvency situation ceases or all creditors consent to closing the proceedings; or
d when the insolvency administrator concludes that the insolvent’s estate is insufficient to pay the court costs and the remaining debts of the insolvent’s estate.

On the other hand, the pre-insolvency procedure called the ‘special revitalisation procedure’ was implemented in 2012, and was recently significantly amended,8 with the aim of establishing a formal legal framework for companies in financial distress to negotiate a recovery plan with their creditors (which comprises any measure of debt relief). This procedure thus aims to resolve situations of severe economic and financial difficulty, or near-insolvency situations, through the approval of a recovery plan by the creditors.

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7 Decision dated 19 May 2019, proceedings No. 92/05.6TYVNG-M.P1.S1.
8 The amendments were enacted by Decree-Law No. 79/2017 of 30 June.
Pursuant to the amendments recently enacted, in order to be eligible to use this procedure, the debtor must file a statement subscribed by a certified accountant or statutory auditor, whenever applicable, certifying that the debtor is not in a current state of insolvency.

The special revitalisation procedure is initiated by the debtor, together with at least one of its creditors, which cannot be a specially related party and must hold at least 10 per cent of the unsubordinated credits, by submitting to the court a statement of their intention to negotiate a recovery plan. Pursuant to the recent amendments, the said statement of intention to negotiate a recovery plan must be filed together with a proposal of the recovery plan, as well as a description of the company's patrimonial, financial and credit situation.

All creditors are invited to participate in the negotiation of the recovery plan, which takes place in an out-of-court context and lasts for a maximum period of three months. During this phase, a grace period is granted to the debtor, since the creditors are not entitled to request the court to declare its insolvency and all pending legal proceedings envisaging debt collections are halted. After being approved, under the same terms and with the same majorities as the insolvency plan as provided above, and being affirmed by the court, the recovery plan is binding on all creditors, even if they did not participate in the negotiations.

The amendments recently enacted to the ‘special revitalisation procedure’ limited its scope of application to companies, and therefore, a special payment agreement procedure was created. Said procedure is applicable to legal persons that are not companies, as well as natural persons, provided that they are ‘a difficult economic situation or in a situation of imminent insolvency’.

The aim of this procedure is to establish negotiations with the creditors in a simple and efficient form, with the view of creating the necessary conditions for the entering into payment agreements that allow the recovery of the debtor.

In general terms, the legal regime of this new special payment agreement procedure is very similar to that of the special revitalisation procedure regime.

Finally, Portuguese law also provides for a ‘system of extrajudicial recovery of undertakings’ (SIREVE), enacted by Decree-Law No. 178/2012 of 3 August. This is an out-of-court procedure, the goal of which is to promote the extrajudicial recovery of undertakings, creating conditions for an agreement to be negotiated by the undertaking and its creditors that represent at least 50 per cent of the total amount of the company’s debt, and that make the recovery of the undertaking's financial situation viable. Such agreement may comprise the application of any means of debt relief. Contrary to the special revitalisation procedure, the SIREVE is conducted by the Institute for Assistance to Small and Medium-sized Companies and Innovation (IAPMEI).

SIREVE’s scope of application is limited to companies and sole traders with organised accounts that are now in a difficult economic situation or a situation of imminent insolvency, and obtain an overall positive assessment of certain financial indicators, under the new mandatory prior analysis carried out through a IAPMEI platform.

The recovery plan within the SIREVE is considered to be approved if it is voted on by creditors whose claims represent at least one-third of the company’s total debts, receives favourable votes from more than two-thirds of all the votes cast and more than half of the votes cast correspond to unsubordinated claims, not considering abstentions; or it receives favourable votes of creditors whose claims represent more than half of the company's total debts and more than half of these votes correspond to unsubordinated claims, not considering abstentions.
In addition, in the event of insolvency, creditors that during the proceedings finance the debtor’s activities by providing capital for its recovery are entitled to general preferential claims granted to employees, and the guarantees agreed between the debtor and its creditors during the procedure to provide the debtor with the financial means necessary to pursue its business activity shall remain in place for a period of two years even if, at the end of the procedure, the company is declared insolvent or it initiates a new restructuring process.

On the other hand, the measures set out in the recovery plan approved within the SIREVE also benefit from the application of fee and tax relief provided for in the CIRE.

Finally, the amendments introduced by Decree-Law No. 26/2015 establish that once the agreement is signed, enforcement proceedings brought against the company or against its guarantors, or both, are automatically extinguished, and the proceedings aimed at obtaining the payment of credits brought against the company or its guarantors, or both, remain halted, due to prejudice. However, this measure is exclusively applicable to creditors that have signed the agreement.

## ii Duties of directors of companies in financial difficulties

As referred to above, the managers and directors (including shadow or de facto directors) of a company have the legal duty to file for insolvency within 30 days from the date on which they become aware of, or should have become aware of, an insolvency situation. Directors who breach this legal duty may be subject to civil and criminal penalties. For this purpose, there is a legal assumption of serious fault should the directors fail to apply for insolvency within 30 days of the moment when the company was de facto insolvent, or fail to draft and submit yearly accounts for the company.

Furthermore, the insolvency may be classified as culpable or fortuitous when the situation was created or aggravated as a result of the conduct (with dolus or with gross negligence) of the debtor or of its directors, in law or in fact, in the three years preceding the commencement of the insolvency proceedings. Notwithstanding, an insolvency is always classified as culpable when the managers or directors of the insolvent company debtor have:

a. destroyed, damaged, hidden or made disappear all or part of the debtor’s assets;

b. artificially created or aggravated damages or liabilities, or reduced profits, causing, in particular, the execution by the debtor of ruinous contracts for the benefit of the debtor’s directors or people specially related with them (which includes the spouses, descendants or siblings of directors);

c. purchased goods on credit, reselling them or delivering them in payment for substantially less than the current price before satisfying the obligation towards the credit lender;

d. used the debtor’s assets for personal benefit or for the benefit of third parties;

e. exercised under the guise of the legal personality of the company an activity for personal benefit or for the benefit of third parties, and to the detriment of the company;

f. used the credit or assets of the debtor for personal benefit or for the benefit of third parties and to the detriment of the company, in particular to promote another company in which they have direct or indirect interests;

g. for personal benefit or for the benefit of third parties, kept managing the debtor with negative results, despite knowing or having ought to have known that this would likely lead to the insolvency of the debtor;

h. failed to comply with the obligation to keep proper account of the debtor, maintained a fictitious accounting of the debtor or committed a fault jeopardising the chance of understanding the financial situation of the debtor; or
repeatedly violated their obligations to be at court when duly summoned and to cooperate with the insolvency proceedings.

When the insolvency situation is deemed to be caused by the directors’ mismanagement, the court may:

a declare their incapacity to manage any third party’s estate for a given period;

b prevent the persons held liable from performing commercial activities for a given period, including as a member of the board of directors of any company;

c order that these persons may not be considered as creditors of the insolvent company or of the insolvent’s estate, and require them to return to the insolvent’s estate any amount already received; and

d sentence the directors to indemnify creditors up to the amount of their unpaid credits.

In addition, it should be noted that, under extreme circumstances, directors may be subject to criminal penalties if they have, in any way, defrauded creditors or fraudulently contributed to the insolvency of the company, or both.

iii Clawback actions

According to the CIRE, several types of transactions may be challenged by the insolvency administrator once insolvency proceedings have been commenced. All acts that may be qualified as detrimental to the insolvent’s estate, such as acts that diminish, frustrate, hinder, endanger or withhold the satisfaction of the insolvency creditors, performed within two years prior to the beginning of the insolvency proceedings, may be subject to clawback.

In general, the termination of said transactions is only possible if the counterparty acted with wrongful intent (i.e., at the date the act was performed, knowledge that the debtor was in an insolvent situation; knowledge of the prejudicial nature of said act to the debtor’s situation and that the insolvency situation was imminent; or knowledge that the insolvency proceeding had already been initiated). For this purpose, Portuguese law provides for a rebuttable presumption of wrongful intent if the transaction takes place within the two years prior to the commencement of the insolvency proceedings and it involves any parties related to the insolvent.

Notwithstanding, the following acts, inter alia, may be subject to clawback regardless of any other requirements:

a gratuitous acts performed within two years prior to the commencement of the insolvency proceedings;

b granting of in rem security to preexisting credits or to other credits that replace them within the six-month period prior to the commencement of the insolvency proceedings;

c granting of personal guarantees or of credit mandates within the six-month period prior to the commencement of the insolvency proceedings that relate to transactions without any real benefit to the debtor; and

d reimbursement of shareholders’ loans made during the year before the beginning of the insolvency proceeding.

In any case, the termination of the referred transactions must be invoked by the insolvency administrator, by means of a registered letter with notice of receipt, within six months
counted from knowledge of the act, or two years counted from the judicial declaration of insolvency. Should the insolvency administrator decide not to exercise the clawback, any creditor may resort to an actio Pauliana.

Finally, pursuant to the recent enacted amendments, CIRE expressly sets forth that certain transactions, such as those entered into in the context of a special revitalisation procedure, a special payment agreement, a SIREVE and the adoption of resolutions measures foreseen in the General Regime of Financial Institutions,9 are not subject to clawback actions.

III RECENT LEGAL DEVELOPMENTS

The most recent legislative developments pertaining to insolvency and restructuring relate to the above-mentioned special revitalisation procedure.

Although until 2012 the main goal of insolvency proceedings under Portuguese law was to obtain payment for the insolvent’s creditors through the most efficient approach, the enactment of Law No. 16/2012 clearly intended to favour the approval of an insolvency plan with the main purpose of recovering the insolvent company.

To facilitate this goal, and in the context of the ‘Programme to Capitalize’ – a programme to support the capitalisation of companies, investment and relaunch of the economy, approved by the Resolution of the Council of Ministers No. 42/2016, of 18 August – Decree-Law No. 79/2017, of 30 June was recently enacted, significantly amending the special revitalisation procedure.10

The most relevant amendments to the special revitalisation procedure are as follows:

\( a \) the special revitalisation procedure is now only applicable to companies, while other legal persons and natural person are subject to the new special payment agreement procedure;

\( b \) the initial application for a company to be subject to a special revitalisation procedure now has to be accompanied by:

- a statement signed by a certified accountant or statutory auditor, issued no more than 30 days, attesting that the company is not in current insolvency; and
- a proposal for a recovery plan accompanied by at least a description of the company’s patrimonial, financial and credit situation;

\( c \) until now, the special revitalisation procedure could be initiated by the debtor together with any of its creditors; following the amendments enacted, the procedure must now be initiated by the debtor with at least one of its creditors that must hold at least 10 per cent of the unsubordinated claims and cannot be a specially related party;

\( d \) it is expressly set forth that the special revitalisation procedures of commercial companies in a control or group relationship may be joined into one;

\( e \) with the appointment of the provisional judicial administrator, the limitation periods applicable to the company are suspended and the provision of essential public services, such as, water supply service, electric power supply service, etc., cannot be suspended for as long as the negotiations continue;

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9 Approved by Decree-Law No. 298/92, of December 31.
10 Amendments that entered into force on 1 July 2017.
following the amendments enacted, any creditor can, within five days of the publication of the recovery plan in the Citius portal, file a petition alleging the circumstances that he or she considers likely to lead to the same not being approved, the debtor being allowed to amend the plan accordingly; and

following the amendments enacted, the debtor cannot submit a new recovery plan within two years of the approval of the previous recovery plan, unless the company demonstrates that it has fully implemented the previous plan or that the need to submit a new plan is driven by factors unrelated to the previous plan or by supervening and extraneous circumstances.

On the other hand, Decree-Law No. 79/2017, of 30 June also introduced amendments to the insolvency procedure, of which the following are highlighted:

a with regard to the appointment of the insolvency administrator, in the case of a commercial company in a control or group relationship with other companies in respect of which insolvency proceedings have been proposed, the court may, at its own discretion or pursuant to a petition filed by the debtor or the creditors, appoint the same insolvency administrator for all companies, in which case he or she shall also nominate, in general terms, another insolvency administrator with duties limited to the assessment of claims claimed among debtors of the same group;

b with regard to the appointment of a provisional judicial administrator, in addition to situations in which management acts requiring special knowledge are foreseeable, the court may take into account any proposal that may be made in the petition of the debtor, when it is in a control or group relationship with other companies whose insolvency has been sought and the appointment of the same administrator in the various proceedings; and

c CIRE now sets forth that certain transactions, such as those entered into in the context of a special revitalisation procedure, special procedure for a payment agreement, SIREVE and the adoption of resolutions measures foreseen in the General Regime of Financial Institutions, are not subject to clawback.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

In the past couple of years, Portugal has seen several high-profile restructuring cases, of which the landmark case is directly related to the crisis in Group Banco Espírito Santo and Group Espírito Santo Financial Group.

On 3 August 2014, after a succession of events, the Bank of Portugal applied a resolution measure to Banco Espírito Santo in the form of the transfer to a bridge bank created for such purpose (Novo Banco). Banco Espírito Santo was a major Portuguese bank and part of one of the biggest economic groups in Portugal, holding interests across several sectors (namely the insurance, real estate, tourism, health, agriculture and energy sectors). This crisis led to the filing of several insolvency and restructuring proceedings regarding a number of companies within the Banco Espírito Santo and Grupo Espírito Santo group, both nationally and internationally.

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11 Approved by Decree-Law No. 298/92, of December 31.
In effect, in late 2014, five Grupo Espírito Santo companies with head offices in Luxemburg were declared insolvent, albeit having requested to be subject to controlled management: Espírito Santo Control, the holding company of the entire group), Espírito Santo International, Rioforte, Espírito Santo Financial Group and Espírito Santo Financière.

In Portugal, the first company of the group to be subject to a restructuring procedure was Espírito Santo Irmãos, SGPS, SA, which initiated a special revitalisation procedure in 2014. The special revitalisation procedure was not successful, and the company was declared insolvent. Subsequently, Espírito Santo Financial (Portugal), SGPS, SA was also declared insolvent.

As a direct consequence of the group’s crisis, Hotéis Tivoli, SA and Marinotéis, SA, which own 14 hotels in Portugal and Brazil, were not able to sell their properties and had to file for a special revitalisation procedure. Most recently, Espírito Santo Hóteis, SA, which initiated a special revitalisation procedure that was not successful, was also declared insolvent.

On 13 July 2016, the European Central Bank revoked BES’s banking licence, thus, and according to the applicable legislation, the bank was placed into liquidation. In effect, pursuant to Decree-Law No. 199/2006 – which regulates the liquidation procedures of Portuguese credit institutions – the withdrawal of BES’s banking licence produces the effects of the declaration of insolvency, which procedure is subject to the provisions of said Decree-Law.

Furthermore, following the failed attempt by Banif’s shareholders and its board of directors to sell the bank and a succession of events, the Portuguese government and the Bank of Portugal decided to sell Banif’s business and most of its assets and liabilities to Banco Santander Totta. The sale was carried out in the context of a resolution measure, similar to that applied to BES, and is expected to also culminate in Banif’s liquidation, pursuant to the its banking licence being revoked.

Most recently, due to the difficulties felt in the past few years in the construction sector, both in locally and internationally, several companies have implemented restructuring measures. Following the application for a special revitalisation procedure by Opway, a construction company formerly part of the BES group, several companies of the Soares da Costa construction group, one of the largest construction groups in Portugal, also filed for special revitalisation proceedings. More recently, four companies of the MSF construction group also initiated special revitalisation procedures.

V INTERNATIONAL


According to Regulation (EU) No. 2015/848, the proper functioning of the internal market requires that cross-border insolvency proceedings operate efficiently and effectively in order to avoid incentives for parties to transfer assets or judicial proceedings from one Member State to another, or seeking to obtain a more favourable legal position to the detriment of the general body of creditors (i.e., forum shopping).

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12 However, insolvency proceedings commenced prior to 26 June 2017 are still subject to EC Regulation No. 1346/2000.
Regulation (EU) No. 2015/848 is an update of EC Regulation No. 1346/2000. In short, the new Regulation:

- a extends its scope of application to proceedings that promote the recovery and revitalisation of the debtor;
- b strengthens the legal framework for cooperation and communication between the participants, namely between courts, and between courts and insolvency administrators;
- c improves coordination between open insolvency proceedings regarding the same debtor or the same group in the event of proceedings in respect of companies that are part of a group;
- d gives priority to the concentration of efforts in the main proceedings, allowing the judge to halt the opening of secondary proceedings if it is shown that the rights of the local creditors are ensured; and
- e increases the publicity of insolvency through the insolvency registers by the Member States and their respective interconnection.

In this respect it should be noted that, although council regulations are automatically binding on Member States at the equivalent level of domestic law, Portugal has also implemented EC Regulation No. 1346/2000 through the enactment of Articles 271 to 274 of CIRE.

Pursuant to Article 271 of CIRE, whenever the insolvency proceedings uncover the existence of a debtor’s assets located in another Member State of the EU, the judgment declaring the insolvency of the debtor shall state the factual and legal reasons that justify the jurisdiction of the Portuguese courts. In line with this article, it should be noted that Article 3 of Regulation (EU) No. 2015/848 (equivalent to Article 3 of the EC Regulation No. 1346/2000) sets forth that:

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\text{[...]} \text{the courts of the Member State within the territory of which the centre of the debtor's main interests is situated shall have jurisdiction to open insolvency proceedings ("main insolvency proceedings"). The 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.}
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Furthermore, Articles 275 to 296 of CIRE provide for rules of private international law intended to resolve conflicts of law in respect of insolvency matters, which are only applicable provided that they do not contradict the provisions of the EC Regulations.

On the other hand, the recognition and enforcement of foreign insolvency judgments depends on the awarding country. Thus, any judgment declaring the insolvency handed down by a court of a Member State that has jurisdiction pursuant to Regulation (EU) No. 2015/848 shall be recognised in all other Member States from the time that it becomes effective in declaring state. Outside the EU, the recognition and enforcement of a foreign insolvency judgment in Portugal requires a special \textit{exequatur} procedure to be initiated, which shall be granted, provided that:

- a there are no doubts regarding the authenticity of the document;
- b the judgment is final in the awarding country and is not subject to any appeal;
- c the jurisdiction of the country that issued the judgment was not fraudulently created and the subject matter is not of the exclusive jurisdiction of Portuguese courts;
- d there are no lis pendens or \textit{res judicata} exceptions due to cases filed in Portugal, except if the foreign court anticipated jurisdiction;
The defendant was duly served, and the principles of defence and equality duly observed; and
the judgment does not offend the international public policy principles of Portugal.

Finally, it should be noted that the UNCITRAL Model Law on cross-border insolvency has not been adopted in Portugal.

VI FUTURE DEVELOPMENTS

Notwithstanding the recent legislative amendments referred to above, further amendments are expected shortly.

In effect, the government has already announced that it wishes to implement an extrajudicial regime for the recuperation of companies, by means of which a debtor may enter into negotiations with all or some of its creditors with a view of reaching an voluntary and, generally, confidential agreement aimed at its recovery. Once certain requirements have been met, the agreement shall have certain effects, namely, in what regards its tax treatment, as if it were approved in the context of a special revitalisation procedure. According to the Portuguese Minister of Justice, this new procedure may lead to the extinction of the SIREVE.

In what regards restructuring activity in Portugal, the number of insolvency proceedings is expected to decrease further in the next year, although we estimate that the size of the proceedings will increase. However, in light of the recent amendments to the restructuring procedure, namely, the special revitalisation procedure, we expect to see an increase in the number of restructuring procedures of Portuguese companies, in particular, in groups of companies – which procedures can now be evaluated jointly – specifically those in the banking and construction sectors as these sectors are very exposed to the Venezuelan and Angolan economies, which are currently going through severe crises.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

2017 was a watershed year for legal developments concerning insolvency and restructuring in Singapore. The Singaporean parliament passed a landmark set of legislative amendments that introduced radical changes to the restructuring framework (the 2017 Amendments). Economic uncertainties and an upswing in distressed situations in certain sectors of the economy also meant that the Singaporean courts were called upon to decide novel issues of cross-border insolvency. Many of these developments can be attributed to the demands of an increasingly global and interconnected Singaporean economy. With cross-border trade the norm, complex cross-jurisdictional issues in restructuring and insolvency have come to the fore.

While the legislative changes had their origins in Singapore’s endeavour to be an ‘international centre for debt restructuring’, there were also wider social and economic concerns at play. With global corporate defaults reaching highs not seen since the 2008 financial crisis, the slowing trend of global trade, lacklustre consumer and business sentiment and persistently low oil prices dominated financial headlines in Singapore in 2016 and 2017. In 2016, approximately 280 corporate winding-up petitions were filed – the highest levels since the Singaporean economic recession, which lasted from 2001 to 2003. The struggling offshore and marine industry, which saw a number of prominent players fall

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1 Kenneth Lim Tao Chung is a partner at Allen & Gledhill LLP.
2 See further at Section III(i), infra.
3 See further at Section III(ii), infra.
4 Report of the Committee to Strengthen Singapore as an International Centre for Debt Restructuring (Debt Restructuring Committee Report) at p.6.
prey to difficult economic circumstances, employs some 88,000 people in Singapore alone.8 Thus, it was recognised that part of the impetus to the sweeping amendments was to provide viable restructuring alternatives to liquidation so as to rehabilitate ailing businesses.9

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Restructuring and insolvency legal framework

The main sources of legislation in Singapore governing corporate restructuring and insolvency are the Companies Act, with certain provisions in the Bankruptcy Act imported into the Companies Act with necessary modifications. Both Acts are supplemented by various subsidiary legislation.10 Under the framework, there are three broad areas of court-supervised insolvency and restructuring procedures for companies: schemes of arrangement, judicial management and liquidation.

**Schemes of arrangement**

Part VII of the Companies Act sets out the statutory framework for schemes of arrangement. A scheme of arrangement is a statutory mechanism for securing agreement between a company and its creditors, members or shareholders in respect of a compromise or arrangement without the need for unanimous consent. Thus, under the scheme, creditors may, for example, agree to rearrange or extinguish debts owed by the company to them in part or in whole, or to defer repayment of the same. Recent amendments to the Companies Act have sought to address potential shortcomings in the scheme of arrangement process,11 and these are discussed further in Section III, infra.

**Judicial management**

Part VIIIA of the Companies Act sets the statutory framework for judicial management. Judicial management may be utilised either as a tool for corporate rescue or to carry out a more advantageous realisation of a company's assets than would be possible in a winding up. As regards the former, it has been observed that the rehabilitative value of judicial management has been hampered by perceived weaknesses in the statutory regime, arguably contributing to a historically low success rate.12 Recent amendments to the Companies Act have been introduced to address these potential shortcomings, and these are discussed further in Section III, infra.

**Liquidation**

Under the Companies Act, a company may be wound up compulsorily by the court or voluntarily.13 In a compulsory liquidation, parties with standing under the Companies Act,
including creditors of a company, may apply to court for an order that a company be wound up. The Companies Act provides a list of grounds upon which the court may make an order to wind up a company, chief of which is that the company is ‘unable to pay its debts’. A statutory presumption that the company is unable to pay its debts arises in two circumstances. First, and most commonly relied on, if a statutory demand for a sum exceeding S$10,000 has been duly issued to the company and the company for three weeks thereafter neglects to pay the sum or to secure or compound for it to the creditor’s reasonable satisfaction, the company is deemed to be unable to pay its debts. Second, if an execution or other process issued on a judgment of any court against the company is returned unsatisfied in whole or in part, the company is also deemed to be unable to pay its debts.

Where the creditor does not rely on either of these statutory presumptions, the creditor must prove to the satisfaction of the court that the company is unable to pay its debts (including contingent and prospective debts, if any). In this regard, the courts have eschewed any single test for insolvency, preferring instead to have regard to all evidence which may appear relevant to the question of insolvency. That being said, in general, there are two tests that courts typically deploy – namely, whether the company is ‘cash-flow insolvent’ (i.e., unable to pay its debts as they fall due) and ‘balance-sheet insolvent’ (i.e., the company’s liabilities, including contingent and prospective liabilities, exceed its assets).

In a voluntary liquidation, the court need not get involved. There are two types of voluntary liquidation – a creditors’ voluntary liquidation (CVL) and a members’ voluntary liquidation (MVL). As a matter of procedure, both CVL and MVL are commenced by the company resolving by special resolution (i.e., by a majority of not less than three-quarters) that it be wound up voluntarily. If the company’s directors are able to make a declaration that the company will be able to pay its debts in full within a period not exceeding 12 months after the commencement of winding up, the liquidation begins as an MVL. In practice, therefore, in the context of corporate insolvency where the company is unable to pay its debts, it is likely to be wound up by CVL. An MVL may be converted into a CVL at any time if the liquidator appointed forms the view that the company will not be able to pay or provide for the payment of its debts within the period stated in the aforesaid declaration.

A key difference between an MVL and CVL is that in a CVL, the company must convene a meeting of creditors, where the creditors will be able to nominate a liquidator that will prevail over the company’s nomination.

**ii Statutory avoidance provisions and clawback**

This section discusses a number of recent, non-exhaustive examples of clawback actions.

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14 Section 253 of the Companies Act.
15 See Section 254 of the Companies Act for the full list.
16 Section 254(1)(e) of the Companies Act.
17 Section 254(2)(a) of the Companies Act.
18 Section 254(2)(b) of the Companies Act.
19 Section 254(2)(c) of the Companies Act.
20 *Chip Thye Enterprises Pte Ltd (in liquidation) v. Phay Gi Mo* [2004] 1 SLR(R) 434 at [20].
21 Section 290(1)(b) of the Companies Act.
22 Section 298 of the Companies Act.
23 Section 295 of the Companies Act.
24 Section 296 of the Companies Act.
25 Section 297(1) of the Companies Act.
Any disposal of the company’s property made after the commencement of winding up is void. However, it is possible to apply to court to prospectively or retrospectively validate such disposal. In Centaurea International Pte Ltd (in liquidation) v. Citus Trading Pte Ltd [2016] SGHC 264 the court confirmed that it was empowered to make a prospective validation order, or a retrospective validation order where the applicant party is unaware of the winding-up proceedings.

Additionally, certain transactions entered into by the company prior to the commencement of liquidation may be void or voidable. An ‘unfair preference’, which is a transaction that has the effect of putting a creditor in a better position than the creditor would otherwise have been in the event of the company’s insolvency had the preference not been given, may be set aside if the transaction was entered into in the six months preceding the commencement of winding up. Where the person preferred is a ‘person connected with the company’ (including directors of the company), this period is two years. An unfair preference must have been made with the intention to prefer – an intention that is presumed if the transaction is entered into with a person connected with the company. The Singapore courts recently accepted the ‘running account’ principle as a defence of the intention to prefer, whereby a continuing relationship of debtor and creditor may be sufficient to show that the transaction was entered into by reference to proper commercial considerations (provided that the impugned transaction has been entered into with the intention of obtaining new value to keep the business going).

An ‘undervalue transaction’, including transactions that were entered into for no consideration, or for a value of which (in money or money’s worth) is significantly less than the value (in money or money’s worth) of the consideration provided, may be set aside if entered into within the five years preceding the commencement of winding up. However, the transaction will not be set aside if it is proven that the transaction was entered into in good faith for the purpose of carrying on the company’s business, and there were reasonable grounds for believing that the transaction would benefit the company.

A floating charge entered into within six months from the commencement of the winding up is valid to the extent of any cash paid to the company in consideration for the charge, unless it is proven that the company was solvent immediately after the creation of the charge.

In respect of the potential remedies that a Singaporean court may order, it has been recently affirmed that a Singaporean court has powers to order a partial reversal of transactions in appropriate cases if ‘justice so requires’, for example, where the parties’ claims are uncontroversial, or there is an agreement between the creditors and the liquidator. This is to avoid a situation in which related companies repaid the monies to the company, only to have a substantial portion of those monies repaid to themselves as unsecured creditors of the company.

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26 Section 259 of the Companies Act.
27 Section 329 of the Companies Act, read with Section 99 of the Bankruptcy Act.
28 Living the Link Pte Ltd (in creditors’ voluntary liquidation) v. Tan Lay Tin Tina [2016] 3 SLR 621 (Living the Link) at [48].
29 Section 329 of the Companies Act read with Section 98 of the Bankruptcy Act.
31 Section 330 of the Companies Act.
32 Living the Link at [76].
The above applies similarly in judicial management, with the necessary modifications.33

iii The position of secured creditors
When entering into a loan transaction with a company which is insolvent or near insolvency, secured creditors should be mindful of the statutory avoidance provisions discussed in Section II(ii), supra.

Further, any creditor intending to secure the debt with a floating charge should take care to ensure the floating charge is registered within 30 days, failing which the floating charge is void as against a liquidator.34

As to the enforcement of security, in a winding up, the court may make an order to stay or restrain further proceedings against the company at any time after the making of a winding-up application.35 Further, upon the winding-up order being made, no action or proceeding shall be commenced without the leave of court.36

As to the ranking of creditors in distribution, a creditor with a registered floating charge is subordinated to a creditor with a fixed charge and certain statutory preferential debts, but ranks ahead of unsecured creditors.37

The Singaporean courts have also recently clarified that, in an insolvency situation, where goods in which one secured party has a perfected security interest have been commingled with goods in which another party has a perfected security interest, each party is entitled to the proportion of the product that the value of that secured party’s collateral bore to the sum of the value of both parties’ collateral at the time of the commingling.38

iv Directors’ duties in insolvency
A director is under a duty to act honestly and use reasonable diligence, as statutorily provided for in the Companies Act,39 which mirrors fiduciary duties imposed on directors by common law.

It has been recognised for some time under Singaporean law that where the company is insolvent or near insolvency, directors must additionally take into account the interests of the company’s creditors to ensure the company’s assets are not dissipated.40 As to what constitutes ‘nearing insolvency’, the courts have steered clear of applying any bright-line test, preferring instead a broad approach – as long as there are reasons to be concerned that the creditors’ interests are or will be at risk, directors ought to have due regard to their interests.41

In addition to the above, personal and criminal liability may potentially be imposed on directors under the Companies Act. A director who is knowingly a party to the company contracting a debt of which there was no reasonable or probable ground of expectation that the company would be able to pay off could face civil and criminal liability for insolvent

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33 Sections 227X(b) and 227T(1) of the Companies Act.
34 Section 131(3)(g) of the Companies Act.
35 Section 258 of the Companies Act.
36 Section 262(3) of the Companies Act.
37 Section 328 of the Companies Act.
38 Pars Ram Brothers (Pte) Ltd (in creditors’ voluntary liquidation) v. Australian & New Zealand Banking Group Ltd [2017] SGHC 38 at [14]-[16].
39 Section 157(1) of the Companies Act.
trading.\textsuperscript{42} Additionally, if the business is found to have been carried on with the intent to defraud the company’s creditors, the director could face civil and criminal liability for fraudulent trading.\textsuperscript{43}

Further, while the statutory avoidance provisions discussed in Section II(ii), supra, are not per se expressed to impose duties on directors, the court has recently confirmed that a director would likely be liable for a breach of fiduciary duties where there has been an adverse finding under the statutory avoidance.\textsuperscript{44} Further, the court has confirmed that the mere fact that the relevant time limit for the statutory avoidance provision has passed will not preclude liability for breach of common law fiduciary duties.\textsuperscript{45}

\section*{III RECENT LEGAL DEVELOPMENTS}

\subsection*{Amendments to the Companies Act}

As mentioned earlier, the 2017 Amendments saw significant changes to Singapore’s restructuring and insolvency legal framework with the introduction of amendments to the Companies Act through the Companies (Amendment) Bill 2017 (the Bill), followed by the insolvency-related amendments coming into effect on 23 May 2017 (the Amended Companies Act). These amendments, part of Singapore’s concerted push to be an international centre for debt restructuring, trace their origins to recommendations proposed by the Insolvency Law Review Committee (ILRC) formed in 2010 by the Ministry of Law to review Singapore’s corporate insolvency laws.

\textbf{Schemes of arrangement}

One of the key amendments supplementing the scheme of arrangement framework is the enhanced moratorium, previously recognised by the ILRC as a key shortcoming of the previous regime for schemes of arrangement.\textsuperscript{46} There are four broad enhancements: first, an interim 30-day moratorium now arises automatically upon a company making an application for a moratorium.\textsuperscript{47} Next, the moratorium now covers a wider scope, including restraining secured creditors from enforcing their security.\textsuperscript{48} Third, the court may now order for a moratorium to have in personam worldwide effect.\textsuperscript{49} Lastly, an application may be made to extend the moratorium to the company’s related companies.\textsuperscript{50}

Next, in view of concerns that a minority dissenting class of creditors can stymie an otherwise viable scheme of arrangement,\textsuperscript{51} the 2017 Amendments provide for cross-class

\begin{thebibliography}{99}
\bibitem{42} Sections 339(3) and 340(2) of the Companies Act.
\bibitem{43} Section 340 of the Companies Act.
\bibitem{44} Living the Link at [48]. See further at section III.
\bibitem{45} Parakou Shipping Pte Ltd (in liq) v. Liu Cheng Chan [2017] SGHC 15 (Parakou) at [121]-[122].
\bibitem{46} ILRC Report at p.140.
\bibitem{47} Section 211B(8) of the Amended Companies Act.
\bibitem{48} Section 211B(1) of the Amended Companies Act.
\bibitem{49} Section 211B(5) of the Amended Companies Act.
\bibitem{50} Section 211C of the Amended Companies Act.
\bibitem{51} ILRC Report at p.154.
\end{thebibliography}
cramdowns, provided that the scheme does not discriminate unfairly between the classes of creditors and is fair and equitable (provided that the requisite majority is attained in respect of all the creditors as a whole). 52

Third, in recognition of the potential for significant time and costs savings, the court may now approve a pre-packaged scheme where it is satisfied that the requisite majority of creditors would have approved the scheme. 53 Thus, the process for scheme of arrangement may be fast-tracked.

Fourth, in a bid to facilitate the possibility of ailing companies obtaining fresh financing, the 2017 Amendments empower the court to confer various levels of ‘super priority’ for rescue financing in certain circumstances. 54 ‘Rescue financing’ is statutorily defined to mean financing which is necessary either for the survival of the company as a going concern, or to achieve a more advantageous realisation of the company’s assets than in a winding up. 55

**Judicial management**

The 2017 Amendments relating to ‘super priority’ in rescue financing in schemes of arrangements are mirrored in the judicial management regime. Further, in an effort to address observations that judicial management has historically been invoked at too late a stage for the intervention to result in successful rehabilitation of the company, 56 the threshold for a judicial management application to be made has been lowered from a company being ‘unable to pay its debts’ to being ‘likely to become unable to pay its debts’. More significantly, the amendments now allow foreign companies to avail themselves of the judicial management regime.

**Cross-border insolvency**

Prior to the 2017 Amendments, cross-border insolvency was principally governed by Sections 351 and 377 of the Companies Act and the common law. 57 The former gave Singaporean courts the power to wind up an ‘unregistered company’ (including a foreign company). The latter provided, *inter alia*, for liquidators appointed in a foreign company’s place of incorporation or origin to have the same powers and functions as a liquidator for Singapore. Following the 2017 Amendments, the UNCITRAL Model Law on Cross-Border Insolvency (the Model Law) has now been adopted in Singapore with certain modifications, and for the first time, Singapore has a clear legislative framework under which courts may recognise and assist any foreign restructuring or insolvency proceedings.

Additionally, the 2017 Amendments abolish the ring-fencing rule that previously required a Singaporean liquidator appointed over a foreign company to pay net amounts recovered in the liquidation process to the foreign liquidator appointed in the company’s place

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52 Section 211H of the Amended Companies Act.
54 Section 211E of the Amended Companies Act.
55 Section 211E(9) of the Amended Companies Act.
56 ILRC Report at p. 84.
57 On developments in the common law, see further at Section III(ii) of this chapter, supra.
of incorporation only after paying debts and satisfying any liabilities incurred in Singapore. The revised law, the ring-fencing rule applies only to ‘relevant companies’, defined to include, inter alia, banks, finance companies and insurers that are licensed.

The above amendments are subject to statutorily provided carve-outs. Thus, certain classes of companies, for example, financial institutions, are excluded from the scheme of arrangement, judicial management and Model Law provisions. Further, certain prescribed arrangements, including set-off or netting arrangements, are excluded from the newly minted provisions on moratoriums.

**ii Case law**

*Universalist trends in cross-border insolvency cases in line with the 2017 Amendments*

Even before the 2017 Amendments took effect, judicial decisions in Singapore in recent insolvency and restructuring matters had already begun to demonstrate a steady, but unmistakeable, trajectory away from traditional notions of territoriality in favour of a more universalist approach.

The case of *Beluga Chartering GmbH v. Beluga Projects (Singapore) Pte Ltd* [2014] 2 SLR 815, opened the doors for Singapore courts to recognise and render assistance to foreign insolvency proceedings. In *Re Opti-Medix Ltd (in liquidation)* [2016] 4 SLR 312 (*Re Opti-Medix*), bankruptcy trustees appointed in Japan over a company incorporated in the British Virgin Isles sought recognition of their appointment in Singapore. The court observed that a universalist approach (in which the court in one jurisdiction leads the administration of liquidation, with the other courts rendering assistance) was the most ‘conducive to the orderly conduct of business and resolution of business failures across jurisdictions’. The court rejected the notion that it should be constrained from developing the common law, and went on to accept that the ‘centre of main interests’ (COMI) test was a basis for recognising foreign insolvency proceedings at common law. Thus, the COMI test was, even before the Model Law took legislative effect (through the 2017 Amendments) in Singapore, already a part of Singapore law.

*Re Opti-Medix* was followed by *Re Taisoo Suk (as foreign representative of Hanjin Shipping Co Ltd)* [2016] 5 SLR 787, where Hanjin Shipping Co Ltd sought recognition of rehabilitation proceedings that had been commenced in the Republic of Korea and a moratorium over proceedings against it in Singapore. The court similarly observed that the benefits of a universalist approach was ‘to the ultimate overall benefit of all creditors’, thus avoiding a ‘free for all’ that would result from disparate proceedings. The court, therefore, ordered that the Korean proceedings be recognised, and ordered a moratorium over proceedings against the company in Singapore – a first instance of a Singaporean court invoking its inherent power to provide assistance in a cross-border restructuring.

In *Re Gulf Pacific Shipping Ltd (in creditors’ voluntary liquidation)* [2016] SGHC 287, foreign liquidators appointed in Hong Kong sought recognition of their office in Singapore. The court declined to follow the English position that no assistance may be provided to

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58 Section 377(3)(c) of the Companies Act.
59 Sections 377(3)(c) and s 377(14) Companies Act.
60 *Re Opti-Medix* at [17].
61 *Re Opti-Medix* at [21].
62 *Re Taisoo Suk (as foreign representative of Hanjin Shipping Co Ltd)* [2016] 5 SLR 787 at [16].
a foreign voluntary liquidation, and instead found that it had the power to recognise voluntary liquidation. In doing so, the court reiterated that ‘the foundational doctrine in the recognition of foreign insolvency proceedings is the promotion and facilitation of the orderly distribution of assets’.

In *Pacific Andes Resources Development Ltd [2016] SGHC 210 (Pacific Andes)*, the court accepted that it could exercise jurisdiction to restructure foreign loans, provided that sufficient nexus to assets within jurisdiction had been shown. Thus, a Singaporean court would be able to restructure loans extended or debts incurred offshore, and exercise in personam jurisdiction to restrain lenders or creditors for proceedings that are within the court’s jurisdiction. In effect, the court rejected the traditional common law rule that a discharge of debt is not effective unless in accordance with the law governing the debt. The court observed that this reformulation of the rule was an ‘important and timely step in the global insolvency landscape’, which would otherwise impede ‘good forum shopping’.

Prior to the enactment of the Model Law, however, the ability of Singapore courts to recognise foreign restructuring and insolvency proceedings and render assistance thereto was arguably limited by the lack of clear legislation. In *Pacific Andes*, the applicant companies had applied for a scheme of arrangement in Singapore and sought, *inter alia*, orders for a worldwide moratorium over proceedings commenced against them. With its powers circumscribed by the express words of statute, the court found that schemes of arrangement were inherently territorial in nature, and as a necessary implication, so were the moratoriums granted in conjunction with the scheme of arrangement. Therefore, the court held that it had no power to restrain foreign proceedings, or even to restrain creditors within its jurisdiction from commencing proceedings outside Singapore. Further, the court declined to exercise its inherent power to order an extra-territorial moratorium be put in place as this would be contrary to the principles of international comity.

The effect of the holding in *Pacific Andes* was that companies would, as a necessary step to facilitating effective restructuring, have to apply for recognition proceedings or commence parallel proceedings in a number of overseas jurisdictions to secure the necessary court protections. Illustrating the potentially unwieldy nature of such a process, three days after the release of the decision in *Pacific Andes*, the company announced that it was abandoning the Singaporean scheme in favour of US Chapter 11 proceedings, in order to seek the necessary protection for its assets.

With the coming into effect of the 2017 Amendments, the promise is that a situation like that in *Pacific Andes* might now be resolved differently. In particular, the 2017 Amendments now allow the court to order that a scheme moratorium have extraterritorial (albeit

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63 As was decided in *Singularis Holdings Ltd v. Pricewaterhouse Coopers (PC)* [2015] AC 1675.
64 *Re Gulf Pacific Shipping Ltd (in creditors’ voluntary liquidation)* [2016] SGHC 287 at [10].
65 *Pacific Andes* at [46].
66 As was decided in *Antony Gibbs & Sons v. La Societe Industrielle et Commerciale des Metaux* (1890) LR 25 QBD 399.
67 *Pacific Andes* at [51].
68 *Pacific Andes* at [17].
69 *Pacific Andes* at [17]-[19].
70 *Pacific Andes* at [27].
It can, therefore, be seen that the 2017 Amendments (many of which were modelled after their US Chapter 11 counterparts) seek to position Singapore on a par with other international centres for debt restructuring.

**Other significant developments in case law**

**Classification of scheme creditors**

Apart from cross-border issues, one significant development had to do with classification of creditors in schemes of arrangement. In *Re Conchubar Aromatics Ltd* [2017] 3 SLR 748 (*Re Conchubar*), the court expanded on the principles previously articulated in the landmark case of *The Royal Bank of Scotland NV v. TT International Ltd* [2012] 2 SLR 213. In the latter, the court had found that certain votes of creditors in a scheme of arrangement should be discounted. The court in *Re Conchubar* reaffirmed that the votes of related party creditors should be discounted in light of their ‘special interests’, though the court declined to define what ‘special interests’ entailed, going only so far as to say that it was ‘not a term of art and neither should it be construed narrowly’. As far as the court was concerned, the term was deemed sufficiently wide to include where the debtor and creditor shared a common sole shareholder and common director, and had acted as a single entity on some occasions, and also where the creditor had entered into a convertible loan agreement with the debtor under which the debt could be converted into shares constituting 99.82 per cent of the debtor’s share capital.

In *Re Conchabar*, the court also rejected the suggestion that a scheme proposal providing for contingencies or conditions would automatically render the scheme so uncertain that it should not be approved. Thus, provided the scheme sets out clearly what kind of results would follow on the occurrence of clearly defined events, the court held that there was no reason for it to refuse the scheme.

**Scheme moratoriums**

In relation to the scheme moratorium, the court in *Pacific Andes* considered the principles relating to the required standard when applying for a moratorium pursuant to Section 210(10) of the Companies Act before the application under Section 210(1) for a scheme of arrangement had been filed. It clarified that the particulars required to be provided in the former could be less detailed than that which would be required in the latter, provided that any lack of particulars was ‘explained away by cogent, credible and reasonable reasons’. Further, the fact that it would be unlikely that the scheme proposal presented for the purposes of the application for a scheme moratorium would attain the requisite majority approval was irrelevant – the court categorically rejected an approach that would amount to taking ‘straw poll’ at this preliminary stage. Recognising that it was liberalising the requirements for the grant of a moratorium, the court opined that such an approach was not justifiable merely on principle, but also ‘warranted in present day circumstances’.

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71 See above at section III(i).
72 *Re Conchubar* at [26].
73 *Re Conchabar* at [34]-[35].
74 *Re Conchabar* at [47].
75 *Pacific Andes* at [68].
76 *Pacific Andes* at [71].
77 *Pacific Andes* at [73].
Separately, in *BDG v. BDH* [2016] 5 SLR 977, the court clarified that in granting a stay of winding-up proceedings in favour of arbitration, the threshold was lower than usual – instead of showing a ‘triable issue’, it would be sufficient that the party seeking a stay show a ‘*prima facie* dispute’.78

**Test of insolvency**

The courts also fine-tuned the approach pertaining to when financial support (from related parties or otherwise), which features in many an insolvency case, may negate a finding that the company was insolvent. Thus, in *Living the Link*, the court declined to rely on past financial support extended by associate companies to the company to prove it was not insolvent, given that there was no obligation to provide such support.79 In *CCM Industrial Pte Ltd (in liquidation) v. Chan Pui Yee* [2016] SGHC 231, the court reiterated that financial support was ‘meaningless’ unless it was accompanied by an obligation to provide the support. Further, the court observed obiter that the effect of the financial support would depend on whether the support was given by way of equity injection. On a related note, the court in *Parakou Shipping Pte Ltd (in liquidation) v. Liu Cheng Chan* [2017] SGHC 15 (*Parakou*) acknowledged that while letters of support are relevant, the weight to be given to them would depend on the likelihood that they would be honoured. It would be an ‘exceptional case’ that a company that would, otherwise, have been cash-flow insolvent should be found to be cash-flow solvent merely on the basis of non-binding letters of support.80

**Removal of liquidators**

Finally, in *Petroships Investment Pte Ltd v. Wealthplus Pte Ltd (in members’ voluntary liquidation)* [2017] SGHC 122 (*Petroships*), the court considered how the legal test for the removal of liquidators in a solvent liquidation may differ from that in an insolvent liquidation. Thus, in a solvent liquidation, the court will ordinarily take into account the views of the members, and not the views of the creditors.81 Additionally, the majority’s view on any necessity for investigation is the starting point for the liquidator (though it is not the ending point).82 The court further observed (albeit obiter) that where a contributory applies to wind up a solvent company, it must meet a higher standard of proof and show that it has a ‘very strong case’ to succeed in winding up the company. Such ‘strong case’ would include suspicious circumstances or fraud.83

**IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES**

The beleaguered offshore and marine and oil and gas industries have been in the spotlight, with several high-profile casualties. On 27 July 2016, Swiber Holdings Limited (Swiber), a listed offshore services firm, filed for liquidation. Two days later, Swiber applied to court for judicial management instead. Technics Oil & Gas, an oil and gas services firm, was placed

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78 *BDG v. BDH* [2016] 5 SLR 977 at [20], [22].
79 *Living the Link* at [30].
80 *Parakou* at [84].
81 *Petroships* at [128].
82 *Petroships* at [140].
83 *Petroships* at [263].
into judicial management on 25 July 2016. Swissco Holdings Limited, a listed marine firm, was placed into judicial management on 21 April 2017. As at the time of writing, these three companies are still in judicial management. Singapore-listed offshore service provider Ezra Holdings Limited (Ezra) also filed for Chapter 11 protection in the US in March 2017.84

There is significant public interest in the outcome of the restructuring of the above companies, given the reported exposure of local banks to this sector.

V INTERNATIONAL

As discussed above at Section III(i), Singapore has recently adopted the Model Law. In addition, the Guidelines for Communication and Cooperation between Courts in Cross-Border Insolvency Matters (the Guidelines), first proposed at the inaugural Judicial Insolvency Network (JIN) in October 2016, were adopted by Delaware and Singapore courts on 1 February 2017. The Guidelines, intended to “improve in the interests of all stakeholders the efficiency and effectiveness of cross-border proceedings”,85 mark the first time that a formal framework has been adopted and implemented by courts in coordination and cooperation in relation to cross-border insolvency. Thus, for example, the Guidelines provide for communications between courts to take place via telephone or video conference call or any other electronic means.86 As at the date of writing, jurisdictions that have implemented the Guidelines include England and Wales, the Southern District of New York, Delaware, the British Virgin Islands, Bermuda and Singapore.

VI FUTURE DEVELOPMENTS

The 2017 Amendments are in line with Singapore's stated efforts to position itself as an international debt restructuring hub. The government’s efforts in this area have received some recognition to date, with Singapore being named ‘most improved jurisdiction’ by Global Restructuring Review in June 2017.87 The universalist trend that has been observed in leading Singaporean court decisions in cross-border matters is expected to continue, even as court-led initiatives such as the JIN further enhance the potential for cross-border cooperation in insolvency matters.

85 The Guidelines at introductory paragraph A.
86 Guidelines 7 and 8 of the Guidelines.
87 The Straits Times ‘Republic lauded for efforts to help troubled firms’ (23 June 2017)
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

South Africa is the 30th ranked economy in the world. South Africa has been termed one of the 'fragile five', along with Brazil, India, Indonesia and Turkey, all of which are countries with large current account deficits, weakening currencies, plummeting stock markets and surging bond yields in the latter part of 2015 and early 2016.

At the end of March 2017, the President of South Africa reshuffled his cabinet and removed the Minister of Finance, Mr Pravin Gordhan, whom he appointed in December 2015 when he removed the then Minister of Finance. These political events led to credit rating agencies downgrading South Africa to what is referred to as junk status. The credit rating agencies attributed the downgrade to political instability. Fitch Ratings indicates that South Africa's ratings are 'weighed down by low trend GDP growth, sizeable contingent liabilities and deteriorating governance. Positively, they are supported by deep local capital markets, a favourable government debt structure and a track record of fairly prudent fiscal and monetary policy.' South Africa, however, remains one of the three largest economies in Africa.

South Africa has seen regular filings for business rescue in terms of Chapter 6 of the Companies Act 71 of 2008 (the Act) since the Act came into law in South Africa on 1 May 2011. According to the website of the Company and Intellectual Property Commission (CIPC), as at 31 December 2016, for the period 2016–2017, a total of 296 business rescue proceedings were commenced, of which six filings were invalid and during which period 60 business rescue proceedings ended and 16 were placed in formal liquidation. This number was 38.5 per cent down on the 481 filings for the period 2015–2016. From when the Act came into law on 1 May 2011 to 31 December 2015, some 2,422 companies and close corporations filed for business rescue.

According to the most recent statistical release by Statistics South Africa, on 22 May 2017, the number of liquidations in South Africa increased by 6.4 per cent in the first four months of 2016, compared with the first four months of 2016.
Informal restructuring occurs, and a large informal restructuring of Edcon,\textsuperscript{7} South Africa’s largest non-food retailer, which has almost double the market share in the clothing and footwear market of that of its nearest competitor, was completed in February 2017. Edcon’s debt restructuring was finalised with new ownership and gross third party debt in the operating group significantly reduced to 6.2 billion rand as at 25 March 2017.\textsuperscript{8}

Formal restructuring takes place under Chapter 6 of the Act, which provides for the entering into of compromises or schemes of arrangements between companies and its creditors\textsuperscript{9} or business rescue.\textsuperscript{10}

\section*{II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK}

\subsection*{i Restructuring other than under business rescue\textsuperscript{11}}

Before 2011, under the Companies Act\textsuperscript{12} (the 1973 Companies Act) the only restructuring ‘tool’ available was to place a company under provisional liquidation and to then propose a scheme of arrangement or compromise in terms of the 1973 Companies Act.

Since 2011, over and above the voluntary commencement of business rescue proceedings by board resolution,\textsuperscript{13} a company or close corporation may also propose a compromise or an arrangement to its creditors.\textsuperscript{14}

This section of the Act\textsuperscript{15} is titled ‘Compromise with creditors’, but also provides for an ‘arrangement or a compromise’ of its financial obligations to be proposed.\textsuperscript{16} Neither term is defined in the Act, but its meaning should be determined with reference to the equivalent procedure used under the prior company’s legislation. The aim of this section is, therefore, to also achieve the goals of ‘business rescue’ as defined, in furtherance of the Act’s purpose of encouraging successful rescue of companies outside formal business rescue and also under winding up.

\subsection*{ii The meaning of ‘business rescue’}

The term ‘business rescue’\textsuperscript{17} describes the purpose and aims of the corporate rescue procedure included under Chapter 6 of the Act, and is also used as a noun to describe the proceedings encapsulated in Chapter 6 as a whole.\textsuperscript{18} It means proceedings that ‘facilitate the rehabilitation’ of a company that is financially distressed, where there appears to be a reasonable prospect

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\textsuperscript{7} Accessible at: www.edcon.co.za/news_article.php?articleID=3240 (accessed 12 June 2016).
\textsuperscript{9} In terms of Section 155 of the Act.
\textsuperscript{10} In terms of Sections 128–154 of Chapter 6 of the Act.
\textsuperscript{11} This is largely based on an article co-authored by the author hereof: Klopper & Bradstreet ‘Averting Liquidations with Business Rescue: Does a Section 155 Compromise Place the Bar to High?’ 2014 25.3 Stellenbosch Law Review 549.
\textsuperscript{12} Act 61 of 1973.
\textsuperscript{13} Section 129 of the Act.
\textsuperscript{14} Section 155 of the Act.
\textsuperscript{15} Section 155 of the Act.
\textsuperscript{16} This arrangement between a company and its creditors must be distinguished from the ‘scheme of arrangement’ between a company and holders of its securities under Section 114 of the Act.
\textsuperscript{17} Section 128(1)(b) of the Act.
\textsuperscript{18} Delport PA and Vorster Q, Henochsberg, on the Companies Act 71 of 2008, page 446.
\end{flushleft}
of rescuing the company, or that result in a better return for the company’s creditors or shareholders than would result from immediate liquidation of the company. It was described in one of the first judgments relating to the business rescue provisions in the Act that these provisions ‘reflect a legislative preference for proceedings aimed at the restoration of viable companies rather than their destruction.’

The term ‘financially distressed’ means that when it ‘appears to be reasonably unlikely that the company will be able to pay all of its debts as they become due and payable within the immediately ensuing six months’, or ‘appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months.’

The objective of the business rescue process is achieved by:

- the development and implementation, if approved, of a plan to rescue the company by restructuring its affairs, business, property, debt and other liabilities, and equity in a manner that maximizes the likelihood of the company continuing in existence on a solvent basis or, if it is not possible for the company to so continue in existence, results in a better return for the company’s creditors or shareholders than would result from the immediate liquidation of the company.

Business rescue proceedings can be initiated on a voluntary basis by way of a resolution of the board of directors of the company to begin business rescue proceedings, and also on a compulsory basis by way of an application to court by an ‘affected person’ – a shareholder, creditor, the registered trade union representing employees or any of the employees of the company.

Two requirements must be satisfied for the board of directors to voluntarily commence business rescue proceedings, namely, that the company is financially distressed and that there appears to be a reasonable prospect of rescuing the company. The board of directors of a company may accordingly commence business rescue proceedings by passing a board of directors’ resolution supported by a majority vote. When passing a resolution the directors must act in good faith. Bad faith will be demonstrated when the intention of the directors in passing the resolution is an abuse.

Compulsory proceedings will commence if the court determines that there is a reasonable prospect of rescuing the business. In the first reported case for the compulsory business rescue of a company heard in 2011, the court dismissed the application with costs, on the basis that the application was an abuse of process by the applicant.

In January 2013, the High Court converted formal liquidation proceedings to business rescue proceedings by giving effect to the legislature’s preference to ‘come to the aid of ailing companies’ and found that there was reasonable prospect of rescuing the business of the company.

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19 Cape Point Vineyards (Pty) Ltd v Pinnacle Point Group Ltd and Another 2011 (5) SA 600 (WCC) per Rodgers AJ.
20 Section 128(1) f) of the Act.
21 Section 128(1) b) of the Act.
22 As envisaged in Section 129(1) of the Act.
23 Griessel and Another v Lizemore and Others 2016 (6) SA 236 (GJ) Spilg J at page 258.
24 Griessel and Another v Lizemore and Others 2016 (6) SA 236 (GJ) Spilg J at page 259.
25 Swart v. Beagles Run Investments 25 (Pty) Ltd 2011 (5) SA 422 (GNP), Makgoba J.
26 Cardinet (Pty) Ltd v Wedgewood Golf and Country Estate (Pty) Ltd (in liquidation) and Others 19599/2012 30 January 2013 (WCC); Delport PA et al Henochsberg on the Companies Act 71 of 2008.
The Act sets out certain procedural requirements that the company must comply with to ensure that the business rescue proceedings remain in place. After the board of directors’ meeting, the resolution must be filed with CPIC, and only once the resolution has been filed do the business rescue proceedings commence.

Within five business days thereafter, the company must publish a notice of the resolution to every affected person and appoint a duly licensed and qualified business rescue practitioner who has accepted the appointment in writing. Notice of this appointment must be filed within two business days. The notice to affected persons must include a sworn statement of the facts relevant to the grounds on which the resolution was founded.

Initially, it appeared that strict compliance with the aforesaid procedures was peremptory and rendered the board of directors’ resolution to commence business rescue proceedings a nullity in the event of a failure to comply. This approach was adopted by the courts in a number of early cases, and also in the Panamo Properties case in 2014.

The Supreme Court of Appeal (SCA), however, set the Panamo Properties judgment aside in 2015 on appeal and held that non-compliance with procedural requirements did not automatically terminate business rescue proceedings.

Only if a court set aside the resolution would the business rescue terminate. The SCA referred to the aim to ‘provide for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders’ as contained in the Act and, inter alia, the ‘leading to a better result for the company’s creditors and shareholders’, but then stated that:

> these commendable goals are unfortunately being hampered because the statutory provisions governing business rescue are not always clearly drafted. Consequently, they have given rise to confusion as to their meaning and provided ample scope for litigious parties to exploit inconsistencies and advance technical arguments aimed at stultifying the business rescue process or securing advantages not contemplated by its broad purpose. This is such a case.

Once the board has resolved to commence business rescue proceedings, the company may not adopt a resolution to put the company under liquidation, unless the resolution has lapsed or the business rescue proceedings have ended.

27 These requirements are set out in Sections 129(3) and (4) of the Act.
28 Section 129(3) of the Act.
33 Section 129(6) of the Act.
iii What avenues are open to challenge business rescue proceedings?

To prevent abuse of voluntary business rescue proceedings, the Act provides that until the formal adoption of a business rescue plan, an affected person may, under the appropriate circumstances, apply to court for an order to set aside the board of directors’ resolution to commence business rescue proceedings. The grounds for this is that there is no reasonable basis for believing that the company is financially distressed, there is no reasonable prospect for rescuing the company, or the company has failed to satisfy the procedural requirements specified in the Act.

It was mentioned in a number of judgments that there is always the possibility that business rescue applications to court might be used by debtors to avoid liquidation.

An affected person is also entitled to apply to a court for the setting aside of the appointment of the practitioner identified by the board on the grounds that he or she ‘is not independent of the company or its management’ or otherwise does not qualify for appointment.

It is to be noted that where an affected person successfully challenges the appointment of a practitioner, the court will have the right to appoint the substitute practitioner who satisfies the requirements (i.e., being licensed) recommended by, or acceptable to, the holders of the majority of the independent creditors’ voting interest who were represented in the hearing before the court.

It is, therefore, imperative to ensure that the person appointed as the practitioner is truly independent of the company or its management.

iv Duration of business rescue proceedings

It is clear that the legislature intended for business rescue proceedings to be a swift process, hence the provisions in the Act that a practitioner must be appointed within five business days of the company adopting and filing a resolution to voluntarily commence with business rescue proceedings, a plan must be published by the practitioner within 25 business days after the date on which he or she was appointed, and it is intended that proceedings must end within three months.

It has, however, become clear during the past six years since this legislation came into law that the time period for the publication of the plan and the three months’ duration of business rescue proceedings is almost always unattainable and that an extension of this time period is almost always sought.

Fortunately, the legislature provides for mechanisms to procure such extensions, and if these are not granted by creditors, it provides for the option of court intervention.

36 Investec Bank Ltd v. Bruyns 2012 (5) SA 430 (WCC); Blue Star Holdings (Pty) Ltd v. West Coast Oyster Growers CC 2013 (6) SA 540 (WCC) and Standard Bank of South Africa Ltd v. Gas 2 Liquids (Pty) Ltd 2017 (2) SA 56 (GJ).
37 Section 138 of the Act.
38 Section 132 of the Act.
39 Section 129(3) of the Act.
40 Section 150(5) of the Act.
41 Section 132(3) of the Act.
v Stay of legal proceedings/moratorium

The ability to stay legal proceedings against the entity while exploring restructuring options is vital for a successful business rescue regime. The Act makes provision for a general moratorium on legal proceedings, including any enforcement, against the company or in relation to any property belonging to the company, or lawfully in its possession, while the company is subject to business rescue proceedings. This has not been without legal challenges, and in this regard the courts have had differing views as to what ‘legal proceedings’ are in certain instances and whether ‘arbitration’ or labour law issues are included. The matter was settled in the SCA where it was held that on the basis that the phrase ‘legal proceeding’ may, depending on the context within which it is used, be interpreted restrictively, to mean court proceedings, or more broadly, to include proceedings before other tribunals, including arbitral tribunals.

The aim of this moratorium is to provide a company with breathing space pending a restructuring of its affairs. It was, however, held in the SCA that where a right to cancel an agreement had accrued prior to the commencement of proceedings that the subsequent cancellation is not ‘enforcement action’.

The SCA held that if cancellation is ‘enforcement action’, such steps would change the basic principles of the Law of Contracts, which provides for a unilateral act of cancellation in the case of a breach of contract.

It was held that the moratorium did not apply to proceedings for the ejectment of a company in business rescue where the lease regulating rights of occupation had been validly cancelled and the company had failed to vacate and was, thus, not in lawful possession of the property.

The Act provides that during business rescue proceedings no legal proceedings (including enforcement action) against a company may be ‘commenced or proceeded with’ in any forum, except with the written consent of the business rescue practitioner or with the leave of the court, in accordance with such terms as the court may deem ‘suitable’.


42 Section 133 of the Act.
43 Section 133 of the Act.
44 Van Zyl v. Euodia Trust [Page 478(5)] (Edms) Bpk 1983 (3) SA 394 (T) at 397 as to mean: ‘...the ordinary meaning of legal proceedings in the context of s 13 ['regsgeding' in the signed Afrikaans version] is a law suit or 'hofsaak', a definition accepted in Lister Garment Corporation (Pty) Ltd v. Wallace NO 1992 (2) SA 722 (D) at 723; The test in the Van Zyl case supra was accepted in Chetty t/a Nationwide Electrical v. Hart NO and Another (12559/2012) [2014] ZAKZDHC 9 (25 March 2014).
45 The Chetty (a quo) case, supra, was reversed on appeal in Chetty t/a Nationwide Electrical v. Hart and Another NNO 2015 (6) SA 424 (SCA).
47 Cloete Murray and Another NNO v. FirstRand Bank Ltd t/a Wesbank 2015 (3) SA 438 (SCA).
48 Kythera Court v. Le Rendez-Vous Café CC 2016 (6) SA 63 (GJ).
49 Section 133(1)(a) of the Act.
50 Section 133(1)(b) of the Act.
In this judgment, the court referred to the various conflicting judgments on the issue and the opposite views that have been expressed as to whether the provisions of the Act require a separate prior application to be made for leave to commence or proceed with legal proceedings, or whether such leave may be sought in one and the same matter.

In recent judgment the court held that if ‘the legislature had intended to limit the grant of leave to ‘exceptional circumstances’, that test would have been expressly stated’. The court then held that it is ‘given wide powers not only to grant leave, but also to determine the terms on which such leave is granted.’

**vi Property interests**

A company in business rescue may dispose of property in the ordinary course of business and on a *bona fide* transaction at arm’s length for fair value, approved in advance and in writing by the practitioner.

Secured creditors are protected as, if the company wishes to dispose of any property over which another person has any security or title interest, the company must obtain the prior consent of the secured creditor. This applies where the proceeds of the realisation of the asset will not be sufficient to pay the secured creditor in full. If the proceeds of the disposal will realise more than the value of the amount outstanding to the secured creditor and if the secured creditor’s debt will be fully discharged, such consent is not necessary.

**vii Post-commencement finance**

One of the cornerstones of a successful rescue or restructuring regime is the ability of the entity to procure new money for purposes of funding ongoing operations. Akin to debtor-in-possession (DIP) finance under Chapter 11 in the USA, the Act provides for the procurement of the funding on the basis that such a creditor would become a ‘super-preferent’ creditor subsequent to the proceedings.

This finance ranks ahead of pre-commencement claims. The ability to obtain such finance is deemed to be the biggest obstacle in procuring the successful restructuring of any business.

**viii Employees and contracts**

The sanctity of employees’ contracts and the protection of their position is an important feature of business rescue. The Act provides that, despite a provision of any agreement to the contrary, during business rescue proceedings of a company, the employees continue to be employed by the company under the same terms and conditions that applied prior to

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53 *Safari Thatching Lowveld CC v. Misty Mountain Trading 2 (Pty) Ltd* 2016 (3) SA 209 (GP).

54 *Arendse and Others v. Van der Merwe and Another NNO* 2016 (6) SA 56 (GJ).

55 *As was held in Redpath Mining SA (Pty) Ltd v. Marsden NO and Others.*

56 Section 134 of the Act.

57 Section 135 of the Act.

58 Section 136 of the Act.
the company being placed under business rescue. Where changes to the workforce occur in the ordinary course of attrition and where employees of the company, in accordance with applicable employment related legislation, agree different terms and conditions, such agreements would be enforceable.

An important ‘tool’ at the disposal of a practitioner is to, upon being appointed, suspend the company’s obligations in terms of certain contracts. This has become an important way to control the company’s cash flow, especially under retail scenarios where rentals are payable.

In a specific case, the successful restructuring of a retailer’s affairs was procured as a consequence of suspending obligations under lease agreements over the lucrative festive season that enabled the company to be provided with the necessary breathing space to restructure its affairs.

ix  Effect on shareholders and directors\(^{59}\)

Directors of a company are not removed from office during business rescue proceedings. They continue to exercise their functions and remain in a fiduciary position towards the company, subject to the authority of the practitioner.

The practitioner has certain duties and powers,\(^ {60}\) the most important of which is that he or she has full management control of the company in substitution for its board and preexisting management. He or she may delegate any power or function to a person who was part of the board or preexisting management of the company and may also remove from office any person who forms part of the preexisting management of the company or appoint a person as part of the management of a company, whether it is to fill a vacancy or not.\(^ {61}\)

x  Qualification and removal of practitioners\(^ {62}\)

Practitioners may only be appointed if they are members of a legal, accounting or business management profession accredited by CIPC. However, no such professional body has as yet been accredited. Between 2011 and 2015 practitioners were licensed on an *ad hoc* basis, in that they were required to apply for a licence in respect of each and every new matter where they were appointed as the practitioner. Since 2015, conditional licences have been issued to practitioners on the basis that they need not apply for *ad hoc* licences any longer. The process of determining the professional bodies to be accredited is ongoing.

Practitioners may be removed by a court and upon a number of grounds, such as incompetence, failure to perform the duties, failure to exercise proper degree of care, engaging in illegal acts, no longer satisfying the requirements set out in the act, a conflict of interest, a lack of independence or being incapacitated.

xi  Investigation

The practitioner must investigate\(^ {63}\) the company’s affairs, business, property and financial situation to assess whether there is any reasonable prospect of the company being rescued,

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59 Section 137 of the Act.
60 Section 140 of the Act.
61 Subject to Section 140(2) of the Act.
62 Sections 138 and 139 of the Act.
63 Section 141 of the Act.
as contemplated in the Act. The practitioner has an obligation to report any contravention of any law, reckless trading, fraud, misappropriation of assets or any criminal activity, and is further obliged to rectify any contravention, including recovering misappropriated assets.

The Act does not, however, equip the practitioner with the necessary powers to conduct formal enquiries or investigations. It is, therefore, questionable as to how the practitioner will be able to force recalcitrant parties to assist him or her with his or her investigations into the affairs of a company. This issue is yet to be determined by our courts.

The Act specifically requires directors to cooperate with the practitioner, but it is as yet uncertain as to how the practitioner may enforce this. The practitioner may remove a director by way of an order of court.

xii Participation by creditors and holders of the company’s securities
Creditors are entitled to be kept fully informed about all court proceedings, decisions, meetings or other relevant events, and may participate in any court proceedings. Although they are entitled to form a creditors’ committee, such a committee does not have the powers that one would expect. The committee may consult with the practitioner about any matter relating to the proceedings, but may not direct or instruct the practitioner.

The Act requires that, for purposes of developing a plan, the practitioner should consult with creditors, other affected persons and management of the company in the process of preparing a plan.

xiii The business rescue plan
The ultimate aim of the practitioner must be to develop and publish a plan for consideration by creditors and affected persons, if applicable.

The practitioner must publish his or her plan within 25 days of his or her appointment, or such longer period as may be allowed by the holders of the majority of the creditors’ voting interests. The plan must comply with the Act and must contain at least the following:

a) a list of the company’s assets;
b) a list of the creditors of the company;
c) the probable dividend that would be received by creditors in a liquidation;
d) a list of the company’s shareholders;
e) a copy of the written agreement, concerning the practitioner’s remuneration; and
f) a statement of whether the plan includes proposals informally made by creditors.

The plan must, furthermore, contain details of the proposals, assumptions made and conditions contained in the plan.

Save for the compliance with certain basic information, plans adopted in business rescue matters to date contain a wide variety of ‘techniques or methods’ available to restructuring professionals worldwide and that are also often informal methods, such as, inter alia:
a) sale of the business;
b) conversion of debt to equity;
c) repayment of debt over a fixed term;

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64 In terms of Section 145 of the Act.
65 Section 149 of the Act.
66 Section 150(1) of the Act.
67 Section 150 of the Act.
d proposal of a scheme of arrangement between the company and its creditors;
e a compromise between the company and its creditors; and
f an informal winding down of the company’s affairs that entails the sale of assets and the pro rata distribution of the proceeds to creditors.

Over and above basic information as required in terms of the Act, the plan may contain whatever the practitioner deems appropriate.

There are further requirements, such as to provide a projected balance sheet and income statement for the company for the ensuing three years, together with a statement of the conditions that must be satisfied for the plan to come into operation and be fully implemented.

In summary, plans may contain a myriad of proposals and the extent and nature of the proposal to creditors is not limited in any manner.

xiv Meeting to determine the future of the company

The practitioner is required to convene a meeting of creditors who have a voting interest to consider the published plan, within 10 days (with a minimum of five days) from the date of publication of the plan.

The plan will be approved on a preliminary basis if approved by 75 per cent of the creditors’ voting interest (i.e., the face value of their claims) present and voting at the meeting.

Once that threshold has been obtained, more than 50 per cent of independent creditors (i.e., creditors that do not have a relation to the company, such as being connected to a shareholder or director) must also vote for the adoption of the plan.

Once it has been adopted, the plan becomes binding on the company, its creditors and the shareholders. Dissenting creditors become bound by the plan. When the plan is substantially implemented, the practitioner must file a notice of the substantial implementation thereof, which then brings the proceedings to an end.

If the plan proposes to alter the rights of shareholders, a meeting of the shareholders must be convened to vote on the approval of the plan. If a simple majority of the said shareholders approve the plan, it will be regarded as having been adopted. If they oppose it, the plan is regarded as having been rejected.

xv Failure to adopt a business rescue plan

The Act provides that:

any affected person, or combination of affected persons may make a binding offer to purchase the voting interest of one or more creditors who opposed the adoption of a business rescue plan, at a value independently and expertly determined, on the request of the practitioner, to be a fair and reasonable estimate of the return to to that person, all those persons, if the company were to be liquidated.68

Why did the legislature include this provision in the Act? It can only be to force recalcitrant creditors, who have inappropriately voted against a reasonable proposal that places them in a better position than under liquidation circumstances, to ‘sell’ their voting interest or claim to other affected persons at the determined liquidation value of such a claim.

68 Section 153 (1)(b)(ii) of the Act.
Our courts have, in a number of judgments, expressed differing views to what the SCA held in 2015 in the *Kariba* judgment\(^9\) – that the meaning of ‘offer’ is that only an acceptance of an offer creates a right and obligations. It held that a contract can only come into existence if there was an agreed or readily ascertainable ‘price’ at the time that the offer was made.

The *Kariba* judgment does not necessarily affect the ability of affected persons to purchase the voting interest of a dissenting creditor in future, as this judgment was based on the actual facts pertaining to this case.

The first step in this process is for the practitioner to obtain a proper independent and expert valuation of the underlying assets forming the subject matter of the proceeds likely to accrue to creditors upon liquidation. The practitioner in the *Kariba* matter relied on his own valuation and not an independent professional expert valuation. Furthermore, in *Kariba* the affected persons did not demonstrate that they had the financial means and ability to make an immediate payment in respect of the amount offered. Their ‘offer’ was not accompanied by the demonstration of immediate funding being available to make payment in respect of the offer. The SCA criticised the practitioner in the *Kariba* matter, who appeared not to have provided sufficient financial detail in his plan to enable a valuation of the liquidation value of the bank’s voting interest to be ascertained.

What would, therefore, be required in future, is for the practitioner to provide a detailed determination duly executed by an expert, as set out in the determination. The offer in the *Kariba* matter did not present the creditor with an opportunity to, in the face of an expertly determined valuation of its voting interest and likely liquidation outcome, consider the offer in a business-like manner. The criticism levelled at the practitioner in the *Kariba* judgment and the successful appeal related to an ill-conceived ‘offer’ without any amount attributed to the ‘offer’. What is provided in the Act\(^7\) is that the holder of a voting interest may apply to a court to ‘review, re-appraise and re-value a determination by an independent expert’.

The legislature provided for this remedy to unlock a potential deadlock. If an offer has to be accepted before a legally enforceable contract to purchase a voting interest can come into existence, then, it can be asked, why would it be necessary to approach the court\(^7\) if consensus is necessary and an agreement has to come into existence on every occasion? The intention of this legislation is surely that an ‘unhappy’ holder of a voting interest who received and was bound by a properly determined ‘binding offer’ has only one remedy and option, and that is to approach a court to ‘review, re-appraise and re-value a determination by an independent expert’.

Upon a business rescue plan being rejected the Act entitles the practitioner to advise the meeting that the company will apply to a court to set aside the result of the vote by the holders of voting interests or shareholders, as the case may be, on the grounds that the vote against was inappropriate.\(^7\)

Likewise, an affected person present at a meeting to apply to court to set aside the vote by a particular a creditor or creditors holding a voting interest who voted against the adoption of a business rescue plan on the grounds that the vote was inappropriate.\(^7\)

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\(^7\) Section 153 (6) of the Act.

\(^1\) As is provided for in terms of Section 153(6) of the Act.

\(^2\) Section 153 (1) (a) (ii) of the Act.

\(^3\) Section 153 (1) (b) (i) (bb) of the Act.
Upon an application in terms of the Act ‘a court may order that the vote on a business rescue plan be set aside if the court is satisfied that it is reasonable and just to do so.’\textsuperscript{74}

In a judgment\textsuperscript{75} handed down in April 2017 the SCA set aside a vote against a business rescue plan by a financial institution holding 29.8 per cent of the voting interest and where the vote for the adoption of the business plan by other creditors was 70.2 per cent as opposed to the required statutory majority of 75 per cent.

The SCA held that is not necessary to reconvene the meeting of creditors once a court ordered that the vote was inappropriate as the Act does not envisage that. When the vote is set aside by the court, it follows by operation of law that the business rescue plan would be considered to have been adopted without any further voting.

**Informal methods to restructure companies in financial distress**

Informal workouts are often initiated by the banking sector and conducted with banking officials serving on credit committees, which then, jointly with the distressed company’s management or board of directors, embark upon a reorganisation of the company’s affairs, with a view to turning its operations around.

Instances of pre-packs in the context of South African law have been known. The company in distress and its creditors would agree to the terms of an arrangement akin to the business rescue plan agreed, and would then formally file for business rescue on a voluntary basis. The agreed pre-packed plan would then be formally published and adopted, whereafter the practitioner will be able to end business rescue proceedings swiftly.

Not much has been published about these processes.

**General framework of the laws of insolvency**\textsuperscript{76}

The law regulating insolvency is substantially provided for in the Insolvency Act.\textsuperscript{77} The common law of insolvency, as contained in the Roman-Dutch sources, also applies insofar as it is not inconsistent with any legislation. The effect of insolvency is, however, not unified in a single piece of legislation. The Insolvency Act essentially governs the relationship between creditors and debtors in the insolvent estates of natural persons, trusts and partnerships. Insofar as legislation governing the insolvency of corporate entities such as companies and close corporations does not provide for a specific set of circumstances, the Insolvency Act still applies, as is explained below.

Companies are incorporated in terms of the Act, and close corporations are incorporated in terms of the Close Corporations Act.\textsuperscript{78} As mentioned above, the Act\textsuperscript{79} came into law on 1 May 2011. Although the previous Companies Act\textsuperscript{80} (the 1973 Companies Act) has been

\textsuperscript{74} Section 153 (7) of the Act.
\textsuperscript{75} FirstRand Bank Limited v KJ Foods CC (In business rescue) (734/2015) [2015] ZASCA 50 (20 April 2017).
See also Collard v Jatara Connect (Pty) Ltd (23510/2016) [2017] WCC (14 March 2017) where a vote against business rescue plan for ulterior purposes was set aside by the court.
\textsuperscript{77} Act 24 of 1936.
\textsuperscript{78} Act 69 of 1984.
\textsuperscript{79} Act 71 of 2008.
\textsuperscript{80} Act 61 of 1973.
repealed,\textsuperscript{81} the Act provides, in terms of a transitional arrangement, that Chapter 14 of the 1973 Companies Act continues to apply with respect to the winding-up and liquidation of companies.\textsuperscript{82}

In terms of the Act, the Close Corporations Act was amended, and close corporations that existed as at 1 May 2011 will remain in existence, but no new close corporations will be formed thereafter.

Upon the liquidation of a company, the provisions of the aforementioned Chapter 14 of the 1973 Companies Act apply. However, insofar as Chapter 14 of the 1973 Companies Act does not deal with a specific set of circumstances, the provisions of the Insolvency Act apply \textit{mutatis mutandis}.

Upon the liquidation of a close corporation, insofar as the Close Corporations Act does not provide for a specific set of circumstances, the provisions of Chapter 14 of the 1973 Companies Act may apply \textit{mutatis mutandis}, and insofar as the Chapter 14 of the 1973 Companies Act does not apply, the provisions of the Insolvency Act will apply.

The concursus creditorum is one of the key concepts of the South African laws of insolvency, in that it entails that the rights of creditors of a group are preferred to the rights of individual creditors. The concept of the concursus creditorum ensures that, upon the arrival of insolvency, the position of the insolvent natural person or entity (the insolvent) is crystallised and that once the ‘hand of the law’ is laid upon the affairs of the insolvent, that the rights of the general body of creditors have to be taken into consideration.\textsuperscript{83}

\textbf{xvii The taking and enforcement of security}\textsuperscript{84}

The law provides real security to be taken in the form of a mortgage, pledge, landlord’s hypothec, tacit hypothec, right of retention or lien. Registering mortgage bonds confers security over immovable property.

Insofar as moveable assets are concerned, security is taken by or conferred upon a creditor by entering into an agreement of pledge, a tacit hypothec, the exercising of a lien, entering into instalment sale agreements in terms of which reservation of title of moveable assets are retained, the registration of a general notarial bond over moveable assets and the registration of a special notarial bond.\textsuperscript{85}

Security is enforced by way of an order of court and execution by a recalcitrant creditor who is unwilling or neglected to make payment or under insolvency proceedings if the creditor is ‘unable’ to pay.\textsuperscript{86}

Under insolvency, such creditors will be defined as ‘secured creditors’, as opposed to ‘preferent’\textsuperscript{87} and unsecured (described as ‘concurrent’) creditors.

\textbf{xviii Duties of directors of companies in financial difficulties}

Directors of companies in financial distress should note that:

\begin{itemize}
  \item \textsuperscript{81} Section 224(1) of the Act.
  \item \textsuperscript{82} Schedule 5, Paragraph 9 of the Act.
  \item \textsuperscript{83} Walker v. Syfret NO 1911 AD 141.
  \item \textsuperscript{85} Security by means of Moveable Property Act 57 of 1993.
  \item \textsuperscript{86} Mostert H, Pope A: \textit{The principles of the law of property in South Africa}, page 295. See also, the definition of ‘security’ in Section 2 of the Insolvency Act 24 of 1936.
  \item \textsuperscript{87} See the definition of ‘preference’ in Section 2 of the Insolvency Act 24 of 1936.
\end{itemize}
If the board of a company has reasonable grounds to believe that the company is financially distressed, but the board has not adopted a resolution contemplated in this section, the board must deliver a written notice to each affected person, setting out the criteria referred to in Section 128 (1) (f) that are applicable to the company, and its reasons for not adopting a resolution contemplated in this section.88

Therefore, if the circumstances necessary for the commencement of business rescue exist and the board of directors do not adopt a resolution placing the company under business rescue, a failure to do so without notice to affected persons may have consequences for the company’s directors.89 The Act90 provides that: ‘any person who contravenes any provision of this Act is liable to any other person for any loss or damage suffered by that person as a result of that contravention.’

xix Clawback actions

The Insolvency Act provides for the setting aside of impeachable transactions91 by the insolvency practitioner appointed in the insolvent estate of a natural person or a corporate entity.

Dispositions without value92 made more than two years before the commencement of insolvency proceedings may be set aside under circumstances where the insolvency practitioner must prove that disposition of property was not made for value and it is proved that, immediately after the disposition was made, the liabilities of the insolvent exceeded his or her assets or, if it occurred within two years of the commencement and the person claiming under or benefited by the disposition is unable to prove that, immediately after the disposition was made, the assets of the insolvent exceeded his or her liabilities.

Every disposition of property93 made by a debtor not more than six months before the commencement of insolvency that has had the effect of preferring one creditor above another, may be set aside by the court if immediately after the making of such disposition the liabilities of the debtor exceeded the value of his or her assets, unless the person in whose favour the disposition was made proves that the disposition was made in the ordinary course of business and that it was not intended, thereby, to prefer one creditor above another.

Furthermore, if a debtor unduly prefers a creditor94 by disposing of property at a time when the debtor’s liabilities exceed his or her assets, and it is proved that it was done with the intention of preferring one of his or her creditors above another, and the debtor is, thereafter, declared insolvent, the court may set aside such a disposition.

If it is found that there were collusive dealings95 before the commencement of insolvency, a court may set aside such transaction entered into by the debtor, whereby the

88 Section 129(7) of the Act.
89 Section 22 of the Act.
90 Section 218(2) of the Act.
92 Section 26 of the Insolvency Act.
93 Section 29 of the Insolvency Act.
94 Section 30 of the Insolvency Act.
95 Section 33 of the Insolvency Act.
debtor, in collusion with another person, disposed of property belonging to him or her in a manner that had the effect of prejudicing his or her creditors or of preferring one of his or her creditors above another.

Any person who was a party to such collusive disposition shall be liable to make good any loss thereby caused to the insolvent entity in question and shall pay, by way of penalty, such sum as the court may adjudge, not exceeding the amount by which he or she would have benefited by such dealing if it had not been set aside; if this party is a creditor he or she shall also forfeit his or her claim against the entity.

III RECENT LEGAL DEVELOPMENTS

No significant legislative developments have taken place during the past year since the promulgation of the Companies Act in 2011.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

The mining and manufacturing sector would appear to be the most significant and active industry insofar as the filing for business rescue is concerned.

Some significant further significant retail filings took place involving, among others, the furniture, clothing and jewellery industries.

V INTERNATIONAL

South African companies are by and large isolated from international developments and the research conducted for this publication indicated that no significant developments or key cases under the EC Regulations or any other significant regulatory environment took place.

South Africa has adopted the UNCITRAL Model Law by way of enacting the Cross-Border Insolvency Act 42 of 2000. However, this has so far, some 16 years later, failed to come into effect. This Act adapts the UNCITRAL Model Law on Cross-Border Insolvency, adopted in Vienna on 30 May 1997.

The Cross-Border Insolvency Act will not take full effect, however, until the Minister of Justice has designated the foreign states in respect of which the Act will apply. South Africa is not a party to an appropriate international convention treaty on cross-border insolvency.

VI FUTURE DEVELOPMENTS

Prior to 2000, there have been regular workshops with a view to reforming the South African laws of insolvency, bearing in mind that the South African Insolvency Act dates back to 1936. In March 2003, the South African cabinet approved, in principle, ‘the insolvency and business recovery bill’ but nothing has transpired since. It would, therefore, appear that there is very little likelihood of the South African insolvency law being reformed in the near future.

96 Section 33(2) of the Insolvency Act.
97 Ellerines, Platinum Group and Galaxy Jewellers.
Chapter 25

SPAIN

Alberto Núñez-Lagos Burguera and Beatriz Albors Cano

I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

i Liquidity and state of financial markets

Monetary policies conducted by the European Central Bank have improved liquidity in the Spanish financial markets. This has resulted in financial entities progressively granting funds again. However, such liquidity has only reached Spanish-based international companies and listed or major companies. Small and medium companies (SMEs) are still finding it difficult to access funding.

The European financial crisis has directly affected the bailout of the savings banks, which has led to the creation of a bad bank (Sociedad de Gestión de Activos Procedentes de la Reestructuración) that, unlike in other jurisdictions, is privately controlled. The bad bank has enabled prices of assets (especially real estate assets) offered to the market to adjust at sufficiently attractive rates so as to encourage investment again. Foreign real-estate investment funds have played an important role in this process by investing in and recapitalising the Spanish economy. This policy has led to sustainable growth. The general consensus is that Spain is expected to grow 3 per cent this year. By contrast, other southern European countries continue to reject the amount of non-performing loans (NPL) and, thus, are not growing.

Furthermore, the single resolution mechanism (SRM) has lived up to expectations and has proven to help Banco Popular. This case is recognised as the first and only bail-in case in Europe. However, this should have been embraced by other countries in southern Europe (such as Italy with Banca Popolare di Vicenza and Veneto Banca).

ii Market trends in restructuring procedures and techniques employed during this period (formal or informal)

A ‘before and after’ line has been drawn recently in relation to restructuring tools and procedures to avoid what had been occurring in Spain (and elsewhere in Europe) ever since the Spanish Insolvency Act (SIA) entered into force. Specifically, that most of the SMEs that entered into insolvency proceedings ended up in liquidation.

Consequently, the SIA modified its basic structure to enhance the continuity of viable businesses. This change of structure has been evidenced by several amendments to the SIA that, among other things, enforce the restructuring of companies (by introducing the Spanish equivalent to the English scheme of arrangements) (see Section II.iii, infra) and free the insolvency proceedings from obstacles that were initially foreseen to protect creditors in

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Spain
general and secured ones in particular (e.g., the reduction of secured creditors voting power by introducing the value of the security rule). Thus, a highly effective and efficient regime is being shaped, turning Spain into an attractive and competitive market to restructure debt.

In practice, companies are now seeking to prevent insolvency proceedings by resorting to out-of-court restructuring methods – such as, refinancing agreements, Spanish schemes or out-of-court payment agreements. Moreover, companies are no longer turning to foreign jurisdictions (e.g., the United Kingdom) for restructuring purposes.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Introduction to the insolvency legal framework

The SIA foresees a single insolvency proceedings (concurso) for companies that are not able (or expect not to be able) to regularly pay their debts as they fall due. In this regard, the directors of a company or the debtor must file for insolvency within two months following the date on which they became aware or should have become aware of the insolvency situation.

Every insolvency proceedings begins with the ‘common phase’. In this phase, the judge appoints a receiver that will be in charge of determining the debtor’s estate and outstanding debts and overseeing the management of the debtor’s business. The receiver will issue a report analysing the causes of the insolvency, the company’s net worth and its accounting situation. The receiver’s report will also include an inventory of the debtor’s estate and a list of creditors.

Once this report has been filed with the court, the creditors or any interested party may challenge the inventory or the list of creditors. The common phase will not end until the court resolves these challenges, unless they represent less than 20 per cent of assets or claims. In such case, the court may decide to automatically proceed to next phase in order to reduce the length of the proceedings and preserve the value of the assets.

At this point, the proceedings may take two directions: (1) if the debtor’s business is considered viable, the composition agreement phase will be initiated for the debtor to reach an agreement with its creditors with a view to restructuring the business; and (2) if the debtor’s business is not viable, the liquidation phase will begin in order to wind up the company. Nevertheless, the debtor is entitled to request that liquidation begin at any point during the insolvency proceedings.

Summary insolvency proceedings may be applied in some cases, where: (1) the debtor has fewer than 50 creditors; (2) estimated liabilities do not exceed €50 million; or (3) if the debtor files an early composition agreement proposal (see Section II.ii Composition agreements, infra). The summary insolvency proceedings will also apply where the debtor has filed for insolvency requesting the opening of the liquidation phase with an agreed binding purchase offer for the business or where the debtor has ceased its activity and has no employees.

ii Formal methods to restructure companies in financial difficulties

Insolvent companies have the following mechanisms at their disposal to restructure their debts.
Composition agreements

An insolvent debtor may restructure the company’s debt by entering into composition agreements with its creditors. The SIA distinguishes between two types of composition agreements: (1) early composition agreement; and (2) ordinary composition agreement.

Composition agreements include debt release and deferrals. They may also establish reorganisation measures such as mergers, the sale of assets or business units as a going concern (with the same specialities as described in Section II.i.ii. The sale of the business during the insolvency proceedings: special reference to the prepackaged sales, infra), debt-for-equity swaps (with equity consent), conversion into subordinated loans or debt capitalisation. Other alternatives are also available. These measures cannot affect public creditors. Moreover, under no circumstance can composition agreements determine the global liquidation of a company. The proposal for a composition agreement shall include a viability plan and repayment schedule.

The court must verify if the composition agreement complies with all legal requirements. If this is the case, it will be voted by creditors (which are classed by the SIA into financial, trade, public and labour) and will be approved and imposed on the creditors of the class if a majority vote succeeds, at least among unsecured creditors. No cross-cramdown is possible. The composition agreement may also be imposed on privileged creditors (which include secured creditors) if qualified majorities are met. There is an specific voting rule established for syndicated creditors. It will be understood that the syndicate accepts the composition agreement if 75 per cent of the participants favour the proposal, unless a lower majority is provided in the syndicated agreement.

Under composition agreements, subordinated creditors do not have the right to vote and they are only paid after all privileged and ordinary creditors have been fully paid. If the composition agreement includes debt deferrals, those terms will be counted for subordinated creditors as from the expiry of the forbearance period of ordinary creditors.

Ordinary composition agreements

Ordinary composition agreement proposals may be made by the debtor or creditors representing at least 20 per cent of the debtor’s estate, once the common phase has ended and for up to 40 days before the creditor’s meeting.

The voting of the proposal may be carried out in writing, or at a creditor’s meeting arranged by the judge.

Early composition agreements

Only debtors are entitled to make early composition agreement proposals at an early stage of the insolvency proceedings and may do so at any time from filing for insolvency, subject to certain restrictions linked to the directors’ failure to comply with their management duties. Moreover, the debtor can only make an early composition agreement proposal with the backing of creditors representing at least 20 per cent of the overall amount of the claims included in the list of creditors (or 10 per cent if the proposal is made together with the petition for insolvency). However, even if approved, the early composition agreement would only be effective after the common phase.

Creditors may adhere to the early composition agreement once it has been verified by the court until the term to challenge the receiver’s inventory and list of creditors expires.
Sale of the business during the insolvency proceedings: special reference to pre-packaged sales

The debtor’s business, or a business unit, can be sold as a going concern at any time during the insolvency proceedings. Moreover, the SIA provides an specific type of accelerated pre-packaged sale when a debtor files for insolvency and simultaneously requests liquidation with an agreed binding purchase offer for the business with a third party. In such a case, the judge is obliged to open the liquidation phase following the summary insolvency proceeding (please refer to Section II.i, supra) but with some special features to enable a quick sale.

An important aspect of the sale of business units or pre-packaged sales is that the transferee automatically subrogates to the position of the debtor in all the agreements, licences and administrative authorisations provided that they are related to the debtor’s business or professional activity and, unless it expressly opposes to the subrogation.

The transferee is also exempted from assuming debts incurred by the debtor prior to the closing of the pre-packaged sale (even if they are classified as insolvency claims or post-insolvency claims) except for social security claims and, in certain circumstances, pending salaries.

When the pre-packaged sale is made up of secured assets and the transferee refuses to assume the security interest, the secured creditors will be repaid out of the price of the business unit in proportion to the value of the collateral and will have to cancel the security. If the price offered is lower that the value of the collateral, consent would be required by the secured creditors. Where there is more than one secured creditor, the SIA establishes that consent is given when the transfer is accepted by 75 per cent of the secured creditors of the same class with an individual right to enforce the claim.

iii Informal methods to restructure companies in financial difficulties

Ordinary out-of-court refinancing agreements

Under the SIA, there are two types of ordinary out-of-court refinancing agreements that may be immune to clawback if some requirements are met: (1) collective refinancing agreements; and (2) non-collective refinancing agreements.

Collective refinancing agreements

The debtor can enter into these agreements if:

\[a\] they entail at least a significant increase in the credit or an amendment or cancellation of the debtor’s obligations, either by extending their maturity or establishing other obligations in lieu;

\[b\] it has the backing of creditors (not only secured and ordinary creditors but also trade creditors) who have at least three-fifths of the claims against the debtor at the time the refinancing agreement is executed. If the refinancing agreement affects a group of companies, it must be backed by creditors holding at least three-fifths of the claims against each of the companies of the group and against the whole group of companies, excluding, in both cases, intra-group claims;

\[c\] the debtor’s auditor issues a certificate on the sufficiency of the liabilities required to execute the agreement; and

\[d\] the refinancing agreement and related documents are executed in a deed before a notary public.
Non-collective refinancing agreements

Immunity to clawback actions is also possible where the requirements described in II. 3. Collective refinancing agreements, supra are not met, but by means of a restructuring agreement: (1) the debtor’s asset-liability proportion is increased; (2) the current assets resulting from the refinancing are greater than the current liabilities; (3) the applicable interest rate does not exceed a certain percentage; and (4) the agreement is executed in a deed before a notary public, and sets out the reasons for the agreements.

Spanish schemes

One of the main novelties introduced by the recent amendments to the SIA is the ‘Spanish Scheme’. This special type of refinancing agreement, in addition to becoming immune to clawback actions, allows the cramdown of dissenting creditors (including secured creditors), provided that they hold financial liabilities.

The Spanish Scheme must be backed by a qualified majority of creditors (the required majority will depend on the restructuring measure to be imposed on dissenting creditors). In addition, the agreement must be executed in a deed before a notary public.

The claims owned by related parties and commercial creditors are not taken into account for the purpose of calculating majorities, even if they decide to voluntarily adhere to or are ultimately affected by the cramdown. Moreover, secured claims will be treated as unsecured for the proportion of the claim that exceeds the value of the security.

The agreement must be approved by the judge in order to cram down dissenting creditors. Non-participating or dissenting creditors may challenge the resolution approving the cramdown but based on limited grounds (e.g., disproportionate sacrifice, failure to meet the required percentages). Once the judge has accepted the Spanish Scheme, enforcement proceedings (also of security) may only be initiated (or, if applicable, seeking the debtor’s declaration of insolvency) if the court believes that the refinancing agreement has been breached.

Out-of-court payment agreements

Dissenting creditors (including secured ones) can also be crammed down through this out-of-court refinancing mechanism, but it only applies to individuals and small companies (i.e., companies with fewer than 50 creditors, estimated liabilities or estimated assets of €5 million or less).

Persons related to the debtor are those that the SIA considers not to be independent of the debtor. If the debtor is a natural person, related parties would refer to family members. If the debtor is a legal person, related parties would be, for example, companies of the same group and directors and shareholders that hold a certain percentage of the share capital. The claims held by persons that are related to the debtor are subordinated and are subject to certain restrictions (e.g., they will not have voting rights when reviewing a proposal of composition agreement and will only be paid once the privileged claims and the ordinary claims have been paid).
The taking and enforcement of security

Taking security

Under Spanish law, security over assets is created and perfected as a right in rem (i.e., enforceable against third parties) when a security agreement is executed and some formalities are met. This allows creditors to enforce their credit rights against those assets before other creditors.

In practice, real-estate mortgages are very commonly used to obtain security interest. The debtor creates a mortgage over one or several fixed assets that must be granted in a public deed and be registered. Possession does not need to be transferred. Mortgages can cover all ancillary assets (e.g., buildings and factories), construction improvements, indemnities, insurance proceeds and expropriation proceeds and must be executed in a deed before a notary public and registered with the land registry.

Chattel mortgages are another option. In this case, the debtor creates a mortgage over its title to certain types of moveable assets (e.g., business premises and industrial parts, machinery and industrial and intellectual property) which must be granted in a public deed and registered. Possession does not need to be transferred.

Another common type of security are pledges (with or without displacement of the possession of the pledged asset). By creating a pledge with displacement, the debtor delivers to the creditor a moveable asset (including security) or a credit right (e.g., accounts receivable) owned or held by the debtor. In this case, possession of the pledged assets must be transferred to either the pledgor or a third party (e.g., a security agent) and the pledge must be granted in a public deed to be enforceable against third parties. This type of pledge is not subject to registration.

The pledge without displacement (which may be created over, among other assets, harvesting machinery, proceeds of agricultural land, raw materials, merchandise held in a warehouse and credit rights) does not require transfer of possession but must be executed in a deed before a notary public and registered.

Another way of taking security over assets is through a retention of title agreement.

Enforcing security

A debtor’s declaration of insolvency entails that no enforcement of security in rem may be initiated or continued against a debtor’s assets which are necessary for its business: (1) until a composition agreement is approved; or (2) one year after the declaration of insolvency if the liquidation phase has not already started.

However, enforcement of security in rem may be pursued before the above-mentioned terms if the judge of the insolvency proceedings declares that the assets are not necessary for the debtor’s business. In this regard, the SIA illustrates examples of assets that are not considered necessary for the continuity of the debtor’s business.

Moreover, actions such as the following may not be carried out against assets that are considered essential for the continuity of the debtor’s business: among others, actions for the termination of sales of fixed assets with deferred payment in the event of default, even if the faculty is registered with the relevant land registry and actions aimed at recovering assets transferred under financial leasing formalised in a document involving enforcement or that have been registered with the above-mentioned registries.

The enforcement of security may be blocked even before the declaration of insolvency, if the debtor notifies the court that it has started to negotiate with its creditors to reach a
collective refinancing agreement, a Spanish scheme, an early composition agreement or an out-of-court payment agreement within the two months in which the debtor is obliged to file for insolvency (please refer to II.1, supra).

This is known as a ‘pre-insolvency notice’ and is the period in which the SIA grants certain benefits to the debtor and to a certain extent limits the creditors’ rights, to enable the debtor to negotiate with its creditors (e.g., it is no longer obliged to file for insolvency until the pre-insolvency period elapses).

During that period, it will not be possible for secured creditors to initiate enforcement actions over assets that are necessary to continue the debtor’s professional or business activity (exceptionally, enforcement of security in rem may be initiated but will be stayed) and already initiated enforcements will be stayed.

However, enforcement of security in rem by financial creditors over any type of assets (even if they are necessary to continue the debtor’s professional or business activity) may not be initiated or will be suspended, if financial creditors representing at least 51 per cent of the liabilities of the company support starting a Spanish scheme.

v Clawback actions

Under the SIA, the debtor’s acts within two years prior to the declaration of insolvency may be revoked if they are detrimental to the debtor’s estate, even in the absence of fraud.

In such a case, the SIA also provides some rebuttable or non-rebuttable presumptions. For instance, acts of disposal carried out for no consideration or debt pre-payment due after the insolvency that are not secured with security in rem will be considered detrimental in any event (non-rebuttable presumption). Other acts, such as: (1) transfers made for consideration in favour of a related party; (2) the creation of security in rem to secure pre-existing unsecured obligations, or new obligations substituting unsecured obligations; or (3) the pre-payment of claims secured with a security in rem due after the insolvency will be presumed detrimental but may be rebutted with evidence to the contrary (rebuttable presumptions).

Some acts will never be subject to clawback, including, among others: (1) acts carried out in the ordinary course of business under standard conditions; (2) acts included within the scope of the special laws that regulate the payment and clearing and liquidation systems for securities and derivatives; and (3) guarantees or security created for claims under public law and in favour of the salary guarantee fund in the recovery agreements or conventions foreseen in their particular provisions.

Other than the above, the burden of proving the detriment caused to the debtor’s estate lies with those exercising the clawback action.

If the act is revoked, it will be considered void. Consequently, both parties will have to return the consideration received for the act, together with the relevant proceeds and interest. Moreover, if the judge believes that the party entered into the agreement with the debtor in bad faith, he or she will award damages and losses caused to the debtor’s estate.

Finally, the claims that arise in favour of the defendant as a result of the parties returning the consideration will be considered a claim against the debtor’s estate and must be paid together with the consideration returned to the debtor, unless the act was carried out in bad faith, in which case the claim will be deemed subordinated.

vi Duties of directors in companies with financial difficulties

When a company is in financial distress, directors may be found liable in the following cases.
Capital impairment situation

If the company is subject to mandatory dissolution – i.e., when its net worth is less than 50 per cent of its share capital – directors must call the general shareholder’s meeting within two months following the moment they became aware (or should have become aware) of the situation to either restore the net worth or wind up the company.

If a general meeting is not held or the corresponding resolutions are not passed, directors must file for the judicial dissolution of the company within two months following the general meeting or the date on which the meeting should have been held. If directors fail to comply with these obligations, they are jointly and severally liable for the obligations arising after the capital impairment situation.

Nevertheless, the directors’ obligation to file for judicial dissolution is substituted for an application for insolvency if the company is insolvent.

Guilty insolvency

The SIA establishes a specific liability for cases when the debtor’s insolvency has been caused or made worse by the debtor’s, directors’ (including shadow and de facto directors) or general attorneys’ bad faith or gross negligence (including those who were directors or general attorneys within two years prior to the declaration of the insolvency).

This regime provides a general rule (described above) and specific rebuttable and non-rebuttable presumptions. For example, the SIA establishes a rebuttable presumption of bad faith or gross negligence when directors fail to comply with their obligation to file for insolvency within two months following the date on which they became aware or should have become aware of the company’s insolvency. A non-rebuttable presumption is where the debtor fails to comply with its obligations of keeping accounting records or if material inaccuracies are found in the company's financial statements.

Directors, including shadow and de facto directors, who are considered liable for the insolvency, may face the following consequences: (1) they could be disqualified from being directors for two to 15 years; (2) they could lose all claims against the debtor; and (3) they could lose their right to compensation for damages. They could also be fined if they are deemed liable for the insolvency and this results in the debts not being settled with the debtor's assets.

III RECENT LEGAL DEVELOPMENTS

No other significant changes to the insolvency proceeding have come into force recently. The Recast Regulation approved by the European Parliament has entered into force on 26 May 2016.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

i Restructuring of Abengoa

The restructuring process of Abengoa’s Group has been by far the largest restructuring in Spain (with an initial debt of €20 billion) with impact worldwide due to the size of the group (with more than 8,000 financial creditors and 600 group companies). The restructuring process began on November 2015 when the debtor filed a pre-insolvency notice to the court
and was completed on March 2017. In this process, two major agreements were subject to homologation in less than one year (a standstill agreement to extend the negotiation period and the major restructuring agreement).

ii  **Banco Popular**

Banco Popular was the first European financial entity subject to the SRM. Having declared its unviability before the relevant European and national organisms, the SRM was activated. As a result, the FORB and Spanish Central Bank agreed to the sale of the bank to Banco Santander for the amount of €1. Equity holders were subject to the debt reduction of all their investments.

V  **INTERNATIONAL**

Cross-border insolvencies are different to those that are subject to EU Regulation 2015 and are subject to the Spanish private international law system that has adopted the EU Regulation model when determining the rules of law recognition and enforcement (without the principle of community trust).

VI  **FUTURE DEVELOPMENTS**

No future developments are foreseen in the short term.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

The Swedish economy is expected to continue its recovery during 2017. According to the Swedish Ministry of Finance’s April 2017 macroeconomic assessment, growth is expected to reach 2.6 per cent during 2017 and slow down to 2.1 per cent during 2018. Growth is expected to be driven by higher exports, increased private investments – primarily in housing construction – and increased consumption, both private and public.

Competition between the banks is picking up and new categories of lenders (such as insurance companies, pension funds and specialised debt funds) have entered the market, in particular for long-term credit. Sponsors and other borrowers are using the increasing competition to achieve more attractive terms. In addition, a growing Swedish and Nordic high-yield bond market is competing with traditional forms of lending.

Even though the economy is growing, the unemployment rate is falling, interest rates are low and the bank and capital markets offer attractive financing terms, certain industries are facing industry-specific challenges, for example, the mining industry, the print media industry and industries with exposure to the oil price.

In 2016, 5,270 limited liability companies entered formal bankruptcy proceedings and 182 companies entered formal company restructuring proceedings (with judicial composition). For 2015, the figures were 5,484 and 160, and for 2014, 6,017 and 108, respectively – indicating a declining trend for bankruptcies and a slightly rising trend for company restructuring proceedings.

As is apparent, bankruptcy is a far more frequently used procedure than court restructuring. In practice, most restructurings are done informally, without the involvement of the courts or any public authorities. As the lenders maintain full control in out-of-court proceedings this is a preferred route compared with in-court proceedings. The spate of bankruptcies in the early 1990s has also had a permanent effect on the Swedish market as most lenders then realised that it is often economically more viable to restructure ailing firms outside formal procedures. Informal restructuring has, therefore, largely become the preferred solution. That said, there are circumstances in which judicial procedures are needed and can be efficiently employed to restructure and finance distressed companies.

The techniques employed in restructurings have developed and become more sophisticated. The main driver for this development has been the larger restructuring cases of recent years and the international restructuring market has also been an influence.
increase in both international groups’ insolvencies and also a growing market for distressed debt transactions has increased the awareness on the local market. In addition, the growing Nordic high-yield bond market has added layers of complexity to restructurings, not only due to the different kind of terms for bonds compared with loans, but also with respect to the different objectives of bond investors compared with bank lenders.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

In Sweden, there are two main formal proceedings available for companies in financial difficulties: company restructuring and bankruptcy. A company may also be mandatorily liquidated. Mandatory liquidation is triggered by the equity of the company being less than half of its registered share capital (this is essentially a balance-sheet solidity test) and is often caused by over indebtedness. Bankruptcy is triggered by insolvency, which means that the debtor is not able to discharge its debts as they fall due and that such inability is not only temporary. Bankruptcy aims at the disciplined liquidation of the company’s assets with a view to optimising creditor returns and usually ends with the liquidation of the company. Formal company restructuring is based on a ‘prospective illiquidity’ test and aims at restructuring a company’s financial position so that it can continue operations with reasonable prospects of profitability. Company restructuring takes place under the supervision of a court-appointed ‘reconstructor’ and bankruptcy is managed by a court-appointed administrator, who takes the place of the shareholders and directors in managing the company’s business.

Although Swedish insolvency law does not provide for extensively ‘pre-packed’ insolvency procedures, it is common for some element of pre-packaging to take place, usually in close cooperation with an administrator appointed by the court. The courts normally accept the company’s choice of official if it is supported by the largest secured creditors. In recent years there have been a number of successfully ‘pre-packed’ deals within the real estate sector with sales of distressed real-estate portfolios via an official auction process conducted by the Swedish Enforcement Authority. The advantage of choosing the formal auction process in these types of transactions is that any sale of real property made through a formal auction process effectively extinguishes all claims and security in relation to the sold property. Thus, if existing junior creditors do not consensually agree to an informal debt restructuring, a formal auction process could be a way to squeeze out such creditors and sell the property free from claims and encumbrances. Obviously, such pre-pack solutions need to be carefully planned and structured in order to maximise the value of the sold assets.

i Company restructuring

A formal company restructuring aims to achieve a financial workout of financially distressed companies that are deemed to have sustainable long-term business prospects. Financially distressed companies can apply for a restructuring with the local court. An application will only be approved if the company is unable to pay its overdue debts or will be unable to do so in the near future and there are reasonable grounds to believe that the restructuring can achieve its purpose.

When approving the restructuring the court appoints a ‘reconstructor’ to manage the restructuring. Formal company restructuring is a debtor-in-possession proceeding where the management and board of directors of the company remains in control of the business but supervised by the reconstructor. The reconstructor will, inter alia, investigate the financial
situation of the company and, together with the company, establish and implement a restructuring plan. The creditors will be afforded an opportunity at the creditors’ meeting to express opinions regarding whether the company restructuring should continue. If requested by any of the creditors, the court will appoint a creditors’ committee of no more than three to four persons from among the creditors. Representatives for the Swedish Tax Authority, the largest secured creditor and the employees are normally included in the committee. The committee is purely advisory; in matters of material importance the reconstructor is obliged to consult with the committee but is not bound by any advice given.

Crucial for the success of the restructuring is often that the total unprioritised debt of the company is decreased to a manageable level in order for the company to regain its financial viability. The composition may be conducted on a voluntary basis; however, more commonly, the negotiations will aim at a mandatory judicial composition, during which claims of creditors who are entitled to participate in composition proceedings may be mandatorily reduced. The composition should provide all entitled creditors with similar rights at least 25 per cent of the amount of the claims, unless a lower composition percentage is approved by all known creditors who would be covered by the composition, or where special cause exists for a lower percentage.

Only creditors whose claims arose prior to the application for company restructuring may participate in composition proceedings. A creditor whose claim enjoys priority or can be satisfied through set-off will not participate, nor may a subordinated creditor participate in the proceedings, unless the other creditors who are participating in the proceedings so consent. There is case law to suggest that a creditor is subordinated in company restructuring only if this is clear from the relevant agreement; but subsequent statutory changes may inadvertently have changed the law in this regard, in which case a creditor contractually subordinated in bankruptcy will automatically also be subordinated in a company restructuring.

An obvious advantage of a judicial composition is that, contrary to a voluntary write-down of debts, not all (participating) creditors need to agree to the write-down provided that an acceptable majority has done so. Before proposing a composition, however, the company and reconstructor should bear in mind that major trade creditors can play a vital role in the success of the restructuring, for example, by extending credit periods or converting their trade credits into long-terms debt. Any forced compositions could therefore jeopardise relations with important trade partners and reduce the chances of a successful restructuring.

A sometimes useful effect is that judicial composition will effectively extinguish all subordinated claims in the company. Thus, by just achieving a smaller composition with the unprioritised creditors, all subordinated debt will automatically be extinguished and the capital structure of the company can be significantly improved, which will also have a positive impact on the value of the remaining debt and the value of the shares in the company. From the point of view of the subordinated creditors this is unreasonable since it puts the shareholders’ interests before the subordinated creditors, the claims of which are being extinguished, whereas there is no possibility to, for example, reduce the shareholders’ equity interests correspondingly without the consent of the shareholders.

One of the most important features of the company restructuring regime is that a new financier can be given a ‘super-priority’ right in respect of any new debt provided by it, with the consent of the reconstructor, during the restructuring. In order to facilitate a formal restructuring and for the company subject to such to regain financial stability and be able to continue its business, the Swedish Preferential Rights of Creditors Act contains a provision giving ‘super-priority rights’ to claims that are assumed and approved by the
reconstructor during the restructuring. Pursuant to the Act such claims are given general priority and rank before other claims of general priority such as claims for compensation for the performance of auditing functions required by law, employees’ claims for wages or other compensation arising from the employment, certain pension benefits and claims with priority connected to floating charges. Although the super-priority right is essential in finding new financiers, existing financiers (e.g., banks that hold floating charges in the company) are disadvantaged in that the super-priority claims are prioritised over the assets covered by a floating charge. This has given rise to much debate on the implications of the super-priority rights and whether it is reasonable for, for example, a financing bank to see the value of its floating charge being diminished as a result of a restructuring without being able to object to its outcome. The reconstructor is, however, responsible for procuring that the value of claims secured by floating charges does not decrease more than necessary. Further, it should be stressed that the super-priority right does not apply to claims that arise (e.g., interest) during the restructuring under agreements entered into prior to the commencement of the restructuring. Apart from the super-priority right described above, Swedish law does not provide for any further special priorities.

Restructuring also automatically imposes a moratorium on enforcements and termination of existing agreements and provides conditional protection against bankruptcy. The moratorium does not, however, apply to secured creditors that hold possessory pledges, which may be enforced if the relevant pledgee has a due and payable claim, meaning that the underlying debt must actually have been accelerated to be effective.

Unless terminated prematurely by court order, restructuring may last for no more than three months, subject to an extension for up to nine months in certain circumstances. In our experience, the court performs a fairly summary review of the application – it is usual that the application be accepted (or, exceptionally, rejected) the same day. It is customary to submit the application before – often immediately before – the court opens for business to allow the court as much time for deliberation as possible. In practice, it has also proved relatively easy to obtain the prolongation, at least if the reconstructor supports it. The difficulties of Saab Automobile shows that, in some circumstances, renewed restructuring proceedings may also be granted very close to a previous failed restructuring. In the Saab case, the first restructuring was granted in 2009 and continued, unsuccessfully, through prolongation. In 2011 the company applied again for company restructuring. After having been denied at first instance, the application was granted upon appeal. Saab then carried out a second, prolonged and ultimately unsuccessful company restructuring.

At the end of the restructuring (regardless of whether it has been successful), the reconstructor resigns and the moratorium is automatically lifted. The court will not be required to make any decision if the time allocated to the company restructuring merely elapses. After an unsuccessful company restructuring, the company will usually have gone through more of its liquidity and accumulated more debt than at the commencement of the proceedings (including a debt to the state corresponding to the state’s guarantee for staff remuneration). This creates powerful incentives for creditors caught by the moratorium to act swiftly when the moratorium has been lifted; creditors who have not been prevented by the moratorium from enforcing their security (that is, creditors with security over specific assets) will often already have enforced security leaving the company potentially without crucial business assets. Unsecured creditors – such as suppliers and other trade creditors whose continued support is absolutely necessary to the continuation of business – will often have been hard hit by the moratorium and any compulsory composition, and may, therefore, be
reluctant to assume continued credit risk after the end of company restructuring proceedings. This is one of the contributing factors as to why company restructuring proceedings often are quickly followed by formal bankruptcy. This is also a factor making informal restructuring by contractual negotiation earlier in the life of the ailing company an often more attractive solution to creditors.

As a final reflection, treatment of the shareholders – or rather the inability to judicially involve the shareholders in the process – is thought to be a major challenge in any successful restructuring of an ailing company. One solution might be for legislation to abolish the artificial distinction between insolvency law – dealing with debt – and company law – dealing with equity – by allowing insolvency proceedings to also reconstruct the equity of a company. In the absence of any such Swedish legislation, however, it is often found that neither company restructuring nor bankruptcy proceedings provide the flexibility required, which may be an important contributing factor for both the frequent failures of company restructuring proceedings and the prevalence of informal contractually negotiated arrangements. As mentioned earlier, informal restructuring proceeds often involve a restructuring of both the debt and the equity.

ii Bankruptcy

Bankruptcy proceedings are initiated as a consequence of a company becoming insolvent. The relevant test is cash-flow insolvency and a company may enter bankruptcy if it cannot pay its debts as they fall due and such inability is not merely temporary.

Proceedings are aimed at winding down an insolvent company by way of selling its assets and distributing any cash received to the creditors. The normal result is a negative balance leading to the automatic liquidation of the company. Any positive balance accrues to the shareholders, who may choose whether to liquidate the company. The proceedings can be initiated by the company as well as by a creditor by filing of a petition for bankruptcy with the local court. The company’s application will normally be granted without investigation of its merits. A creditor will have to prove that the conditions for bankruptcy have been met; but can in some specified circumstances rely on legal rules that shift the burden of proof to the debtor to prove that it is solvent. Contested applications are litigated in full civil trial.

After the court has declared a company bankrupt it appoints an administrator that independently takes control over the company’s assets with the main task of realising such assets and repaying the debts of the bankruptcy estate in accordance with the creditors’ statutory ranking. Upon formal bankruptcy, the company loses its legal capacity and the administrator takes the place of the shareholders and directors in running the company. Statute classifies claims into one of the following:

- claims with special priority (essentially security over specific assets);
- claims with general priority (including various statutory costs, transactions costs and taxes);
- claims without priority; and
- subordinated claims.

Shareholders have no claims in the ranking and are only entitled to any positive balance post-bankruptcy in accordance with normal company-law principles. The priority ranking cannot be changed or amended by contractual agreement, but a creditor may agree to its claim being subordinated in relation to all other creditors of the company, whereby the repayment of such debt is conditional upon the full payment of all other claims against
the company. Through inter-creditor agreements, creditors may also contractually agree to an order of payment between themselves. The administrator and the bankruptcy estate will not be bound by the inter-creditor arrangements as a party, but certain features of a typical inter-creditor agreement (for example, that the junior debt may not be repaid before the senior debt has been discharged) should be taken into account by the administrator when distributing funds from the bankruptcy estate. To mitigate the risks of the administrator not honouring inter-creditor principles, it is important to carefully consider turnover provisions that, albeit not being binding upon the administrator, are binding and enforceable among the creditors who have signed up to the agreement.

As regards the existing creditors of the company, neither unsecured nor secured creditors are generally free to take independent enforcement actions in bankruptcy. Secured creditors that hold possessory pledges may sell the security assets subject to such pledges at a public auction or, in respect of certain financial assets, in any other manner (including by way of appropriation). With the exception of certain financial assets, the administrator must also be given the right of first refusal to the security assets. A valid claim against a bankrupt company — regardless of whether it is due and payable — may be set off against a claim that the bankrupt company had against the creditor when the bankruptcy commenced.

iii Clawback actions

Any pre-insolvency planning (including planning of pre-commencement financing) is arranged with a view to avoiding clawback risks, minimising upstreaming complications and maximising the value and robustness of the security package. Other aspects that need to be addressed in this context include subordination of debt layers as well as limiting potential subrogation rights of intragroup security providers. The latter aspects are usually addressed in inter-creditor agreements dealing with both debt subordination and the waiver of subrogation rights by the intragroup security providers.

The principal clawback provision under Swedish law are based on the Roman law concept of *actio Pauliana* (fraudulent conveyance) and, therefore, require a degree of fraudulent behaviour in order to be triggered. Thus, that clawback provision will only come into play if the relevant transaction entails: (1) that a particular creditor has, in an unfair manner, been favoured in preference to other creditors; (2) the property of the debtor having been concealed from its creditors; or (3) its debts being increased, and provided that such transaction (by itself or together with other transactions) led to the company becoming insolvent. Another prerequisite is that the other person party to the transaction knew, or should have known, of the insolvency of the debtor and the circumstances making the transaction improper.

Consequently, any recovery would have to be based on some degree of ‘disloyalty’ as against the relevant debtor’s general collective of creditors. As Swedish law makes a clear distinction between the contractual creation of legal arrangements inter partes and the perfection of those arrangements erga omnes, care is usually taken to ensure that all

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2 An interesting and practical implication of the turnover provisions in the context of bond financing is that it is virtually impossible to enforce a traditional turnover provision against a large and often unknown collective of bond investors. The practical solution provided is instead that the a corresponding amount of any funds received by a bond investor which should have been turned over to the other creditors, will be withheld by the security agent the next time any funds are run through the payment waterfall in the intercreditor agreement.
important arrangements – in particular, security arrangements – have not only been created but also perfected in circumstances that would make a recovery action unlikely to succeed. For instance, perfection would typically be sought well in advance of the likely starting date for any suspect period (usually three months prior to the borrower’s entering into formal insolvency proceedings) to avoid recoveries.

When renegotiating or providing new financing to a group facing financial difficulties, debt providers often require that new or additional security and guarantees are granted by the borrower group. The debt provider in this scenario needs to pay close attention to the risk of such security and guarantees being subject to clawback in the formal insolvency proceedings in respect of the security provider. Under these rules, a security interest granted after the security provider incurred the secured obligations may be subject to clawback unless the granting of the security nonetheless can be considered as ‘ordinary’. This exception for ‘ordinary’ transactions is sometimes referred to as a ‘safe haven’ for creditors, although it is difficult to clearly define a transaction as ordinary.

Simply put, security or guarantees will be deemed ordinary in the event: (1) they were agreed no later than the incurrence of the debt or more than three months prior to the insolvency; and (2) the terms providing for security or guarantees have been implemented by the parties in a manner that does not amount to an opportunistic application of the terms with a view to a looming insolvency. However, the exception for ‘ordinary’ security has been introduced quite recently and Sweden therefore lacks court precedents on the subject. Some guidance may be found in the preparatory works to the legislation that states that in order to meet this condition (i.e., that the granting of the security is ordinary), the security should be granted in direct relation to the funding and not by reason of the security provider experiencing financial difficulties. According to the prevailing view in Swedish legal literature, on the other hand, one needs to make an overall assessment of the circumstances in which the security was taken, taking into account all circumstances of the transaction. The exception can also be considered from the view that the security transaction in any event may not diverge from what can be considered as normal and natural.

A change of creditor will not, however, affect the validity of the security provided that the underlying claim remains the same and that the relevant transfer expressly includes the existing creditor’s portion of the security securing the transferred debt. Similarly, the fact that a creditor has acquired its portion of the debt from another creditor would not generally restrict the new creditor from benefiting from the provisions under Swedish law granting a creditor the right of set-off under certain circumstances. However, the right of set off may be restricted in the event that the creditor assuming the debt had (or should have had) knowledge about the debtor’s financial difficulties and consequently has acquired the debt in order to improve its situation in any insolvency proceeding affecting the debtor.

Any security that is deemed to have been granted for ‘old’ debt will be at risk of being subject to clawback during a hardening period of three months from the time that the security is perfected. The hardening period may, however, be up to five years if the security provider was insolvent at the time that the security was perfected. The five-year hardening period applies to certain intentionally fraudulent or conniving transactions whereby a certain creditor is unduly favoured over other creditors in such a way that the debtor’s assets have become unavailable to its other creditors. The extended hardening period also applies where the effect of the fraudulent transaction is that the debtor has assumed additional debt. A general criterion for the extended hardening period is that the debtor was insolvent when the transaction took place or became insolvent through the transaction (either independently or
in connection with other transactions). The hardening period may, however, be unlimited to certain connected persons who are assumed to have the required knowledge about the debtor unless they can show that it was reasonably likely that they did not have the information.

As regards third-party creditors, there is a ‘safe haven’ to the extent that they did not have any knowledge of the debtor’s insolvency and that they did not have knowledge of any circumstances that would render the transaction inappropriate.

As mentioned above, a number of clawback provisions are triggered if and to the extent the relevant debtor was or became insolvent as a result of the transaction. Pursuant to the Swedish Bankruptcy Act, a company is generally considered to be insolvent if it lacks the ability to pay its debts as they fall due and such inability is not just temporary. This definition and the interpretation of it have been subject to much debate among legal scholars and practitioners as the exact point in time when a company is deemed insolvent has several implications. However, the prevailing view among scholars and practitioners is that a company that cannot pay its debts when they fall due could, nonetheless, be considered solvent if the company has a realistic plan for successfully restructuring the company and finding a long-term financing solution. Whether a company is solvent is therefore to be separated from it being liquid, which relates to the company’s immediate ability to service its debts rather than the company’s financial situation over a longer period. For example, a company with a strong balance sheet will likely be able to pay its long-term debt, but might at a particular time lack the liquidity to service its debt.

In addition to the clawback risks, any security or guarantees that are granted in violation of the relevant provisions may make directors of the company personally liable for losses incurred by a creditor due to the mismanagement of an insolvent company. Such mismanagement is generally considered to include the directors’ having continued the company’s business past the point when they knew, or should have known, that there was no reasonable prospect of avoiding the insolvency of the company, and did not take the required steps with a view to minimising the potential loss to the company’s creditors. In addition to the risk of incurring personal liability for losses incurred by the company’s creditors, a director may face criminal charges for crimes against creditors, as set out in the Swedish Penal Code. These offences include situations in which a director is deemed to have acted carelessly towards the company’s creditors or to have favoured a particular creditor by, for example, paying a debt that had not fallen due or providing security or guarantees that were not required under the terms of an existing agreement.

### III RECENT LEGAL DEVELOPMENTS

Swedish bankruptcy law is based on long-standing principles and company restructuring, although a fairly new procedure (introduced in 1996) is largely based on older law dealing with compositions. After 2010 several official committees have presented proposals for amendments of the Swedish insolvency regime.

In 2010 it was proposed to unify the separate bankruptcy proceeding and company reconstruction proceeding into a new unified ‘insolvency proceeding’.

On 17 October 2016 the Entrepreneurship Committee presented a new proposal with an objective to give companies ‘a second chance’, but also to reduce the risk that companies which have no chances of becoming viable get protection under a formal company restructuring and thereby delay a liquidation of their assets. The proposal includes, amongst other things, changes to the rules on judicial composition, introduction of specialist insolvency
courts, increased ability for the debtor to transfer rights under contracts, protection under the proceeding already from the filling of the application rather than from the opening of the proceedings and a requirement for a liquidity prognosis to be provided at filing.

It is not yet clear if the proposals will result in any changes of the laws.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

The financial distress of a group often requires that the terms of its existing financial arrangements be renegotiated in order to, *inter alia*, reset financial covenants, provide a more flexible amortisation structure, defer interest payments and allow for various restructuring measures. These actions are often sufficient if the business generates free cash flow. It is not uncommon, however, that a group facing financial difficulties may need additional liquidity to continue to operate or capital for necessary investments. In such cases a successful restructuring of the group will not only require a strengthening of the balance sheet by reducing the debt but also additional financing from either existing stakeholders or third parties in order to provide additional liquidity or finance the necessary investments.

In the event of a balance-sheet problem where existing shareholders cannot provide sufficient equity, the improvement of the balance sheet can be supported by the lenders through a debt-to-equity swap. An example of a Swedish debt-equity swap transaction launched in recent years is the Nobina group restructuring. Nobina had issued a US high-yield bond and was expected to fail to meet its repayment obligations under its US bonds. The solution included an exchange of the US high-yield bonds for new Swedish law-governed high-yield bonds and shares in the parent company of Nobina. The settlement of the transaction took place across Euroclear Bank and Clearstream Luxembourg for the US bonds that were exchanged against new Swedish high-yield bonds held by Euroclear Sweden. Simultaneously, a portion of the existing US bonds were used for an in-kind share issue in the parent company of Nobina. The end result was a dilution of the shareholders and a significant reduction of the debt. This was a successful out-of-court restructuring and saved Nobina from entering formal insolvency proceedings. Through this solution the debt level was decreased and the currency exposure was reduced, giving the company the necessary means to survive long term and develop its business. Another type of 'debt to hybrid equity swap' was recently employed in the restructuring of the Basler Fashion group, a distressed group within the fashion industry, where the senior debt providers swapped their senior claims against the operating entity against a value participating debenture in the ultimate parent company, giving the value participating lenders the right to a certain percentage of the group’s profits, instead of an outright ownership stake. In addition, a majority interest in the group was transferred to a trust vehicle with the ultimate aim of selling the group to an investor after the conclusion of the operative restructuring. From a lender’s perspective, this type of hybrid solution can be an attractive alternative as the lenders can avoid taking ownership of the group at the same time as they can benefit from the economic value or profit generated by the group.

Whether a financially distressed group requires that the terms of its existing financial arrangements be renegotiated or if it also requires additional financing will have a significant impact on the financing process. A provider of new or additional financing to a financially distressed group often requires more control and economic return as compared with the existing stakeholders. The new finance provider will usually also be in a position to elect –
taking certain legal, practical and commercial aspects into consideration – the way in which
the new funds will be provided. The different type of financial instruments available can
be used and combined in a way to achieve the most feasible restructuring of the group,
considering the different stakeholder positions and also the group’s need for a new capital
structure.

In practice, a combination of a renegotiation of the terms of the existing debt together
with the provision of new debt is often sought. As set out above, the additional financing
can be provided by way of debt, common equity, preference shares, convertible loans or
various other forms of hybrid debt instruments. Which financing method is preferred varies
depending on numerous factors, including whether the relevant company is in a position to
take on and service additional debt and on the financing provider’s preferences.

As a consequence of the failing iron ore prices several companies in the mining industry
have faced difficulties. For example, Dannemora, Northland Resources and Nordic Mines
have encountered financial difficulties. The mining industry has been suffering for quite some
time and all three companies have been through out-of-court and in-court restructurings.
The crisis is still not over and even though the different companies have different issues there
is one common denominator, the iron ore price. If the price increases sufficiently, it will most
likely be much easier for companies such as these to access the capital markets to obtain
financing.

Another industry under pressure is the print media industry. On 23 May 2016, 16 entities in the Stampen group owning local newspapers, printing facilities and newspaper
distribution companies in the western part of Sweden applied for formal company
restructurings. In terms of the number of companies involved, this is the largest company
restructuring in Sweden.

It should also be noted that the growing high-yield bond market has added a layer of
complexity to restructurings. Restructuring of bonds is significantly different to restructuring
of bank loans. The bonds are traded freely and it is sometimes difficult to identify and convene
a bondholders committee with the sufficient majority. Also, the sharing of information can be
sensitive from an insider perspective, which makes restructuring negotiations more difficult.
More importantly, the objectives of the bond holders differ more than among lenders in a bank group. There are participants in the bond market who acquire distressed debt with
the aim of subsequently acquiring control over the equity interest in the borrower. There is
also an increasing number of bond investors who target financially distressed bond issuers
by acquiring corner positions at a significantly discounted price. The corner positions are
then used to block any consensual restructuring proposals until that investor is bought out
at a higher level than its original investment or the borrower is forced into equitisation. The
restructuring strategies employed by the borrowers may also entail strategies regarding the
timing of information to the market to manage the pricing of the bonds before restructuring
proposals are launched. It may be easier to achieve a restructuring solution if many of
the bond holders have acquired their bonds significantly below par. Examples of recent
restructurings that involved bond debt and debt-for-equity swaps are RURIC (Russian Real
Estate Investment Company), a real property development and investment company owning
assets in Russia; Trigon Agri AS, a soft commodities producer with operations in Ukraine,
Russia and Estonia; and PA Resources AB, an oil and gas company.

3 For example, by way of debt, equity, preference shares, convertible loans, value participating loans or any
other form of instruments.
PA Resources used a formal company restructuring proceeding in a novel way. As part of a composition procedure, the creditors were offered an additional alternative to being paid a certain fixed percentage of their debt within a year, as prescribed by the Swedish Company Restructuring Act. Creditors could choose to be paid an unknown sum out of available cash from the sale of certain assets during a specific period, after which the remainder of their claims would be converted into equity of the company. Creditors holding a large majority of the claims on the company accepted the offer to be paid out of available cash and participate in a debt-for-equity swap.

Other recent larger company reorganisations also include INDISKA, a retailer focusing on clothing and interior decoration, and Teknikmagasinet, an electronics retailer.

V INTERNATIONAL

Traditionally, Swedish insolvency law has been characterised by a certain asymmetry in respect of the international ramifications of a company’s insolvency. The basic rules are that foreign insolvency proceedings are not recognised or enforced in Sweden, and Swedish insolvency proceedings in respect of a Swedish entity are universal and, in respect of a foreign entity, includes all its assets in Sweden (but not elsewhere). The first rule has been modified by, first, treaty law in the Inter-Nordic Insolvency Treaty and, second, by the EU Insolvency Regulation (originally Council Regulation No. 1346/2000 on insolvency proceedings as recast by Regulation No. 2015/848 on insolvency proceedings) (EIR). The treaty is now only effective in respect of Denmark, Norway and Iceland, with the effect that insolvency proceedings in those jurisdictions will be given effect in Sweden as if they were Swedish. In respect of Finland, the treaty has, to all intents and purposes, been superseded by the EIR.

The EIR, insofar as it seeks to encourage the cooperation among the courts of the various Member States in respect of insolvency proceedings, would not in principle be a novelty for Swedish courts. There have long been special arrangements with the other Nordic countries enabling and encouraging courts and administrative authorities in the various states to deal directly with each other and to cooperate as appropriate.

VI FUTURE DEVELOPMENTS

On 22 November 2016, the European Commission issued a proposal for a new directive which aims to introduce effective preventive restructuring frameworks across Europe. The proposal is in an early stage and will be subject to negotiations and (most likely) amendments before it can be approved by the European Council and the European Parliament. Thereafter each member state must implement the proposal into national law before it will become effective. This process will likely take several years to complete.

As mentioned in Section III, supra, several proposals to amend the Swedish insolvency legislation have been presented by official Swedish committees during the last couple of years.

Furthermore, in June 2015, the Nordic-Baltic Insolvency Network published the Nordic-Baltic Recommendations on Insolvency Law. The Nordic-Baltic Insolvency Network consists of academics and practitioners from Sweden, Norway, Denmark, Finland, Estonia, Latvia and Lithuania, and its main purpose is to encourage efforts towards a harmonisation of the substantive insolvency laws of the member countries. It remains to be seen if it will influence Swedish insolvency laws.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

The economic slowdown that affected the UAE, and Dubai in particular, from 2009 to 2011 highlighted the inadequacy of the existing legal framework for restructuring and insolvency. While liquidity shortfalls and the collapse of the construction and real estate markets have had adverse impacts on many UAE-based businesses, the existing laws relating to restructuring and insolvency remain largely untested in view of the lack of procedures for reorganisation and protective composition. The requirement for a new restructuring and insolvency regime arose because of the lack of adequate legislation to govern bankruptcy of businesses in the UAE. The resulting Federal Law No. 9 of 2016 on Bankruptcy (the Bankruptcy Law) came into effect on 31 December 2016, repealing the previous law relating to insolvency and attempts to address these issues and signalling a move away from a creditor-friendly regime to one that favours the debtor and its ability to have control over the state of its solvency. This year’s chapter, therefore, departs markedly and almost completely from the prior years’ chapters on this topic.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

i Overview

The UAE provides a framework for the restructuring and insolvency of companies and traders, which is contained in UAE Federal Law No. 9 of 2016 on Bankruptcy (the Bankruptcy Law). UAE Federal Law No. 8 of 2015 on Commercial Companies (as amended) (the Commercial...
Companies Law) contains provisions for the dissolution of a company.\(^3\) The Bankruptcy Law also repeals the Penal Code of the UAE (contained in Federal Law No. 3 of 1987) provisions on non-fraudulent bankruptcy.\(^4\)

**ii The Bankruptcy Law**

The Bankruptcy Law applies to any company governed by the provisions of the Commercial Companies Law,\(^3\) businesses formed in the free zones (except those in the financial free zones of the Dubai International Financial Centre (DIFC) and the Abu Dhabi Global Market (ADGM), which have their own bankruptcy rules), licensed civil companies, public sector companies (i.e., those wholly or partially owned by the federal government or an Emirate government), and individual traders.

**Preventive composition**

Under the Bankruptcy Law, a debtor can apply for preventive composition rather than having to proceed directly to bankruptcy proceedings. During the preventive composition scheme, the debtor will be under court protection from individual creditor claims. This option is only available to debtors if it has not been in default for more than 30 consecutive business days and it is not insolvent. Once the scheme is in place, the debtor cannot dispose of any property, stocks or shares, make any borrowings, or (if it is a company) change ownership or corporate form.

The debtor must make an application to the court that must include, among other things, a description of its economic and financial position, details of its moveable and immovable properties, employees and creditors, and its cash flow and profit and loss projections for the 12 months following the date of its application.

The debtor must continue to perform its obligations under any of its contract, provided that the court has not issued a judgment of stay of execution due to its failure to perform its obligations under such contract. A trustee will be appointed to facilitate the preventive composition process, and such trustee will have the right to request the court to rescind any contract if that is what is in the best interests of the debtor and its creditors and provided that it does not substantially harm the other contracting party’s interests.

The court will appoint one to three trustees as designated by the debtor, or it will appoint an expert or other person (if more appropriate). The trustee is obliged to publish in two daily local newspapers: (1) a summary of the decision approving the preventive composition, with a request that all creditors file appropriate claims; (2) a list of the debts and statement of accounts accepted from each of those debts; (3) the invitation to creditors to discuss and vote on the draft preventive composition arrangement; and (4) once approved by the court, the decision and summary of the arrangement. Ultimately, the court will approve

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3 This framework does not apply to all free zones within the UAE. The Dubai International Financial Centre (DIFC) and Abu Dhabi Global Market (ADGM) (both financial free zones) have developed their own insolvency law and insolvency regulations for DIFC and ADGM entities.

4 The criminal sanctions relating to bankrupt estates under UAE law are not elaborated upon in this chapter, which focuses on the restructuring and insolvency framework in the UAE.

5 The Commercial Companies Law provides for the following types of companies: limited liability companies, simple commandite companies (a type of partnership), joint liability companies (another type of partnership), public joint stock companies, private joint stock companies. Its provisions (excluding the incorporation provisions) also apply to foreign companies.
the final list of approved creditors, having reviewed any objections received following the publication of the debts. The trustee will submit the draft arrangement to the court, who will then have five business days to make its decision to approve or reject it (taking account of any creditor objections).

Thereafter, the trustee is responsible for supervision of the arrangement throughout the implementation period, including submission of quarterly reports to the court detailing progress and any failures by the debtor to implement the arrangement. The trustee can apply to the court for any amendments to be made to the arrangement if it considers it necessary at any point during the implementation period.

The arrangement must be implemented within three years of the date of court approval. This term can be extended for a further three year period if a two-thirds majority of the unpaid creditors consent to such extension.

Following a request by the trustee, and pending discharge of the debtor’s obligations under the arrangement, the court will issue its decision confirming that the arrangement has been fulfilled. Such decision will be published in two daily local newspapers.

**Conversion from preventive composition into bankruptcy proceedings**

At the request of an interested party, or in exercise of its own discretion, the court may initiate the termination of the arrangement and convert it into a bankruptcy proceeding if: (1) it is proved that the debtor was in payment default for more than 30 consecutive business days or was insolvent on the date of commencement of the preventive composition proceedings, or if this became clear to the court during the court of preventive composition proceedings; or (2) it becomes impossible to apply the arrangement, and ending the same would result in payment default for more than 30 consecutive business days or result in the debtor’s insolvency. (The Bankruptcy Law does not provide any guidance as to what constitutes ‘impossible’.)

**Ability to raise new finance**

While undergoing the preventive composition or restructuring process, a debtor (or the trustee) has the option to apply to the court for authority to obtain new funding. Any ‘new’ creditor will have precedence over any ordinary outstanding debt owed by the debtor (but providing protections for existing creditors).

**Application for initiation of bankruptcy proceedings**

There is a minimum threshold of 100,000 dirhams before a creditor, or group of creditors, can initiate bankruptcy proceedings against the debtor, provided that such creditor has adequately notified the debtor of such debt and the debtor has still failed to repay it within 30 consecutive business days of notification. (The Bankruptcy Law does not address how disputed amounts will be treated by the court).

The debtor must apply to the court to initiate proceedings if it cannot repay its debts as they fall due for more than 30 consecutive business days.

**Company bankruptcy**

The Bankruptcy Law has expanded the number of parties that may apply for the bankruptcy of a company. It is now possible for a debtor company, its creditors, the competent controlling body of the debtor company and the public prosecutor to apply to the courts for a
bankruptcy order. Bankruptcy applications from the above parties will be subject to different requirements. For a creditor, or group of creditors, to make a bankruptcy application against a debtor, it must show that: (1) the debtor remains in default 30 consecutive business days after the creditor sent a written notice of the overdue debt to the debtor; and (2) the debt meets the minimum threshold of 100,000 dirhams. This 100,000 dirhams threshold may prove challenging for smaller trade creditors who are unlikely to meet this threshold and may not be able to identify other creditors to join in taking action, in particular as the annual accounts of most UAE companies are not publicly available. The creditor's bankruptcy application must be accompanied by: (1) the aforementioned notice to the debtor; (2) information on the debt and any related guarantees; and (3) a payment or bank guarantee for 20,000 dirhams, to meet the expenses and costs on initial procedures for deciding the application. This provides a much more debtor-friendly position than under the old bankruptcy regime.

A creditor will have one year from the: (1) date of death of the debtor; (2) striking off of the trader from the commercial register; or (3) date of judgment of incapacity, to apply for bankruptcy proceedings against a debtor. A bankruptcy application can be made for any company, even when the company is in the process of liquidation.

**Bankruptcy of a trader**

A trader may be declared bankrupt in the same ways as a company (see above).

**Bankruptcy proceedings and declaration of bankruptcy**

Within 10 business days of receiving of a bankruptcy application the court will appoint an expert (ideally from its approved list of experts) to help the court evaluate the position of the debtor. The expert will prepare a report for the court outlining the debtor’s financial position and provide an opinion on the possibility for the restructuring the debtor. The court will make a determination on the bankruptcy application within five business days of the later of the receipt of the application or the expert report.

Upon receipt of the bankruptcy application, the court may take such measures (either at its own initiative or at the request of an interested party) as are deemed necessary to maintain or manage the properties of the debtor while it makes its decision (including sealing the place of business of the debtor). While the court evaluates the bankruptcy application, the secured creditors can still enforce the pledge or lien as and when they become enforceable. The court may grant permission within 10 business days of the application from the secured creditor to the court. The court will decide the degree of priority if there are many secured creditors for the same asset.

If the court accepts the bankruptcy application the court may appoint one or more trustees to administer the bankruptcy. A trustee has various responsibilities including publishing a summary of the court’s decision to initiate bankruptcy proceedings in two local newspapers, notifying known creditors, review the claims and supporting documentation from creditors, provide updates to the court on the bankruptcy, maintain a record of creditors and debtors of the bankrupt company and submit a list of creditors to the court - the court will approve the final list of approved creditors, having reviewed any objections received following the publication of the debts. Certain persons cannot act as trustees, e.g., a creditor of the debtor, spouse or fourth degree relative of the debtor or a convicted felon, fraudster or perjurer.
Once a bankruptcy judgement is delivered the trustee shall publish a notification of the judgement in two newspapers and ask all creditors to file a final claim within 10 days of the publication. All late filings of debt will be disregarded, unless the court decides otherwise.

If the trustee fails to notify any creditor to attend a creditors’ meeting or fails to make a publication in accordance with the Bankruptcy Law, the relevant creditor may lodge a grievance with the court within 10 business days of the relevant creditor becoming aware of the creditors’ meeting. If the court approves the grievance, it may order the stay of any decision based on the results of the creditors’ meeting, provided that the remaining creditors shall not be harmed.

**Administration of the bankrupt’s estate**

The trustee may sell all assets of the debtor at auction, under the supervision of the court. The trustee shall update the court and trustee on a monthly basis and distribute the proceeds from the sale of the debtor’s assets to the creditors.

Any interested party may also submit a grievance with the court if the trustee: (1) has acted or has proposed to act unfairly, to the detriment of the interested party; (2) fails to perform its tasks with due diligence; or (3) abuses or retains any monies or properties of the debtor or breaches any other obligations to the debtor.

The Bankruptcy Law retains the two-year rule regarding ‘voidable’ or ‘fraudulent’ preferences. Consequently, all transactions made by the debtor during the two-year period preceding the initiation of bankruptcy proceedings can be reviewed by the trustee to determine whether these should be set aside as having been an ‘unfair preference’ and the Bankruptcy Law lists the types of transaction that the court will consider as representing unfair preference, including donations or gifts, payment of debts when such payments were not yet due or the creation of any new guarantee on the debtor’s properties. The court will consider whether such transaction was ‘detrimental’ to the creditors and if the transacting party knew (or ought to have known) when entering into the transaction that the debtor was in financial difficulty and, thereafter, make its judgment on whether it should be set aside.

**Effects on debtors**

As soon as a bankruptcy judgment is pronounced, the bankrupt is, with certain exceptions, prevented from administering and disposing of assets. At the request and under the supervision of the trustee, the court may give the debtor six months (extendable by two years) to sell all or part of its business, if this serves the creditors or public interest.

When a bankruptcy judgment is pronounced, all monetary debts owed by the bankrupt become payable, whether ordinary or guaranteed by lien. The court can deduct legal interest (9 per cent) for the period from the date of the judgment until the maturity date of the debt for deferred debt where no interest is stipulated. The court can grant approval to the following categories of person to purchase the debtor’s properties if that would satisfy the creditors interests: (1) spouse, relative by marriage or up to fourth degree relative; (2) any person who was a partner, employee, accountant or agent of the debtor (within two years prior to the date of judgment); or (3) any person who works or worked as the auditor following the initiation of bankruptcy proceedings.

Where a debtor owns any common properties, the trustee (or any of the co-owners) may request division of such property, even if there is an agreement between the co-owners that does not allow such division. Upon request by the trustee, the court can order the
rescission of any contract that the debtor is a party to, provided such rescission is necessary to enable the debtor to transact his or her business or if it would fulfil the interests of all of the creditors and not significantly prejudice the other contracting party’s interests.

**Effects on creditors**

Following a bankruptcy judgment, a group of creditors is established. The group of creditors consists of persons having valid claims on the bankrupt dating from before the bankruptcy judgment. The pronouncement of the bankruptcy judgment results in the suspension of individual proceedings and actions brought against the bankrupt by ordinary creditors or preferred creditors. When a bankruptcy judgment is pronounced, all monetary debts owed by the bankrupt become payable, whether ordinary or secured by a general or particular charge.

**Effects on creditors with debts secured by a chattel mortgage or lien, or by a mortgage over real property**

The names of creditors of the bankrupt who have debts secured by a chattel mortgage or lien, or by a mortgage over real property, are entered in the group of creditors with reference to the mortgage or lien, and such secured creditors enjoy priority of repayment from the proceeds of sale of the secured assets. Secured creditors shall be paid from the proceeds of the sale of the secured assets. If the sale proceeds of a secured assets do not fully satisfy the relevant secured debt, then any outstanding amount of the such debt shall be treated as ordinary debt. If the sale of the secured asset produces a surplus (after settlement of the relevant secured debt), such amount shall be for the account of the unsecured creditors.

**Preferential payments**

In the course of preventive composition or restructuring proceedings, preference is given to the following:

- **a** judicial fees or charges, or fees and costs of any appointed trustee;
- **b** fees, expenses or costs incurred due to supplying the debtor with services or to continue performance of any contract, to the extent such fees, expenses or costs are to the benefit of the business or properties of the debtor;
- **c** any non-guaranteed new finance (including the principal debt, interest, and unpaid related expenses).

In the course of bankruptcy proceedings, preference is given to the following class of debts:

- **a** any judicial fees or charges (e.g., fees of trustees and experts and expenses paid for the benefit of the common interest of the creditors to maintain or liquidate the debtor’s properties);
- **b** wages and salaries due to workers and staff for the period of 30 days prior to the declaration of bankruptcy;
- **c** debts of maintenance paid by the debtor under a judgment delivered by a competent court;
- **d** any amounts payable to governmental bodies; and
- **e** any fees, costs or expenses incurred:
  - after the date of decision of initiating procedures to procure commodities or services to the debtor, or to continue the performance of any other contract that fulfils the benefit of business or property of the debtor; or
• to continue the course of the business of the debtor after the date of initiating procedures.

The creditors in each class of debts listed above are ranked equally, unless the debtor has insufficient funds to satisfy each creditor ranking equally. In this case, the rank of debts is equally reduced. Following the payment of the preferential debts above, the holders of debts secured by pledges or liens shall be ranked higher than the ordinary creditors.

**Restitution**

Any person is entitled to restitution from the bankrupt’s estate in respect of specific items that the person can prove he or she owned at the time of the bankruptcy judgment.

**Verification and schedule of debts**

The Bankruptcy Law sets out the procedure and timetable for the verification of debts of creditors by the trustee in bankruptcy and the establishment of a final schedule of uncontested debts by the judge supervising the bankrupt’s estate.

In the case of companies, debentures issued by the same in accordance with the Commercial Companies Law are not subject to the procedures for the verification of debts. Such debentures are to be accepted at their nominal value after deduction of any amounts paid by the company.

**Closure of the bankrupt’s estate**

If the bankruptcy proceedings are halted because of insufficiency of assets prior to ratification of a judicial composition or establishment of a state of union the court may, at its own discretion or in accordance with a report from the judge supervising the bankrupt’s estate, order that the bankrupt’s estate be closed. In such instance, each creditor once again has the right to take steps and to initiate individual actions against the bankrupt.

### iii The Commercial Companies Law

The Commercial Companies Law provides for the dissolution of a company in certain prescribed circumstances. This includes, for instance, where the losses to a limited liability company amount to half of its capital whereupon the company’s manager shall ask the general assembly to consider the issue of voluntary dissolution. Similarly, if the losses of a limited liability company reach three-quarters of the capital, the shareholders holding one quarter of the capital of such company may demand to dissolve the company.

The authority of the manager or managers and the board of directors shall terminate immediate with the dissolution of the company and all debts of the company become due and owing upon an application for the company’s dissolution. If the company’s assets are not sufficient to meet all of the debts, then the liquidator is required to make proportional payment of such debts, without prejudice to the rights of preferred creditors. Every debt arising from acts of liquidation must be paid out of the company’s assets in priority over other debts.

Following settlement of all debts, the remaining assets of a limited liability company, resulting from liquidation, shall be divided among all the shareholders. Each shareholder, upon division, shall obtain an amount equal to his or her share in the capital, and the rest shall be divided among the shareholders at the pro rate of their shares in the profits.
shareholder fails to appear to collect his or her share, the liquidator shall deposit such share in
the treasury of the competent court. If the net funds of the company are not sufficient to pay
the shares of the shareholders in full, the loss shall be distributed among them in accordance
with the prescribed rate for the distribution of losses.

III RECENT LEGAL DEVELOPMENTS
The new Bankruptcy Law signals a milestone development in the insolvency regime in the
UAE, offering greater protection for debtors, and encouraging restructuring to enable troubled
businesses to survive rather than having to proceed directly to bankruptcy proceedings.

IV SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST
ACTIVE INDUSTRIES
There are limited means to gauge market trends with respect to restructuring procedures, as
generally little information is published or released with respect to businesses facing financial
difficulties. The insolvency regime set out in the Bankruptcy Law is untested. There is also
significant cultural aversion to the concept of bankruptcy, and the formal insolvency regime
is avoided for that reason as well (in addition to potential criminal penalties for managers or
directors of bankrupt businesses). As such, there is little in the way of information regarding
significant transactions or active industries.

V INTERNATIONAL
The UAE has not entered into any international treaties specifically covering insolvency
or restructuring. The Bankruptcy Law does not envisage how judicial assistance would be
provided in the UAE to proceedings commenced in another jurisdiction.

VI FUTURE DEVELOPMENTS
There are no anticipated future developments in the law applicable to the insolvency regime
in the UAE, as the Bankruptcy Law itself represents a long-awaited and comprehensive
overhaul. However, the Bankruptcy Law is still very new and its adoption, implementation,
and practical application remain largely untested. The practical application of the Bankruptcy
Law, as developed through experience, will be fundamental and must be observed closely as
it occurs.
I OVERVIEW OF RESTRUCTURING AND INSOLVENCY ACTIVITY

The news regarding the US economy remains mixed as it relates to its impact on restructuring and insolvency activity. In 2016, fourth-quarter GDP advanced at an inflation and seasonally adjusted annual rate of 1.9 per cent, marking a slowdown from a short-lived third-quarter 3.5 per cent growth spurt. In April 2017, the Labor Department reported that the US had added only 98,000 jobs in March, a sharp slowdown from the previous two months. However, the unemployment rate in the US fell to 4.5 per cent, the lowest level since May 2007.

Debt remains cheap and readily available. Accordingly, companies in distress continue to roll over and refinance their debt rather than explore court-supervised restructurings. These factors have translated into fewer bankruptcy filings. The US experienced an approximate 4.7 per cent decrease in commercial bankruptcy filings for the 12-month period ending 31 March 2017 compared with the same period ending 31 March 2016. Additionally, Chapter 11 case filings decreased by approximately 3.7 per cent over the same period. To some extent, this outcome is driven by the decline in Moody’s global speculative default rate from 4.4 per cent per cent at the end of 2016 to a trailing 12-month global speculative-grade default rate of 3.3 per cent at closing in May 2017. Moody’s expects the rate to decrease to 2.5 per cent by the end of 2017.

While there continue to be fewer bankruptcy filings, there were also fewer large bankruptcy filings than in previous years. There were some notable exceptions. Clocking in at the top was the bankruptcy filing of Avaya Inc. (Avaya), a multinational telecommunications

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1 J Eric Ivester is a partner at Skadden, Arps, Slate, Meagher & Flom LLP. Mr Ivester acknowledges and gratefully appreciates the substantial work and assistance provided by Bram Strochlic, an associate at the firm, in preparing this chapter.


7 Id.
company that provides real-time communication applications to private and government customers and platforms around the world. Avaya (and certain of its affiliates) filed for bankruptcy on 19 January 2017, with approximately US$6.5 billion in assets. Other large bankruptcies included First NBC Bank Holding Company, Memorial Production Partners LP and Vanguard Natural Resources LLC.

II GENERAL INTRODUCTION TO THE RESTRUCTURING AND INSOLVENCY LEGAL FRAMEWORK

Title 11 of the United States Code (Bankruptcy Code) governs bankruptcy cases filed in the United States.8 The Bankruptcy Code is premised on the theory that an honest debtor deserves a fresh financial start and thus relief from its unsecured debts. It endeavours to allow for this fresh start, while at the same time balancing the rights of the debtor’s various constituents as fairly and equitably as possible. Over the years, however, special interest groups have lobbied Congress for various amendments to the Bankruptcy Code. The last major amendments were contained in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (Revised Code). These amendments have continued the gradual erosion of a debtor’s ability to obtain the benefits of a fresh start and shifted the balance of power among all interested parties in a bankruptcy case, a campaign started by various special interest groups not long after the Bankruptcy Code was enacted by Congress in 1978. In addition to economic factors, these amendments have resulted in substantially fewer bankruptcy cases and, for those that do file, cases of much shorter duration.

The filing of a petition by the debtor (for corporations, this is usually a petition for relief under either Chapter 7 or Chapter 11 of the Bankruptcy Code) commences the bankruptcy case. There is no requirement that a company be ‘insolvent’ to commence a voluntary bankruptcy case. Rather, case law has developed to require only that a petition be filed in good faith. Immediately upon filing a petition, the debtor obtains the benefit of an automatic stay. The stay prohibits most creditors from taking actions against the debtor and its property on account of pre-petition liabilities or agreements without express authorisation from the bankruptcy court.9 Thus, the stay gives the debtor the necessary ‘breathing space’ to complete its reorganisation or orderly liquidation consistent with the terms of the Bankruptcy Code.

A company hoping to reorganise or liquidate with its management in place will file a petition under Chapter 11; a company with no option but to liquidate under court supervision will commence a Chapter 7 case. Banks, savings and loan associations, insurance companies, stockbrokers and commodity brokers are not eligible to file for Chapter 11 protection. In general, these types of entities are liquidated under other federal or state winding-up laws or, in the case of stockbrokers and commodity brokers, under their own sub-chapter of the Bankruptcy Code.10

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8 11 USC, Sections 101–1532.
9 The few exceptions include certain offsets under various financial contracts, taxes and the actions by certain governmental authorities who are asserting their police and regulatory powers. See 11 USC, Section 362(b).
10 Note, however, that holding companies of banks, insurance companies and brokers are eligible to file for Chapter 11 relief: thus the filings of Lehman Brothers Holdings Inc and the holding company of Washington Mutual Bank. Insurance companies are liquidated under state law procedures, which differ among the 50 states. Banks are liquidated under the Federal Deposit Insurance Act.
Unlike many other insolvency proceedings throughout the world, in a Chapter 11 case, the debtor generally continues to manage its own affairs following commencement of the bankruptcy case (referred to as a debtor-in-possession). A trustee is rarely appointed to oversee a debtor’s operations unless the situation suggests that one is necessary.

In addition to the bankruptcy court judge and the US Trustee (UST) (a representative of the Department of Justice responsible for overseeing bankruptcy cases), the debtor-in-possession’s actions will often be subject to scrutiny by one or more ‘official’ committees appointed by the UST. The most common official committee is one composed of unsecured creditors. In larger cases, the committee typically retains its own professionals (including counsel) to represent the unsecured creditors’ interests, and the debtor pays for the cost of these professionals. In some cases, equity holders or retirees will convince the UST to appoint a special committee for their constituents, especially in cases in which it appears the debtor may be solvent. Other official committees can be formed to represent other creditor groups, although such committees are rare, except in cases driven by mass torts such as asbestos liability.

The goal of a debtor in commencing a Chapter 11 case is to confirm and consummate a Chapter 11 reorganisation plan. Unless a trustee has been appointed, the debtor initially has the exclusive right to file a reorganisation plan. The exclusivity period, however, is not indefinite. Indeed, plan exclusivity can only be extended up to a maximum of 18 months after the petition date, with the court’s permission. Before 2005, when the Revised Code became law, a debtor could obtain unlimited extensions to its exclusivity period, provided authorisation was obtained from the bankruptcy court. The limit imposed by the Revised Code on plan exclusivity provides an opportunity for creditors to wait out the debtor’s exclusivity period and ultimately propose their own plan.

Before a debtor can solicit votes on its reorganisation plan, it must provide creditors with a disclosure statement that has been approved by the bankruptcy court. The bankruptcy court’s role is not to approve the contents of the disclosure statement; rather, its role is to ensure that the disclosure statement contains ‘adequate information’ to permit a creditor to make an informed decision to accept or reject the related plan. Following approval of the adequacy of the disclosure statement, the debtor may solicit votes from creditors and equity holders entitled to vote on the plan. Groups of creditors and equity holders will be categorised into different ‘classes’. If the requisite votes are received, the debtor will seek confirmation, or approval, of the plan by the bankruptcy court.

Aside from the required votes, the most critical requirement of the Bankruptcy Code for the plan is the ‘best interests of creditors test’. This test requires that each creditor either accept the plan or receive under the plan a distribution equivalent to what it would receive if

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11 USC, Section 1107.
12 11 USC, Section 1104. Fraud is the main reason a trustee is appointed.
13 11 USC, Section 1103.
14 Note that if a Chapter 11 trustee is appointed, neither the debtor nor the Chapter 11 trustee has the exclusive right to file a plan. 11 USC, Section 1121(c)(1).
15 11 USC, Section 1121(d)(2)(A).
16 USC, Section 1125(b).
17 Id. In some cases, the disclosure statement can be approved at the time the plan is approved.
18 See 11 USC, Section 1129(a)(7).
the debtor were to liquidate rather than reorganise.\textsuperscript{19} In some cases, the test requires valuation of property given to dissenting creditors. Because valuation is a complex and fact-intensive undertaking, a ‘best interests fight’ can lead to time-consuming and expensive litigation.

The second critical requirement is that at least one ‘class’ of claims votes for a plan if there is a class of impaired – or affected – claims. For this vote, the votes of insiders do not count. Two-thirds in amount and more than 50 per cent in number of creditor class members that vote must vote for the plan for the class to be deemed to have accepted the plan. In the event that equity security holders are proposed to receive a distribution, classes of equity security holders must vote for the plan by at least two-thirds in amount.

Usually, at least one class will either affirmatively reject or be deemed to have rejected the plan because that class is not slated to receive a distribution under the plan. In those cases, the debtor can confirm its plan by ‘cramming down’ these creditors or equity security holders. ‘Cram down’ requires the debtor to prove that the plan does not discriminate unfairly and is fair and equitable with respect to each class of claims or interests that is impaired under the plan and has not accepted it.\textsuperscript{20} The ‘unfair discrimination’ test is a nebulous concept. By contrast, the ‘fair and equitable’ test is more straightforward and basically follows an absolute priority waterfall, under which secured creditors are entitled to full payment (at least over time) before unsecured creditors and equity holders receive a distribution. Despite this rather simplistic concept, valuation and issues regarding the present value of future payments to secured creditors are often hotly contested.

Confirmation of a reorganisation plan provides a reorganising Chapter 11 debtor with the fresh start that most debtors hope to obtain by reorganising under the Bankruptcy Code. The discharge that the debtor receives under the Bankruptcy Code is key to the ‘fresh start’. This discharge bars creditors and equity security holders from looking to the debtor for satisfaction of claims owed to them prior to the commencement of the Chapter 11 case. Rather, their sole source of recovery is under the plan. Corporate debtors liquidating under either Chapter 7 or Chapter 11 of the Bankruptcy Code, however, do not obtain a discharge.

\section{Absolute priority rule}

A basic premise under the Bankruptcy Code is that, in the absence of consent,\textsuperscript{21} distributions to creditors must follow the ‘absolute priority rule’. In applying this rule, lower priority creditors may receive a distribution only after more senior classes are paid in full.\textsuperscript{22} Secured creditors are first in the priority scheme. Secured claims typically include pre-petition lenders and trade creditors with security interests (including holders of mechanics’ liens and materialmen’s liens). ‘Administrative expense’ claims are second in priority. Included in this bucket are claims relating to the post-petition operations of the debtor, and ‘cure’ claims that arise when debtors ‘assume’, or agree to be bound by, pre-existing contracts. The Bankruptcy Code also elevates to administrative expense priority status certain pre-petition claims of vendors of goods that would ordinarily have been treated as general unsecured claims before the enactment of the Revised Code. A Chapter 11 reorganisation plan must provide for payment of administrative expense claims and priority claims in full on the plan’s effective

\begin{itemize}
  \item[\textsuperscript{19}] Id.
  \item[\textsuperscript{20}] 11 USC, Section 1129(b)(1).
  \item[\textsuperscript{21}] Consent is obtained through the votes of classes of claims and interests.
  \item[\textsuperscript{22}] The payments may be simultaneous, provided that the senior creditor will eventually be paid the present value of their claims in full.
\end{itemize}
date, although individual creditors may agree to a payout over time. Next in order of priority come ‘priority claims’, which include certain pre-petition wages and commissions, employee benefit plan contributions, unsecured claims in connection with certain prepayments for goods or services from the debtor (e.g., the pre-petition purchase of goods ‘laid away’ with the debtor, up to a cap) and certain taxes.

General unsecured claims, in terms of priority, come after secured claims, administrative claims and priority claims, but before subordinated debt claims. Equity interests (including equity-related damage claims that are treated as equity) are lowest on the distribution ‘waterfall’ and, as a result, equity holders rarely receive a bankruptcy distribution.

ii Treatment of contracts in bankruptcy
A debtor generally has the power to hand-pick which executory contracts and unexpired leases it wants to be bound by following its reorganisation. A contract is usually found to be ‘executory’ when both the debtor and the non-debtor party to the contract have material performance obligations outstanding. If the debtor chooses to assume (or keep) a contract, it will be bound under all the terms of the agreement. Alternatively, if the debtor no longer seeks to be bound by the agreement, it will ‘reject’ it. Upon rejection of a contract, the debtor is no longer required to perform and the contract is deemed breached as of the date the bankruptcy commenced. Damages resulting from such a breach are referred to as ‘rejection damages’. Under certain circumstances, a debtor may be able to assign its interest in a contract or lease to a third party.

In the event a debtor does not assume an agreement, the default option under the Bankruptcy Code is rejection. The deadline to make the assumption or rejection decision with respect to unexpired leases and executory contracts (other than leases for non-residential real property) is the date a Chapter 11 plan is confirmed by the bankruptcy court. The deadline for a debtor to assume or reject an unexpired lease for non-residential real property can be much sooner (i.e., generally 210 days after commencement of the bankruptcy case, absent landlord consent). In a case where leased real property locations number in the hundreds, as in large retail cases, the debtor should make preliminary decisions on which leases it wants to assume or reject prior to commencing its bankruptcy case, and thereby attempt to avoid assuming leases it may not ultimately need.

iii Security interests
In the United States, Article 9 of the Uniform Commercial Code (Article 9 and the UCC, respectively), as adopted by each of the 50 states, generally applies to any security interest created by contract in personal property and fixtures securing payment or other performance of an obligation. Article 9, therefore, is the statute that sets forth the process by which one party may take and enforce a security interest in the property of another party.

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23 See, generally, 11 USC, Section 507(a).
24 11 USC, Section 365(f). See also 11 USC, Section 365(c) for additional assignment restrictions.
25 11 USC, Section 365(d)(1).
26 Each of the 50 states and the District of Columbia have adopted their own version of the UCC. All references to Article 9 contained herein are to Article 9 as set out in the model UCC. Practitioners are encouraged to refer to Article 9 as adopted in the jurisdiction relevant to each particular transaction, to consult local counsel, or do both.
There are three components to the creation and enforcement of a security interest under Article 9 – attachment, perfection and priority. Under Article 9, a security interest attaches to collateral at the moment it becomes enforceable against the debtor. Only an attached security interest may be perfected under Article 9. Perfection is the process by which a secured party gives public notice of its security interest in collateral. A perfected security interest will prevail over claims of an interest in collateral by other parties (including liens of creditors using the judicial process to obtain liens on the collateral). State law, generally uniform throughout the United States, will dictate the method for perfecting a consensual security interest.

In many cases, two or more creditors may have security interests in the same collateral. In such cases, Article 9 provides general rules as to the ranking of security interests – that is, which security interest takes priority over the others. As a general rule, an earlier-secured party will prevail over later-secured creditors. There are, however, exceptions to this general rule and, therefore, practitioners must refer to Article 9 in the applicable jurisdiction relevant to a particular transaction or consult local counsel.

Article 9 has a critical interplay with the Bankruptcy Code. Upon the bankruptcy filing, the debtor steps into the role of a ‘hypothetical lien creditor’. This means, in general, that it may void any unperfected security interest. Accordingly, it is critically important for secured creditors to ensure that their liens are properly perfected, especially when transacting business with a distressed company on the verge of bankruptcy. Again, while there are some variations in the details, security interests are usually ‘perfected’ by filing in a governmental registry or by taking possession of the collateral.

Whereas the UCC, which deals with the creation of security interests in personal property, is fairly uniform as adopted in all 50 states, security interests or mortgages in real property are controlled by different laws in each of the 50 states. However, most state laws provide for the recording of mortgages in local governmental offices. As with security interests in personal property, a bankruptcy trustee or debtor-in-possession can avoid improperly recorded mortgages by stepping into the shoes of state-law creditors.

iv  Clawback actions

The Bankruptcy Code gives a debtor certain ‘avoidance powers’ to recover property transferred by the debtor to third parties before the petition date. Generally, these avoidance actions fall into two categories: the transfers had the effect of preferring one creditor over others; or the transfers were made for the purpose of hindering, delaying or defrauding creditors from collecting on their claims.

‘Transfer’ is defined broadly and encompasses payments as well as the granting and perfection of liens. Transfers that the debtor can prove to be fraudulent or preferential can be treated as voidable transfers. In many instances it is unnecessary to prove that the debtor or the recipient, or both, had a wrongful motive – the Bankruptcy Code is concerned only with ensuring equal treatment of creditors, even if that means unwinding well-intentioned arm’s-length transfers of property. That said, the recipient of a voidable transfer has certain affirmative defences to shield all or a portion of the transfer from the debtor.

The most common voidable transfer is referred to as a ‘preference’. Preferences are those payments a debtor makes to a pre-petition creditor on the ‘eve’ of the bankruptcy filing. 28

27 See 11 USC, Section 544.
28 The reach-back period is generally 90 days, unless the transferee is an ‘insider’ of the debtor, in which case the reach-back period is one year.
that allow such creditor to receive more on account of its claim than it would have received had it waited in line with other creditors and received its distribution in a liquidation of the debtor pursuant to Chapter 7 of the Bankruptcy Code. The amount the creditor received in connection with the transfer will be voidable, subject to certain defences, although the net economic impact to the creditor (after negotiations with the trustee or debtor) will generally be a return of money in excess of the hypothetical liquidation distribution. To the extent the transfer is avoided, the preference recipient would have a claim against the debtor.

Fraudulent transfers that can be recovered include transfers made with the actual intent to hinder, delay or defraud creditors. Recoverable fraudulent transfers also include transfers for inadequate consideration when the debtor (transferor) is insolvent, undercapitalised or was unable to pay its debts as they became due. The Bankruptcy Code has its own fraudulent transfer provisions, but the debtor-in-possession may also prosecute such claims under similar state law provisions.

III SIGNIFICANT TRANSACTIONS, KEY DEVELOPMENTS AND MOST ACTIVE INDUSTRIES

i Pre-planned bankruptcies: a quick escape from an all-out bankruptcy

Pre-planned bankruptcies continue to be a useful tool for debtors as they try to manage the time and expense of a US bankruptcy filing. There are two types of pre-planned bankruptcies: pre-packaged and pre-negotiated bankruptcies. Pre-packaged bankruptcies (pre-packs) are typically utilised by companies seeking to right-size their capital structures (e.g., to address maturities or deleverage from existing secured lender or bondholder indebtedness). The pre-packaged bankruptcy mechanism is not useful for companies seeking to achieve an operational turnaround or that need to modify other significant liabilities such as pension, retiree medical or mass tort liabilities.

In a pre-pack, the Chapter 11 case is commenced after the plan proponent has obtained the requisite votes to approve a reorganisation plan. In pre-negotiated plans, the creditors entitled to vote on the plan indicate their support for the plan before the commencement of the case, often in the form of a ‘lock-up’ agreement, but the vote occurs following the commencement of the case. It is common for pre-packs to last less than 60 days. Absent complications, pre-negotiated bankruptcies will take 45 to 60 days longer than a pre-pack. These periods are far shorter than the duration of traditional Chapter 11 cases.

The pre-pack concept is an important negotiation tool as companies attempt to obtain concessions from their constituents. The requirement to achieve an accepting class of creditors (and, therefore, to bind non-accepting class members) under the Bankruptcy Code is two-thirds in amount and one-half in number of those creditors who cast a vote. If acceptance is received from almost all of the creditors from whom votes are solicited, companies will often consummate the restructuring without filing for bankruptcy. Moreover,

29 11 USC, Section 1125(g) of the Bankruptcy Code provides that an acceptance or rejection of the plan may be solicited from a holder of a claim or interest before the commencement of the case, provided that such solicitation complies with the applicable non-bankruptcy law.

30 The Bankruptcy Code requires that two-thirds in amount and more than one-half in number of a class of creditors vote to accept a plan for that class of creditors to be deemed to have accepted the plan. 11 USC, Section 1126(c).
the threat of a pre-pack makes it less likely that a filing will be required, because there is little reason for creditors to withhold their acceptance once the company has received acceptances sufficient to satisfy the minimum threshold for an accepting class in the Chapter 11 context.

This past year has seen numerous headline pre-negotiated and pre-packaged bankruptcy filings and exits. For example, Roust Corporation, a vodka manufacturer in Poland and Russia, filed for Chapter 11 on 30 December 2016 with a pre-packaged plan to reorganise approximately US$1.14 billion of debt. The plan was confirmed on 6 January 2017 and went effective on 17 February 2017. Notably, because Roust Corporation had provided the required notices before it filed for bankruptcy, the company’s plan of reorganisation was confirmed within six days of its Chapter 11 filing.

ii Active industries: retail

In 2017, the convenience and pervasiveness of online shopping took a significant toll on the retail industry, leading to near-record numbers of bankruptcy filings by major retail chains. By April 2017, the number of major retailers that filed for bankruptcy in 2017 surpassed the total number of retail companies that filed for bankruptcy during all of 2016, putting 2017 on pace to surpass the record of 18 major retail bankruptcies that were filed in 2009. Major retail chains that filed for bankruptcy in 2017 as of the date of this publication include Gordmans, hhgregg, RadioShack (General Wireless Operations Inc), Gander Mountain, BCBG Max Azria, MC Sports, Eastern Outfitters, Wet Seal, The Limited, Payless Inc., Rue21, and Gymboree. According to Bloomberg, citing to an analysis by S&P Global Market Intelligence, department stores, electronics stores, and apparel stores are at highest risk for filing for bankruptcy protection in 2017, while the food and home improvement segments are at lower risks.

iii Case law developments

Puerto Rico debt restructuring

In June 2016, the US Supreme Court upheld certain lower court decisions that declared unconstitutional a Puerto Rican law aimed at restructuring the territory’s debt. In Commonwealth v. Franklin Cal. Tax-Free Tr., the Supreme Court reasoned that Chapter 9 of the Bankruptcy Code (dealing with bankruptcies by municipalities) pre-empted the proposed Puerto Rican law, as Chapter 9 declares any ‘State’ law aimed at restructuring a municipality’s debt to be invalid. However, territories like Puerto Rico are not eligible to utilise Chapter 9 bankruptcy protections because they are not strictly municipalities, which left Puerto Rico without a judicial option with which to restructure or otherwise manage its growing debt.

To fill this gap, Congress passed and President Obama signed into law the Puerto Rico Oversight, Management, and Economic Stability Act (PROMESA) on 30 June 2016. The law establishes a seven-member Oversight Board that has broad latitude to supervise any fiscal plans and budgets that the government of Puerto Rico develops to ensure that such
plans satisfy predetermined criteria. Under PROMESA, local Puerto Rican governmental entities are still responsible for drafting specific fiscal plans and budgets, but any proposed measures are subject to revision by the Oversight Board.

PROMESA also establishes a framework to restructure debt issued by the Puerto Rican government. Under Title VI, the law establishes a collective action restructuring process, and under Title III, the law establishes a process similar to that which is available to municipalities under Chapter 9 of the Bankruptcy Code. On 3 May 2017, Puerto Rico filed to restructure its general obligation debt under Title III, followed by Puerto Rico’s sales tax authority filing for relief under Title III a few days later. The two filings have been combined and account for approximately US$36 billion, roughly half of Puerto Rico’s total debt. As of June 2017, both in-court proceedings and restructuring negotiations remain ongoing.

**Structured dismissals**

The US Supreme Court has recently narrowed the grounds on which structured dismissals may be approved. In a 6-2 decision in *Czyzewski v. Jevic Holding Corp.*, the Court found that structured dismissals must abide by the priority scheme set forth in the Bankruptcy Code, unless otherwise approved by the affected creditors.34

Many times, Chapter 11 is used as a means by which to sell assets free and clear of liens or security interests with such liens and security interests to attach to the proceeds.35 After consummation of the sale, a debtor can either confirm a plan of reorganisation or liquidation or liquidate under Chapter 7 of the Bankruptcy Code. Since these options can be time consuming and costly, ‘structured dismissals’ of such bankruptcy cases have been used with increasing frequency. Bankruptcy courts often introduce new elements in a dismissal. In *Czyzewski v. Jevic Holding Corp.*, the Court articulated that while the Bankruptcy Code does not explicitly require adherence to the priority rules in a structured dismissal context, bankruptcy courts may only approve settlements that follow such priority rules contained in other parts of the Bankruptcy Code.

Jevic is a trucking company that filed for bankruptcy pursuant to Chapter 11. The debtor was found to have violated certain of its employees’ termination notification rights under the Worker Adjustment and Retraining Notification Act (WARN) and, accordingly, such employees had a claim equal to US$1.7 million that was entitled to priority under the Bankruptcy Code. Fraudulent-transfer claims against Jevic’s senior secured lenders were resolved whereby such lenders agreed to a US$3.7 million settlement payment provided that the bankruptcy case was dismissed pursuant to a structured dismissal whereby the employees’ WARN Act claims would not be paid even though the claims of junior creditors would receive payment.

The Supreme Court struck down the lower courts’ approval of this settlement arrangement, asserting that it violated the Bankruptcy Code’s priority system. Indeed, had there been a settlement with the lenders but no dismissal, and had the settlement proceeds been distributed under a plan or in a Chapter 7 liquidation, the workers’ priority claims would have entitled them to US$1.7 million. Had there been no settlement but rather a straight dismissal or conversion, the fraudulent-transfer claims against the senior creditors would have re vested in the workers or become an asset of the Chapter 7 bankruptcy estate, respectively.

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35 See 11 USC, Section 363.
The decision emphasised that structured dismissals could not be used as a workaround designed to achieve results that would not be possible under alternative liquidation mechanisms. The Court found that the priority scheme is a fundamental element of the Bankruptcy Code, and that it would be improper to read in an exemption for structured dismissals to those rules without an explicit statement by Congress or any evidence of legislative intent. As a result, the decision in *Jevic* will likely reduce the popularity of structured dismissals and cause more cases to end in liquidation.

**Noteholder protections**

Section 316(b) of the Trust Indenture Act of 1939 (TIA) provides qualified noteholders with a consent right over any changes to the payment terms or the ability to sue to enforce payment of an indenture. This provision gives minority bondholders protection from any non-consensual changes to the terms of the debt security that would otherwise be favoured and implemented by the majority bondholders. Since 1939, Section 316(b) has almost universally been interpreted to provide protection only to actual alterations to the payment terms or the bondholder's right to sue. However, in *Marblegate Asset Management LLC v. Education Management Corp.*, the District Court for the Southern District of New York held that the statute protected the noteholder’s ‘practical ability’ to receive payment, an interpretation that would broadly expand the scope of 316(b) protection from merely actual changes to payment terms to any transaction that could affect whether a noteholder could be paid back the debt on its notes. The District Court in *MeehanCombs Global Credit Opportunities Funds, LP v. Caesars Entertainment Corp.* reached a similar conclusion. The transaction at issue in the *Marblegate* case involved a restructuring in which the secured creditors released the guaranty of their debt by Education Management Corp., which triggered a similar release of the Education Management Corp.’s guaranty of its unsecured notes. The holders of the unsecured notes argued that this arrangement impaired the ‘practical ability’ of the noteholders to collect payment on the bonds, and as such was a violation of Section 316(b) of the TIA. Though the arrangement did not actually change the payment terms of the indenture or the ability of the bondholders to sue, the District Court agreed with this broad interpretation of the TIA.

The Second Circuit reversed the lower court’s interpretation. The Second Circuit asserted that there is no absolute right to repayment under the statute, and, additionally, that there would be no uniform way to apply the lower court’s ‘practical ability’ standard. Instead, that standard would force courts to determine what implicates an issuer’s ‘practical ability’ to repay its bonds on a subjective and case-by-case basis. Because the Second Circuit did not find that the TIA created an absolute right to repayment, and the transaction at issue did not change any of the terms of the indenture or impair any noteholder’s right to bring a lawsuit, the District Court found that the transaction was not in violation of Section 316(b) of the TIA, and effectively reinstated the narrower interpretation of the provision.

The District Court’s reading of Section 316(b) of the TIA was potentially devastating to an issuer’s ability to achieve an out of court restructuring because almost all restructurings will have an effect on a dissenting bondholder’s ‘practical ability’ to receive repayment and,

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therefore, would require unanimous bondholder consent. Many authors were pondering whether a bankruptcy filing would be required to complete all restructurings that were not truly consensual. The Second Circuit’s reversal likely allays most of those fears – at least for now – and returns the law and practice to its pre-Marblegate status.

IV INTERNATIONAL

i Background on Chapter 15

In 2005, Congress added Chapter 15 to the Bankruptcy Code. Chapter 15 ‘incorporates the Model Law on Cross-Border Insolvency to encourage cooperation between the United States and foreign countries with respect to transnational insolvency cases’. Chapter 15 is based on a ‘rigid recognition standard’ that one court labelled ‘consistent with the general goals of the Model Law’. Thus, if a US bankruptcy court denies recognition of a foreign proceeding, Section 1509(d) of the Bankruptcy Code provides that ‘the court may issue any appropriate order necessary to prevent the foreign representative from obtaining comity or cooperation from courts in the United States’. This has been interpreted to mean that Chapter 15 recognition is now the sole form of relief in the United States with respect to foreign insolvency proceedings.

A foreign representative can obtain recognition under Chapter 15 of the Bankruptcy Code ‘by the filing of a petition for recognition of a foreign proceeding under Section 1515’. Two types of recognition of a foreign proceeding are possible under Chapter 15: recognition as a foreign main proceeding or recognition as a foreign non-main proceeding. Greater relief is available to a foreign representative of a foreign main proceeding than for a representative of a foreign non-main proceeding.

In order for a US court to recognise a foreign proceeding as a main proceeding, the foreign proceeding must be ‘pending in the country where the debtor has the center of its main interests’, (COMI). COMI is not defined in Chapter 15. Section 1516(c), however, sets out a presumption that the debtor’s registered office is the COMI ‘in the absence of evidence to the contrary’. Moreover, one of the first bankruptcy decisions to analyse the matter defined a company’s COMI as a debtor’s ‘principal place of business’ under concepts of United States law. Indeed, the concept of COMI is lifted from the EU Regulation, which defines COMI as ‘the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties’. On the other hand, the Second Circuit has rejected the notion that ‘principal place of business’ analysis should be used.
but did note that the concept is still useful in determining the factors that point to a COMI. The court went on to say that ‘any relevant activities, including liquidation activities and administrative functions, may be considered in the COMI analysis’.49

The Second Circuit also provided more guidance in determining the relevant period to examine in establishing a debtor’s COMI, concluding that the relevant analysis should be based on the debtor’s activities at or around the time the Chapter 15 petition is filed [...] but that a court may consider the period between the commencement of the foreign insolvency proceeding and the filing of the Chapter 15 petition to ensure that a debtor has not manipulated its COMI in bad faith.50

Lacking the required COMI, a foreign proceeding may be recognised as a non-main proceeding under Chapter 15 if the foreign proceeding is ‘pending in a country where the debtor has an establishment’.51 ‘Establishment’ is defined in Chapter 15 as ‘any place of operations where the debtor carries out a nontransitory economic activity’.52 Determining whether a debtor has an establishment in the foreign proceeding jurisdiction ‘is essentially a factual question, with no presumption in its favour’.53 At least one court has held that non-main recognition is restricted to a jurisdiction in which a debtor has assets.54

ii Recent developments

In re Hanjin Shipping Co Ltd

The recent Hanjin Shipping Co Ltd (Hanjin) insolvency provides an interesting example of the practical application of Chapter 15. Hanjin was the largest shipping company in South Korea and the world’s ninth-largest shipper. After experiencing an extreme liquidity crisis, on 31 August 2016, Hanjin filed for protection under the Debtor Rehabilitation and Bankruptcy Act in the Seoul Central District Court of South Korea. At the time of its filing, eight of Hanjin’s vessels were arrested in port, 43 vessels were at sea, 39 vessels were outside ports waiting for some indication that they would not be arrested, and many other vessels were stopped and unable to pass through the Panama or Suez Canal. At the time of the filing, among other things, Hanjin’s vessels were carrying vital components for manufacturers such as HP and Samsung Electronics which were in the process of building inventory for the upcoming holiday season.

Despite the protections afforded by the Korean proceeding, Hanjin feared that its creditors would file enforcement actions in other countries, including the United States. To stave of such risk and to ensure that its shipping routes to the United States would not be adversely impacted, Hanjin’s foreign representative filed a Chapter 15 case in the Bankruptcy Court for the District of New Jersey on 2 September 2016. In the Chapter 15 case, Hanjin sought an order recognising the Korean proceeding and applying Sections 362 and 365 of the Bankruptcy Code to the Chapter 15 case in order to protect Hanjin’s assets in the United

49 Id. at *8.
50 See Id. at *8.
51 11 USC, Section 1502(5).
52 Id. Section 1502(2).
53 In re Bear Stearns, 389 BR at 338.
54 Id. at 339 (‘In general, Section 1521(c) of the Bankruptcy Code limits the scope of relief available in a nonmain proceeding to relief related to assets located in the nonmain jurisdiction or closely connected thereto, while a plenary bankruptcy proceeding where the [debtors] are located would control the [debtors’] principal assets’).
States and prevent contract counterparties from modifying or terminating related contracts. On 9 September 2016, the bankruptcy court entered an order for preliminary relief implementing a stay against the assertion of maritime liens and the seizure of vessels, and providing cargo owners with additional negotiation rights. Without this provisional relief, which was later affirmed when the US bankruptcy court entered the final recognition order on 13 December 2016, and the broad protections contemplated thereby, Hanjin’s idled ships would have not been able to dock at US ports and resume normal business activities. The Hanjin filing thus demonstrates the utility of Chapter 15 in stabilising the US operations of international companies that face seemingly overwhelming logistical challenges during the pendency of a foreign bankruptcy proceeding.

In re Sanjel (USA) Inc

In In re Sanjel (USA) Inc, the Bankruptcy Court for the Western District of Texas provided some guidance as to whether a bankruptcy court may properly modify or limit a stay imposed in a foreign bankruptcy proceeding by modifying language in the recognition order giving effect to such stay in the United States. In this case, Sanjel (USA) Inc, an energy services provider, and certain affiliates (Sanjel) commenced reorganisation proceedings in Canada under the Companies’ Creditor Arrangement Act (CCAA). In that proceeding, the Canadian court approved a broad stay which shielded Sanjel’s directors and officers from litigation. In the Chapter 15 case that followed, the US bankruptcy court entered a recognition order that enforced the broad Canadian stay of litigation against Sanjel’s directors and officers, which is not generally within the scope of the automatic stay under the Bankruptcy Code. Critically, this recognition order would have barred certain of Sanjel’s US employees who sought to bring actions against Sanjel’s directors and officers for unpaid wages, and because the statute of limitations for those actions would continue to run during the course of the Chapter 15 proceeding, such claims would likely be extinguished if the broad Canadian stay were enforced domestically.

Accordingly, two of Sanjel’s employees requested that the bankruptcy court modify the stay in the recognition order. Sanjel argued that the Canadian stay should not be modified, as any such modification would be a distraction for the directors and officers and prevent them from devoting their full attention to the restructuring. Such arguments against modifying the stay were similar to those that ultimately prevailed in In re Nortel Corp, a case before the United States Bankruptcy Court for the District of Delaware; in that case, the bankruptcy court held that any parties asserting prejudice because of the Canadian stay should request relief in the Canadian forum, rather than through a modification to the US recognition order.

Departing from the holding in In re Nortel Corp, the bankruptcy court in this case held that Section 1522(a) of the Bankruptcy Code permits a US bankruptcy court to modify a recognition order in order to narrow the stay enforced therein, provided that ‘the interests of the creditors and other interested entities, including the debtor, are sufficiently protected.’ Accordingly, the court undertook an analysis of the balance of hardships; if such balance lay

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55 Order granting provisional relief pursuant to Sections 362, 365(e), 1519, 1520 and 105(a) of the Bankruptcy Code pending hearing on petition for recognition as a foreign main proceeding, In re Hanjin Shipping Co Ltd, 16-27041 (Bankr. D.N.J., September 9, 2016), ECF 102.
with the creditors seeking relief, then the recognition order (and the underlying stay) could be modified. Here, the court held that the hardships of the movants outweighed those of the debtor, and therefore modified the recognition order to limit the Canadian stay in the United States, thus allowing the employees to pursue their claims against the directors and officers. As part of this holding, the court emphasised that it would be unduly burdensome to require the employees to seek relief from the stay in the Canadian court where the claims they sought to assert were fully based on statutory rights created by United States law to protect employees within the United States.
Appendix 1

ABOUT THE AUTHORS

BEATRIZ ALBORS CANO

_Uría Menéndez_

Beatriz Albors is a lawyer in the Madrid office of Uría Menéndez. She joined the firm in 2015 and she specialises in restructuring and corporate matters, above all in advising debtor companies, credit institutions and distressed investors on out-of-court refinancings and restructurings, as well as on in-court insolvency proceedings. In addition, she also has expertise in M&A and litigation.

KRISTIAN GUSTAV ANDERSSON

_Lundgrens_

Kristian Gustav Andersson is a partner with Lundgrens and works primarily with corporate commercial law and insolvency law, focusing in particular on mergers and acquisitions, restructurings and reorganisations. He has a master’s degree in law from Copenhagen University and also holds an LLM degree in corporate commercial law from King’s College, London.

Mr Andersson has worked on several (including some of the highest profile) insolvency and reconstruction cases, and his experience encompasses corporate restructuring, refinancing and corporate turnarounds, receivership and liquidation. He is a member of the Danish Association for Banking and Finance Law.

Lundgrens’ highly-experienced reconstruction and insolvency department is headed by Kristian Gustav Andersson, who is ‘a rising star within high-profile bankruptcy cases’. Kristian Gustav Andersson is ranked in _Chambers Europe 2017_ as ‘Up and Coming’.

JESSICA ARSCOTT

_Gilbert + Tobin_

Jessica Arscott is a senior associate in Gilbert + Tobin’s restructuring and insolvency group. She specialises in non-contentious restructuring and insolvency work for banks, insolvency practitioners, special situation groups, distressed debt funds, debtors and company directors. Her experience includes preparing forbearance and restructuring documentation; debt restructuring, DOCAs and schemes of arrangement; structured administration and receivership sales; sale and purchase of distressed assets; the Personal Property Securities Act 2009 (Cth); all aspect aspects of security enforcement; and advice to directors, creditors,
receivers, administrators and liquidators. She also has considerable front-end finance experience.

Recent matters include the Slater and Gordon restructure, the Ten Network Holdings administration, the BIS Industries Group restructure, the Arrium administration and Molycop sale, the Emeco restructure, the Triton Minerals Limited administration and restructure, the Mintails Limited administration and restructure, advising receivers appointed to the Parklea Markets and related assets, the Brisconnections receivership and sale of Airport LinkM7, the Eastmark administration and deed of company arrangement, advising a fund in connection with its bid to purchase GE’s leveraged finance book, advising Atlantic Limited in connection with its recapitalisation and associated standstill arrangements, advising Westpac on its $1.45 billion acquisition of Lloyds Banking Australia business, advising funds in relation to the bid to purchase JP Morgan's Global Special Opportunities Group's book, advising a major Australian bank in connection with all workout arrangements in respect of its exposure to a major Western Australian property developer and advising secured lenders and receivers appointed to two power plants located in NSW held by the Sunshine Electricity Joint Venture, an unincorporated joint venture.

Ms Arscott is a member of the Australian Restructuring Insolvency and Turnaround Association and the Turnaround Management Association.

ANNE BACH
Görg Partnerschaft von Rechtsanwälten mbB

Dr Anne Bach (née Laspeyres) is an associate in Görg’s restructuring and insolvency group. She obtained a degree in law in 2009 and her PhD in 2013, both from the University of Mannheim. She was admitted to the Bar in 2013. Mrs Bach’s work encompasses both advising companies and managing directors in insolvency and pre-insolvency matters. She has been involved, together with Christian Bärenz, in high-profile restructuring cases, such as Lehman Brothers and HETA/Hypo Alpe Adria, and regularly acts for foreign clients and in cross-border cases. Mrs Bach is a member of the German Bar, the German-French Jurists Associations, the German-Belgian Lawyers Association and INSOL Europe.

CHRISTIAN BÄRENZ
Görg Partnerschaft von Rechtsanwälten mbB

Dr Christian Bärenz is a partner at Görg and a member of the firm’s restructuring and insolvency group. His practice includes all aspects of insolvency and restructuring law, with a special focus on distressed mergers and acquisitions, cross-border cases and complex group insolvencies and restructurings. He regularly acts for (foreign) court-appointed insolvency administrators, and has been involved in numerous high-profile restructuring cases both in and out of court, including AgfaPhoto, HP Pelzer, Heidelberg Cement, Merckle, ATU Group, Lehmann Brothers and HETA/Hypo Alpe Adria. He is a member of the German Bar, INSOL Europe, INSOL International and the American Bankruptcy Institute. Mr Bärenz has regularly published on restructuring and insolvency topics.
CARL BRODÉN
Roschier Advokatbyrå AB

Carl Brodén is a member of the firm’s finance and restructuring practice in Sweden and focuses on restructuring and insolvency. He acts for both debtors and creditors in cross-border restructurings as well as in local Swedish in and out-of court restructurings. Prior to joining Roschier, Mr Brodén held the position of Head of Trustee Services at one of the leading Nordic trustees and has extensive experience of restructurings of high-yield bonds. He is a member of the insolvency section of Stockholm Centre for Commercial Law and regularly lectures at the Stockholm University and the University of Uppsala.

JAMES BOWDEN
Afridi & Angell

James Bowden joined Afridi & Angell in 2006 and, after leaving the firm in 2009 for two years, he rejoined in 2011. He became a partner in 2014. He advises clients on a broad range of corporate, commercial, employment and compliance matters, focusing on M&A and restructuring.

From 2009 to 2011, Mr Bowden worked as in-house counsel with one of Canada’s leading technology outsourcing companies where he gained in-depth technology outsourcing experience.

Prior to joining Afridi & Angell, Mr Bowden practised in Canada, in the Toronto office of a global law firm. He is admitted to the Ontario Bar.

ROSNA CHUNG
Hutabarat, Halim & Rekan

Rosna Chung is a partner at Hutabarat Halim & Rekan and leads the banking and finance and capital markets and securities practice groups. In addition, her areas of specialisation also encompass real property and land; corporate matters and foreign investment; mergers and acquisitions; and insolvency.

Ms Chung is a member of the Indonesian Association of Capital Market Legal Consultants and is licensed as a capital market legal consultant. She is also a licensed advocate and a member of the Association of Indonesian Advocates. In addition, Ms Chung is a licensed receiver and administrator, and is a member of the Indonesian Receiver and Administrator Association. In the international sphere, she is a member of INSOL International and IR Global.

NAIR MAURÍCIO CORDAS
Uría Menéndez – Proença de Carvalho

Nair Maurício Cordas joined Uría Menéndez – Proença de Carvalho as a trainee lawyer in September 2012 and became a junior associate in September 2014. Ms Cordas graduated in law from the University of Lisbon and has completed her master’s degree course in business law at the same university.
RAHAT DAR  
Afridi & Angell  

Rahat Dar is a senior associate at Afridi & Angell’s Dubai office. His practice includes banking and finance, M&A and general corporate matters. Mr Dar has advised companies and financial institutions on a range of financing transactions, including conventional and Islamic finance.

Prior to joining Afridi & Angell, Mr Dar was a corporate associate in the London offices of two leading law firms. Mr Dar is a member of the Law Society of England and Wales and has co-authored the UAE chapter of the Chambers banking and finance guide.

BART DE MOOR  
Strelia  

Bart De Moor is a partner at Strelia, registered with the Dutch-speaking Brussels Bar and has more than 25 years of experience in insolvency law and conflict resolution. He was a partner at Taylor Wessing and Laga for several years. His practice covers insolvency law in the broadest sense, securities and the rights of creditors. Mr De Moor’s dispute resolution focus is mainly on insolvency law and tort law. He was appointed as liquidator or as administrator in some of the largest reorganisations and bankruptcies in Belgium. Furthermore, he is an invited professor at the Faculty of Economics and Management of the University of Leuven in Belgium.

TIZIANA DEL PRETE  
Grimaldi Studio Legale  

Tiziana Del Prete is a partner at Grimaldi Studio Legale. Ms Del Prete specialises in M&A, corporate and commercial law, and works extensively in the fields of corporate restructuring and turnaround, identification of best practices in corporate governance, acquisitions and transfers of shares, businesses or going concerns, joint ventures, and drafting and negotiation of sales and shareholder agreements.

Ms Del Prete is a legal advisor for major Italian and international corporations and private equity funds for Italian investments.

After graduating in law magna cum laude at the University of Rome in 1989, she attended the specialisation course on international business law at the University of Paris from 1992 to 1993.

She was admitted to practise law in Italy in 1993 and is a member of Rome Bar Association.

ALOK DHIR  
Dhir & Dhir Associates  

Alok is the founder and managing partner of Dhir & Dhir Associates, a leading full service law firm in India. He is a qualified chartered accountant and lawyer with over three decades’ extensive experience in corporate, commercial and civil laws with special focus on corporate and financial restructuring, insolvency laws, mergers and acquisitions, takeovers, banking law, real estate, PE placements, structuring of transactions, the turning around of financially-stressed entities in the country and issues related to asset reconstruction and
securitisation. He is a veteran in advising corporate entities in distress and formulating plans for their revival.

He is also one of the first few insolvency professionals registered under the Insolvency and Bankruptcy Code 2016. He has founded IRR Insolvency Professionals Private Limited, which is the first insolvency professional entity formed and is licensed by the Insolvency and Bankruptcy Board of India (IBBI).

He has been a member of the NCLT Rules Formulating Committee and also co-opted as a member on the National Committee on Dispute Resolution by CII and has been appointed by the Indian Institute of Corporate Affairs (IICA) on the panel of experts for the subject relating to corporate rescue and asset reconstruction. He is also a member of the core group on insolvency laws of the FICCI. He has been recently appointed by the IBBI as a member of a working group constituted to strategise the approach for implementing the IBC 2016 and drafting rules and regulation for corporate guarantors and individuals with businesses. He serves as a member of the Grievance Redressal Committee with the ICSI Insolvency Professionals Agency.

He has been consistently recognised as the leading lawyer for restructuring and insolvency in the country by most global credited rankings for legal services. He is currently advising a large number of stakeholders in cases that are undergoing a CIRP.

PHILIPPE DUBOIS
De Pardieu Brocas Maffei AARPI

Philippe Dubois has considerable experience in restructuring and insolvency. He advises banking and financial institutions as well as large French and foreign industrial groups in a wide range of economic sectors. His practice focuses on restructuring, litigation and arbitration in diverse areas such as shareholder disputes, indemnification agreements and liabilities.

He manages the firm’s restructuring and insolvency, dispute resolution and arbitration teams.


Philippe Dubois is recognised as ‘Lawyer of the Year’ in Restructuring by Option Droit & Affaires magazine (2015).

Recent transactions include: Thomson-Technicolor (advising Thomson-Technicolor on the restructuring of the group); Ascométal (advising a group of French and European investors in connection with their successful takeover bid for Ascométal group, which was approved by the Commercial Court of Nanterre); Groupe Partouche (advised cross-holder lenders of Financière Partouche and Groupe Partouche in connection with the safeguard proceedings); Latécoère (representing one of the major lenders in the framework of a court-approved restructuring agreement); Alma Consulting Group (representing the senior lenders in the context of the first debt-equity swap implemented through accelerated safeguard proceedings); Bata (representing Bata in the context of its rehabilitation proceedings and its court-ordered sale plan; Fram (representing the senior lenders in the context of Fram’s debt restructuring followed by its acquisition by LBO France through a pre-packed sale plan in rehabilitation proceedings); SNCM (representing SNCM in the context of its rehabilitation proceedings and its court-ordered sale plan); Vivarte (representing a group of lenders); Camaïeu (representing a group of lenders in the context of its court-approved restructuring agreement); and
Financière Turenne Lafayette, holding company of William Saurin (representing the biggest group of lenders – ongoing).

DOMINIC EMMETT
Gilbert + Tobin
Dominic Emmett heads the restructuring and insolvency group at Gilbert + Tobin and brings nearly 30 years of significant local and international experience.

Mr Emmett specialises in non-contentious restructuring and insolvency work for banks and financial institutions, as well as special situation groups and distressed debt funds. His expertise includes preparing and negotiating standstill and forbearance arrangements; debt restructuring and schemes of arrangement; structured administration and receivership sales; and advice to directors, receivers, administrators and liquidators.

He is recognised as a leading restructuring and insolvency lawyer in numerous publications, including leading directories such as Chambers, The Legal 500 and IFLR1000. Best Lawyers Australia 2015 recently listed him as a leading lawyer in the areas of insolvency and reorganisation, distressed investing and debt trading and banking and finance. He is also consistently recognised by Best Lawyers as a Lawyer of the Year, most recently in Best Lawyers 2017, which awarded him their Sydney Distressed Investing & Debt Trading Lawyer of the Year accolade. He was nominated at the 2011 ALB Law Awards for Dealmaker of the Year, and in 2008, 2009, 2011, 2014, 2015 and 2016 was part of the teams that won the ALB Law Award for Restructuring and Insolvency Deal of the Year, and in 2013 the ALB Law Award for Australian Deal of the Year. Recently he led the team on the Slater & Gordon restructure, Boart Longyear restructure, BIS Industries Group Restructure, Arrium administration and Molycop sale, Emeco restructure, Atlas Iron restructure, Brisconnections receivership and sale of Airport LinkM7, Billabong, Mirabela Nickel restructure and Nine Entertainment Group restructure.

HEINRICH FOGLAR-DEINHARDSTEIN
Cerha Hempel Spiegelfeld Hlawati Rechtsanwälte GmbH
Heinrich Foglar-Deinhardstein (born 1978) is a partner at Cerha Hempel Spiegelfeld Hlawati Rechtsanwälte GmbH with its headquarters in Vienna and several offices in CEE.

He studied Law in Austria (Mag iur in 2002) and at the King’s College in London (LLM 2005).

Heinrich Foglar-Deinhardstein was admitted as attorney-at-law in Austria in 2009 and became a partner at CHSH in 2013. He specialises in corporate law, insolvency and restructuring, cross-border M&A, corporate acquisitions, takeovers, squeeze-outs and foundations as well as in restructurings and reorganisations.

GABRIELA MARTINES GONÇALVES
TozziniFreire Advogados
A senior associate in the restructuring and insolvency and corporate litigation areas in TozziniFreire Advogados, Gabriela Martines Gonçalves has a law degree from Mackenzie Presbyterian University, holds a specialisation in corporate law from Fundação Getúlio Vargas and studied an introduction to the US legal system at Fordham University School of Law in New York.
JOANNA GUMPELSON

De Pardieu Brocas Maffei AARPI

Joanna Gumpelson is a partner within De Pardieu Brocas Maffei’s restructuring and insolvency department. Her main areas of expertise are insolvency proceedings and debt restructuring. She represents French and foreign investment funds, banks, as well as bondholders or suppliers, etc. She also regularly represents French or foreign issuers, in particular, in the context of failing LBOs.

She also handles – jointly with partners of the litigation group – commercial, banking and finance litigation cases.

Admitted to the Paris Bar in 2002, she graduated from HEC Paris (2000) and holds an advanced degree (DESS) in tax and business law from the University of Paris I Panthéon-Sorbonne (2000). She joined De Pardieu Brocas Maffei’s restructuring and insolvency team in 2002. She was appointed counsel in 2009, before being co-opted as partner in 2014.

Joanna is also recognised by Who’s Who Legal: Restructuring & Insolvency 2016 and by the 2017 edition of Best Lawyers as ‘Lawyer of the Year’ in Restructuring.

Recent transactions include: CGG (representing the senior secured creditors’ committee – ongoing); Foraco (representing the new money providers in the context of its court-approved restructuring); Nextiraone (representing one of the largest creditors in the context of the first French pre-packaged sale plan and debt restructuring at the level of the holding company); JOA (representing Alchemy, having become the majority shareholder through a debt-equity swap); Orco Property Group (representing the bondholders’ committee); Brealu (representing Diversified Machine Inc (subsidiary of The Carlyle Group) in the takeover of Brealu’s business in the framework of rehabilitation proceedings); Belvédère (representing the senior noteholders in the insolvency proceedings opened for Belvédère and its subsidiaries); Coeur Défense (representing the ‘A’ bondholders of the securitisation senior tranche in the safeguard proceedings opened for Hold and its parent company Dame Luxembourg); and Mecachrome (representing the bondholders of Mecachrome International Inc in the safeguard proceedings opened for the two French subsidiaries).

JOHAN HÄGER

Roschier Advokatbyrå AB

Johan Häger is head of the firm’s finance and restructuring practice in Sweden.

Mr Häger works closely with the firm’s private equity and corporate M&A teams, the real estate team, tax structuring team and other practices to achieve the best possible results in complex restructurings and security enforcements. He cooperates closely with financial restructuring advisers, CROs and local in-court-administrators, which enables him to efficiently coordinate a team to facilitate a restructuring of both operations and balance sheet. He has extensive experience in LBO financings and high-yield bonds and acts frequently for both bond arrangers and borrowers with the structuring and negotiation of these instruments, which experience is essential for successful restructurings of bank loans and bonds.

Mr Häger’s restructuring and insolvency credentials span cross-border reorganisations in Sweden, Norway, Finland, Denmark, Lithuania, Latvia, Estonia, Germany, the United Kingdom, Canada, the Netherlands and Luxembourg. He acts for local and international banks, as well as for private equity clients and corporate borrowers. Recent engagements
have included Saab Automobile, Nobina, Basler Fashion, the PMS Group, Dentutech, Centrumkompaniet, Propinvest, Iittur, Homburg and Dannemora Mineral.

Mr Häger has, in the growing high-yield bond market, been engaged both by bond holders, private equity firms and corporate borrowers in restructurings involving senior bonds, junior bonds and bank debt.

**DAN HANQVIST**  
*Roschier Advokatbyrå AB*

Dan Hanqvist is a member of the firm’s finance and restructuring practice in Sweden. He has more than 20 years of experience in assisting both Swedish and international banks, financial institutions, funds, corporations as well as public authorities on transactions involving regulatory matters, financial restructuring, derivative transactions and complex financial instruments. He is also often involved in the legislative process in respect of the financial markets. His work experience includes working for market participants in London, Moscow and Sweden, including in-house work for NASDAQ in Stockolm. He is a regular lecturer at the Universities of Stockholm, Uppsala and Södertörn and frequently writes for the academic and professional press.

**MADELEINE HEAL**  
*Harney Westwood & Riegels*

Madeleine Heal joined Harneys in 2017 and is a member of the firm's restructuring and insolvency practice in the Cayman Islands. She is an advocate of 20 years’ experience at the London Bar and has a broad commercial, trusts and insolvency practice. She is a senior offshore litigator valued for her high energy and tenacious approach to multiparty litigation. Madeleine is known for breaking down complex issues into simple clear points and delivering targeted advocacy that is the key to succeeding in litigation, while never losing sight of her clients’ commercial objectives.

Madeleine specialises in civil fraud, insolvency, shareholders’ and joint venture disputes and contentious trusts. She has significant expertise as an advocate in technology, branding and other intellectual property. She is retained for strategic global offshore litigation advice and advocacy.

Madeleine has consistently ranked in *Chambers & Partners* and *Legal 500* for the last 15 years.

**THOMAS S HEATHER**  
*Ritch, Mueller, Heather y Nicolau, SC*

Mr Heather has more than 40 years of experience in banking, restructuring, and mergers and acquisitions. Prior to returning to his current position as a result of the merger of Heather & Heather into Ritch, Mueller, Heather y Nicolau, SC, he was a partner at White & Case in Miami, where he headed the Latin American insolvency and restructuring group, and Ritch, Heather y Mueller in Mexico City, where he was the managing partner. In Mexico and the US, Mr Heather has published many articles and reviews on legal and financial topics, and has co-authored the treatise *Regulation of Foreign Banks*, among other publications. He is a board member of several leading corporations and one of Mexico’s largest banks. Mr Heather is a founding member of the International Insolvency Institute, of the American
Bankruptcy Institute and was a member of the Mexican Institute of Insolvency Specialists, having acted as a conciliator in over 18 cases, as a liquidator, and as lead counsel in hundreds of consensual restructurings throughout his career. He has lectured extensively and is a member of the Advisory Board of the Programme on International Financial Institutions of Harvard University.

Mr Heather holds an LLM from the University of Texas at Austin and obtained his law degree from the Escuela Libre de Derecho.

PHEO M HUTABARAT

Hutabarat, Halim & Rekan

Pheo M Hutabarat is one of the founding partners of Hutabarat, Halim & Rekan. His areas of specialisation encompass capital markets and securities; banking and finance; project finance; energy and natural resources; corporate and investment; mergers and acquisitions; insolvency and corporate reorganisations; commercial disputes and litigation; real property; franchise, agency and distribution; and manpower and human resources.

Mr Hutabarat is a licensed capital market legal consultant and a licensed advocate in Indonesia. He is a member of the Indonesian Association of Capital Market Legal Consultants, the Association of Indonesian Advocates, INSOL International, the International Bar Association and the Inter-Pacific Bar Association.

J ERIC IVESTER

Skadden, Arps, Slate, Meagher & Flom LLP

J Eric Ivester represents clients including borrowers, creditors, investors, sellers, purchasers and other parties of interest at all stages of complex restructuring transactions, such as in-court and out-of-court reorganisations, debt restructurings, acquisitions and divestitures.

Mr Ivester’s recent representations include SunEdison Inc in its Chapter 11 filing, Exide Technologies in its emergence from its voluntary Chapter 11 case and confirmation of its plan of reorganisation resulting in the reduction of US$600 million of debt, Travelport Limited and related companies in their out-of-court restructuring of US$2.1 billion of debt, and MF Global Holdings Ltd in its Chapter 11 filing. Mr Ivester also represented Ipsen Pharma SA in the Chapter 11 case of Inspiration Biopharmaceuticals Inc, wherein Inspiration and Ipsen successfully consummated sales of two haemophilia drugs and related assets to Baxter International and Cangene Corporation.

Mr Ivester also led Skadden’s representations in the successful restructurings of Interstate Bakeries Corporation, the maker of Wonder Bread and Twinkies and the nation’s largest wholesale distributor of fresh baked bread and sweet goods; Hayes-Lemmerz, the largest global producer of wheels for passenger cars and light trucks; and Mark IV/Dacco Products, a tier-one automotive supplier. In the retail sector, Mr Ivester was one of the partners that led the firm’s representation of Kmart Corporation and its affiliates in their successful emergence from Chapter 11. The Turnaround Management Association recognised Mr Ivester for his work on the Interstate Bakeries Chapter 11, naming it the ‘Large Company Transaction of the Year’ at its 2009 Transaction of the Year Awards. In February 2009, Mr Ivester was named ‘Dealmaker of the Week’ by The Am Law Daily for his work on the same case. He has repeatedly been selected for inclusion in Chambers USA: America’s Leading Lawyers for Business and Best Lawyers in America. Mr Ivester is a fellow of the American College of Bankruptcy.
TARA JAMIESON

_Afridi & Angell_

Tara Jamieson is an associate practising in mergers and acquisitions and corporate and commercial law. She has considerable experience in a wide range of corporate transactions including asset and share sales and purchases, investments, joint ventures, mergers and acquisitions and corporate restructurings.

Prior to joining Afridi & Angell, Ms Jamieson trained at and was a solicitor with a leading firm in Scotland. She is a member of the Law Society of Scotland.

CHRISTINA KALOGEROPOULOU

_Sarantitis Law Firm_

Christina Kalogeropoulou is an associate of the firm. She graduated from the Faculty of Law of the University of Athens in 2012. She holds a postgraduate diploma in Greek tax law from the Research Centre of the Athens University of Economics and Business (PG Diploma, 2014). She received her master's degree in corporate, M&A, capital markets and tax law from the University of Pennsylvania Law School (LLM, 2015) and she also holds a business and law certificate from the Wharton Business School (WBLC, 2015).

Her practice focuses on the areas of corporate and commercial law; mergers and acquisitions; corporate governance; company establishment and regulatory issues; international taxation and customs; banking and finance; contracts and commercial agreements; and real estate.

During her practice, she assisted in the recapitalisation of Alpha Bank and Piraeus Bank and she also participated in the liquidation process of the Agricultural Bank of Greece and TT Hellenic Postbank. She was routinely involved in major transactions of the Hellenic Republic Asset Development Fund, including the privatisation of a public utility and the representation of a preferred bidder in a lease-back transaction of state-owned properties. She was also involved in the representation of AstraZeneca, American Express and Interamerican before the administrative courts of Athens on tax issues involving disputes on clawbacks, VAT, income and real estate taxation.

She is a member of the Athens Bar Association and a member of the American Bar Association since 2014. She speaks English and French proficiently and is a beginner in Spanish.

YOSUKE KANEGAE

_Nagashima Ohno & Tsunematsu_

Yosuke Kanegae is a partner at Nagashima Ohno & Tsunematsu’s restructuring and insolvency group in Tokyo. He brings experience to challenging domestic and cross-border restructurings and reorganisations and has represented distressed companies, trade creditors, financial institutions and strategic investors in highly complex workout arrangements spanning Japan, Asia, the US and Europe.

Companies he has represented operate in a broad compass of business sectors, including retailing, insurance, consumer finance, semiconductor manufacturing, telecommunications, clothing manufacturing, printing and real estate investment.
In the past several years, Yosuke has had a distinguished track record and has been particularly noted for his use of the US Chapter 11 and 15 proceedings in Japanese restructurings, including for clients Takata Corporation, Elpida Memory and Spansion Japan.

He graduated from Kyoto University in 1999 and received an LLM from Northwestern University School of Law in 2005. Since 2012 he has taught a course on restructuring and insolvency practice at the University of Tokyo’s faculty of law as a lecturer.

MARIE KEUP
Strelia
Marie Keup is an associate at Strelia, registered with the French-speaking Brussels Bar. She advises international and national companies on IP and ICT law, data protection and contract law. She also deals with dispute resolution in these areas of law, among others in the context of insolvency proceedings. Ms Keup obtained a bachelor in law from the Facultés Universitaires Saint-Louis (Belgium) in 2008 and a master in law from the Paris Nanterre University in 2010. In 2016, she completed an advanced master of intellectual property rights and ICT law at the University of Leuven in Belgium. Prior to joining Strelia, she was an associate in the Brussels office of Taylor Wessing.

HANS KLOPPER
Independent Advisory (Pty) Limited
Hans Klopper is an admitted attorney in South Africa, specialising in restructuring and insolvency law. He practises from offices in Johannesburg and Cape Town. Hans is currently actively involved in the restructuring and business rescue of multiple businesses in mining, retail, renewable energy and the commercial property sector. He restructured the affairs of two prominent South African golf estates and, in early 2016, a major jewellery retailer with more than 70 stores.

He regularly presents workshops and lectures, and has written on this topic. He recently co-authored an article for The Stellenbosch Law Review, Volume 25, No. 3, 2014 – ‘Averting Liquidations with Business Rescue: Does a Section 155 Compromise Place the Bar too High?’ He was included in Who’s Who Legal: Restructuring and Insolvency 2016.

He is a past director of the South African Restructuring and Insolvency Practitioners Association and the board of directors of INSOL International, the worldwide federation of national associations for accountants and lawyers who specialise in turnaround and insolvency, and serves as the Chair of INSOL’s Smaller Practice Committee.

Hans chaired the Northern Provinces Law Society’s Committee for Insolvencies and Liquidations for five years and served on the Insolvency Standing Committee of the Law Society of South Africa.

NOBUAKI KOBAYASHI
Nagashima Ohno & Tsunematsu
Nobuaki Kobayashi is a partner of Nagashima Ohno & Tsunematsu’s restructuring and insolvency group in Tokyo. He has a wealth of practical experience handling high-profile insolvency and restructuring proceedings, including large-scale corporate reorganisations, including the corporate rehabilitation proceedings of Takata Corporation, as a debtors’
counsel, the corporate reorganisation proceedings of Elpida Memory, as a trustee, and the bankruptcy proceedings of MtGox, a Japanese bitcoin exchange, as a bankruptcy trustee.

Since 2013, he has been chairperson of the Study Committee on the Bankruptcy Law System of the Japan Federation of Bar Associations. He served as a chairperson of the study group on Guidelines applicable to Management Guarantee, established by JCCI (The Japan Chamber of Commerce and Industry) and JBA (Japanese Bankers Association), and a vice chairperson of Japan Insolvency Lawyers Network, which has a membership of over 5,000. He also serves as a board member of the Japan Chapter of the East Asian Association of Insolvency & Restructuring. In 2015, he represented Delta Air Lines, as a candidate of sponsor to Skymark Airlines in their civil rehabilitation proceedings.

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Martina Kronström is a counsel at Uoti, Sotamaa & Co Oy Attorneys-at-law. She has vast experience in the legal field. Ms Kronström has for over 10 years specialised in dispute resolution and has extensive experience in various court proceedings. She has especially focused on and gathered extensive experience in criminal proceedings involving securities market issues. Ms Kronström also assists clients in pretrial investigations. She focused on insolvency matters at University and has for several years worked with various insolvency proceedings and clawback actions. Ms Kronström has previously worked closely with matters relating to housing and real-estate issues. Ms Kronström is a conciliator approved by the Finnish Bar Association. She also assists clients in Swedish and Danish.

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Paul Kuipers is a partner at Linklaters LLP and head of the finance practice of the Amsterdam office. He specialises in a wide range of insolvency-related matters, stressed and distressed reorganisations and asset recovery (including the enforcement of security). Paul Kuipers has been admitted as an attorney-at-law at the Dutch Bar since 1996 and has over 20 years of experience in the field of national and cross-border insolvency law. He is a regular speaker at conferences and seminars dealing with various restructuring and banking issues and has also published on finance and insolvency topics in both Dutch and international legal literature. Current memberships include: the International Bar Association (Section on Restructuring and Creditors Rights), INSOLAD (the Dutch insolvency specialist association), INSOL Europe (the European insolvency specialist association), the Netherlands Association for Comparative and International Insolvency Law and the Dutch Corporate Litigation Association.

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Kenneth regularly advises lenders, borrowers and insolvency professionals in relation to liquidation, judicial management, receivership, schemes of arrangement, and complex international and regional cross-border restructurings. He is recommended for his expertise in restructuring and insolvency by _The Legal 500 Asia Pacific_ (2017). _Chambers Asia-Pacific_
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(2015, 2016) also names him as a recognised practitioner in the field of restructuring and insolvency.

He has also represented clients at all levels of trial and appellate litigation, and in arbitration proceedings, on a wide range of matters. These include contractual claims, property disputes, shareholder disputes, banking claims, breaches of directors’ duties, media and entertainment disputes, employment, professional negligence claims, and defamation.

Kenneth has appeared as amicus curiae under the Supreme Court’s Young Amicus Curiae scheme on novel matters concerning constitutional protections, criminal procedure and sentencing. He has contributed to a number of leading publications, including *Singapore Civil Procedure 2016*, and *Leniency Regimes* (5th Edition) 2015.

In 2015 Kenneth was appointed to the Advisory Committee to the Professional Conduct Council established under the Legal Profession Act, and is a member of the Insolvency Practice Committee of the Law Society of Singapore.

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Harem Mahir is a partner in the firm’s finance and restructuring practice in Sweden. His experience covers various out-of-court restructurings, within various industry sectors, including media, retail, automotive and real estate. In addition, Mr Mahir has experience in various large-scale international acquisition and asset-backed financing transactions, representing international banks and financial institutions as well as private equity investors and large corporate. He also regularly advises various financial institutions and insurance companies in regulatory and derivative matters. In addition, his experience also covers working with debt capital market transactions, representing both arrangers and issuers in various high-yield bond issues.

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Chris Mallon is a partner at Skadden, Arps, Slate, Meagher & Flom (UK) LLP. He leads and has played a leading role in growing the firm’s corporate restructuring practice in Europe. He works closely with the London finance, corporate M&A and private equity teams, and the US corporate restructuring group.

Mr Mallon’s restructuring and insolvency credentials span cross-border reorganisations involving a number of jurisdictions, including England, the US, Ireland, India, Russia, the Cayman Islands, Bermuda, Poland, Germany, Holland, Italy and Luxembourg. His clients have included Enron, Global Crossing, WorldCom, Loral, Telewest, Parmalat, Eurotunnel, Gate Gourmet, British Vita, the Tele Columbus Group, TORM A/S and Excel Maritime Carriers.

Mr Mallon has acted for the Tele Columbus Group in restructuring its debt by means of a debt transfer and debt-for-equity swap implemented via several schemes of arrangement; for Calyon in relation to ongoing negotiations with FGIC regarding settlement of transactions relating to the Rhineland Conduit; for Carlyle in relation to Carlyle Capital Corporation Limited’s restructuring and renegotiation of its credit lines; and Residential Capital LLC in connection with its financial restructuring. He advised British Vita in relation to the restructuring of complex debt facilities for its operating companies, as well as various clients regarding their distressed investments arising in relation to the US Chapter 11 filing of...
Lehman Brothers. He has been advising other lenders with structured investment vehicles on issues arising out of the recent credit crisis in the subprime and related structured investment markets. He also advised TORM A/S in connection with its financial restructuring, reducing its debt from US$1.4 billion to US$561 million, and involving third-party investor Oaktree Capital in contributing a number of vessels to the restructured TORM entity in return for an equity interest.

Mr Mallon has repeatedly been selected for inclusion in *Chambers Global: The World’s Leading Lawyers for Business*.

Mr Mallon writes and speaks frequently on insolvency and restructuring. After graduating from the University of Western Australia, he was admitted as a barrister and solicitor of the Supreme Court of Western Australia in 1982 and as a solicitor in England in 1987.

**IAN MANN**

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Ian Mann is a leading offshore litigator, senior tactician and thought leader. He is the long-term head of Harneys’ offshore litigation and restructuring department in Hong Kong.

He has been involved in every major recent restructuring in the region involving offshore entities and is a specialist in cross-border and conflict of law dilemmas, including Birmingham City Football Club, Centaur, China Fisheries, China Shanshui, Greens Holdings, China Lumena, Mongolian Mining Corporation, Rightway, Titan Petrochemicals Group, Suntech Power Holdings Co Ltd, LDK Solar Co, Kaisa Group Holdings Ltd and Z-Obee Holdings Ltd.

Ian lectures regularly to judicial, professional and academic bodies. He is the author of both of the leading offshore textbooks on *British Virgin Islands Commercial Law* and *Bermuda Commercial Law* (Sweet & Maxwell Thomas Reuters), and is a regular contributor to *The Offshore Litigation Blog*, a Harneys blog that shares news and views about litigation, dispute resolution, restructuring and insolvency offshore. He is a Fellow of INSOL International as well as a qualified trust and estates practitioner. He is regularly asked to provide his expert opinion on offshore law to various courts.

Ian is ranked as a leading offshore lawyer by *Chambers* and *Legal 500*, and is recognised as being among the world’s leading asset recovery, restructuring, and insolvency and private-client lawyers by *Who’s Who Legal 2016*. He is also one of ten offshore lawyers recognised for client service in Asia by *Asian Legal Business* in 2017 Ian is consistently ranked as a Tier 1 lawyer in Asia by *Chambers and Partners* where he is described as being a ‘very seasoned adviser’. Ian is also recommended as a ‘leading lawyer’ by *Legal 500* where he is described as ‘a pleasure to work with’ and as being ‘friendly and hardworking’. He is also recognized by *Who’s Who Legal 2016*, which describes Ian as ‘a gifted advocate who leaves no stone unturned’.

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Grégory Minne is a partner in the banking and financial services, the bank lending and structured finance and the commercial and insolvency practices of Arendt & Medernach. He specialises in banking and finance, in particular in restructuring and insolvency, as well as acquisition, aircraft, project, rail finance, real estate, ship, and structured finance, securities transactions, payment and securities settlement systems and refinancing. He also advises clients on complex private international law matters and on the legal enforceability of set-off, netting and collateral arrangements with respect to cross-border transactions and related insolvency risks and regulatory requirements.

He has been a member of the Luxembourg Bar since 2005. Prior to joining Arendt & Medernach, Grégory worked in Switzerland within the legal department of a leading French investment bank.

Grégory holds a master’s degree in law from the Catholic University of Louvain (Belgium) and a master’s in business law from the Universities of Geneva and Lausanne (Switzerland). He also holds a degree in philosophy and a degree in economic and social ethics from the Catholic University of Louvain.

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Luciana, partner in the restructuring and insolvency and in the corporate litigation areas in TozziniFreire Advogados, is renowned for her practice and knowledge in judicial restructurings. Her experience also encompasses pre-litigation and litigation spheres in a wide range of corporate matters, such as antitrust, corporate, banking and finance fields. Luciana is a member of INSOL (International Association of Restructuring, Insolvency & Bankruptcy Professionals), TMA (Turnaround Management Association of Brazil), IBA (International Bar Association) and ABA (American Bar Association). Luciana is recommended in the 2017 Insol Directory and in Latin Lawyer 250, relevant international legal guides. She also participated in judicial restructurings awarded by IFLR Americas Award in 2017 and in the Latin Lawyer Deal of the Year in 2010, 2012 and 2015.

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Matti Nousiainen is a counsel at Uoti, Sotamaa & Co Oy Attorneys-at-law specialised in dispute resolution and insolvency. One of his main areas of expertise is procedural law. Mr Nousiainen has broad experience in insolvency proceedings and restructuring proceedings as
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Alberto Nunez-Lagos is a partner in the Madrid office of Uría Menéndez. He joined the firm in 1987 and became a partner in 1998. He heads Uría Menéndez’s German desk. Alberto currently represents INSOL Europe before UNCITRAL.

Alberto’s practice covers a wide range of corporate and banking work, although he has tended to specialise in restructuring, thereby becoming engaged in insolvency proceedings involving leading Spanish and international corporations. He has represented clients involved in all major insolvencies in Spain, including cross-border insolvencies in the last years, acting either for the debtor, creditors or management.

Alberto has also been active in M&A transactions involving insolvent companies in their restructuring process.

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Tom Pugh is a partner in Mayer Brown JSM’s restructuring, bankruptcy and insolvency practice, focusing on advising insolvency practitioners, creditors and debtors in respect of cross-border insolvencies and restructurings. His experience includes multibank work-outs; schemes of arrangement; distressed debt and asset trading; and large-scale liquidations and restructurings, such as Lehman Brothers and MF Global, acting for the liquidators in Hong Kong and Chapter 11 cases, such as Pacific Andes. Tom’s restructuring and liquidation work has involved advising on cross-border asset recoveries and settlements; court processes to resolve key issues affecting liquidators’ ability to determine and distribute assets; matters arising on administration of failed brokerages; and assignments involving the PRC, Thailand, Vietnam, the United States, the United Kingdom, Germany, Switzerland and Japan. Mr Pugh is admitted as a solicitor in Hong Kong and England and Wales. He is a board member of the Hong Kong chapter of the global Turnaround Management Association.

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Chai Ridgers is a member of the firm’s restructuring and insolvency group in Hong Kong and supports Ian Mann in leading the practice in Asia.

He specialises in cross-border restructurings, insolvency and workouts of distressed companies. He consistently advises leading international and regional accountancy practices, onshore law firms, financial institutions, insolvency office holders, official and unofficial creditors’ committees, private equity sponsors, hedge funds, debtor-in-possession loan providers, directors, trustees, shareholders and corporate debtors. He has worked extensively on assignments throughout Asia, including in China, Hong Kong, Japan, Singapore, South Korea and Taiwan.
Recently, Chai has played an instrumental role in a number of global restructurings concerning offshore entities including Mongolian Mining Corporation, the Pacific Andes group of companies, Z-Obee Holdings Ltd, China Lumena New Materials Corp., Kaisa Group Holdings Ltd, the LDK Solar group of companies, Birmingham City Football Club, China Shanshui Cement Group Limited, Greens Holdings Limited, Titan Resources Management Limited (part of the Titan Petrochemicals Group) and Suntech Power Holdings Co., Ltd.

Prior to joining the firm, Chai was a senior associate at a global law firm in Singapore and London.

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Alex Rogan is an associate at Skadden, Arps, Slate, Meagher & Flom (UK) LLP, specialising in corporate restructuring. His practice focuses on national and cross-border representation of distressed companies and creditors as well as major financial institutions, funds, manufacturing and telecommunications companies. His clients have included Warwick Capital, British Vita, Tele Columbus, Exide Technologies, BNP Paribas, TORM A/S, MF Global, Grant Thornton, Doughty Hanson, Travelport, Crédit Agricole CIB, Nautilus Group, SunEdison and Roust Trading Limited.

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Mark is a senior associate in the litigation and insolvency department of Harneys’ BVI office. He joined Harneys in 2015 from Thomas More Chambers, chambers of Geoffrey Cox QC, London, where he practised as an independent barrister, principally in the areas of insolvency, company, commercial, and property law.

Before joining Harneys, Mark spent several months working with offshore clients in Mauritius, providing advisory and litigation services to international clients in relation to Mauritian insolvency proceedings, arbitrations, and transactions and projects in a number of African states worth over US$1 billion.

Mark is a member of COMBAR and the Chancery Bar Association and is a scholar of the Honourable Society of Lincoln’s Inn.

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Dorotheos Samoladas is a partner of the firm and head of its corporate practice. Moreover, he is a graduate of the Faculty of Law of the University of Athens and has also completed postgraduate studies in the UK (LLM Soton).

Dorotheos Samoladas has extensive experience and a wide-ranging, successful practice in corporate, M&A, restructuring and commercial law. He advises on mergers and acquisitions (including leveraged buyouts, private equity and public takeovers), leads an active restructuring practice and also advises on joint ventures, IPOs, privatisations, commercial contracts, regulatory compliance, as well as an active commercial litigation practice. Dorotheos Samoladas has been involved in high-profile litigation cases before the
Greek courts in the past 12 years. His litigation practice also includes representing mainly corporate clients before the Greek administrative courts, in various types of administrative disputes. Dorotheos Samoladas has acted for public and private companies, some of Greece’s leading business figures, as well as large multinational corporate clients, banks and high net worth individuals. He has also represented various parties before independent supervising authorities and in government investigations.

According to BestLawyers.com, Dorotheos Samoladas has been selected by his peers as Lawyer of the Year 2014 for Athens, in the practice area of mergers and acquisitions, and he won the Chambers Award 2015 in the practice area of corporate and commercial.

He is a member of the Athens Bar and the International Bar Association. He speaks English and French proficiently.

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He joined the firm in 2005, immediately after graduating from the Catholic University of Portugal. Since then, he has focused his work on corporate litigation and on restructuring and insolvency issues.

He has been consistently ranked as an expert insolvency and restructuring lawyer by several international guides, notably the Chambers Europe directory. He is also the author of several legal articles and co-author of a law book on restructuring issues.

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Stine D Snertingdalen is a partner at Kvale Advokatfirma DA, specialised within banking and finance, and insolvency and restructuring. Ms Snertingdalen gives legal aid to some of the largest banks in Norway in the area of banking and finance, and debt and insolvency-related issues. She also assists clients with restructuring their businesses, and was Norwegian legal counsel for Exide Technologies during the Chapter 11 restructuring process.

She is frequently appointed as bankruptcy administrator by the Oslo Bankruptcy Court, and has worked on several of the largest insolvency cases in Norway. Ms Snertingdalen regularly holds lectures for the Norwegian Law Society and for financial institutions. She has an LLM from Utrecht University in the Netherlands, and has published several articles on Norwegian insolvency law. Ms Snertingdalen is highly ranked both in Norwegian and international rankings such as Legal 500 and Chambers, and she is a government appointed member of the Norwegian Advisory Council on Bankruptcy. In 2015, she was a member...
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ANDREW THORP

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Andrew Thorp heads up Harneys’ BVI litigation and insolvency practice group. For over a decade, Andrew has advised law firms, banks, funds, private equity houses and trust companies on all aspects of BVI contentious law.

Andrew is particularly sought after by clients for cross-border asset recovery and insolvency work, and is a recognised industry leader. Much of his focus is on pre-emptive remedies, including freezing orders, provisional liquidations and discovery orders, often against a background of fraud. He has acted in numerous successful asset retrieval operations across CIS, Latin America and Asia, alongside teams from Harneys, other international law firms and investigatory professionals.

Andrew has been at the forefront of developing insolvency law in the BVI, having successfully led teams in the seminal hedge fund cases following the liquidity crises and high-profile frauds of the last 10 years. Additionally, he has pioneered a number of cross-border protocols between court officers and is regularly retained to advise on restructuring of international distressed structures.

Andrew is a director of INSOL Global as well as chairman of RISA. He is also an honorary member of COMBAR and the Chancery Bar Association.

He is ranked in Band 1 by Chambers and Partners in the British Virgin Islands, is recommended by The Legal 500, and is recognised as being among the world’s leading asset-recovery and private-client lawyers by Who's Who Legal 2016.

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Dr T rettnak (born 1976) is a partner at Cerha Hempel Spiegelfeld Hlawati Rechtsanwälte GmbH with its headquarter in Vienna and several offices in CEE. He heads the insolvency and restructuring practice and is a member of the corporate and M&A practice.

He studied law and business in Austria, Spain and the United States of America (Mag et Dr iur, LLM) and master’s degree in Business Administration at Kellogg School of Management (CM)).

Dr Trettnak is admitted as an attorney in Austria and in New York, and became a partner at CHSH in 2010. He advises domestic and international clients mainly in cross-border M&A, restructurings, venture capital and private equity transactions.

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She has several years’ experience working with various insolvency proceedings, including some of the largest bankruptcy proceedings and judicial debt-negotiation proceedings in
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Sebastian Way is an associate at Skadden, Arps, Slate, Meagher & Flom (UK) LLP and is a member of the firm’s European corporate restructuring group practising primarily in the area of complex cross-border reorganisations. His recent clients have included SunEdison, CME Group, Goldman Sachs, Kaupthing, Roust Trading Limited, Nautilus Group, Fidelity Management and Research, Exide Technologies, BNP Paribas, TORM A/S, MF Global, Grant Thornton, Nike, DuPont, Doughty Hanson, Travelport and Crédit Agricole CIB.

Mr Way graduated from Oxford University in 2004 and received an LLM from King’s College London in 2006. He is a solicitor of the Senior Courts of England and Wales.
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