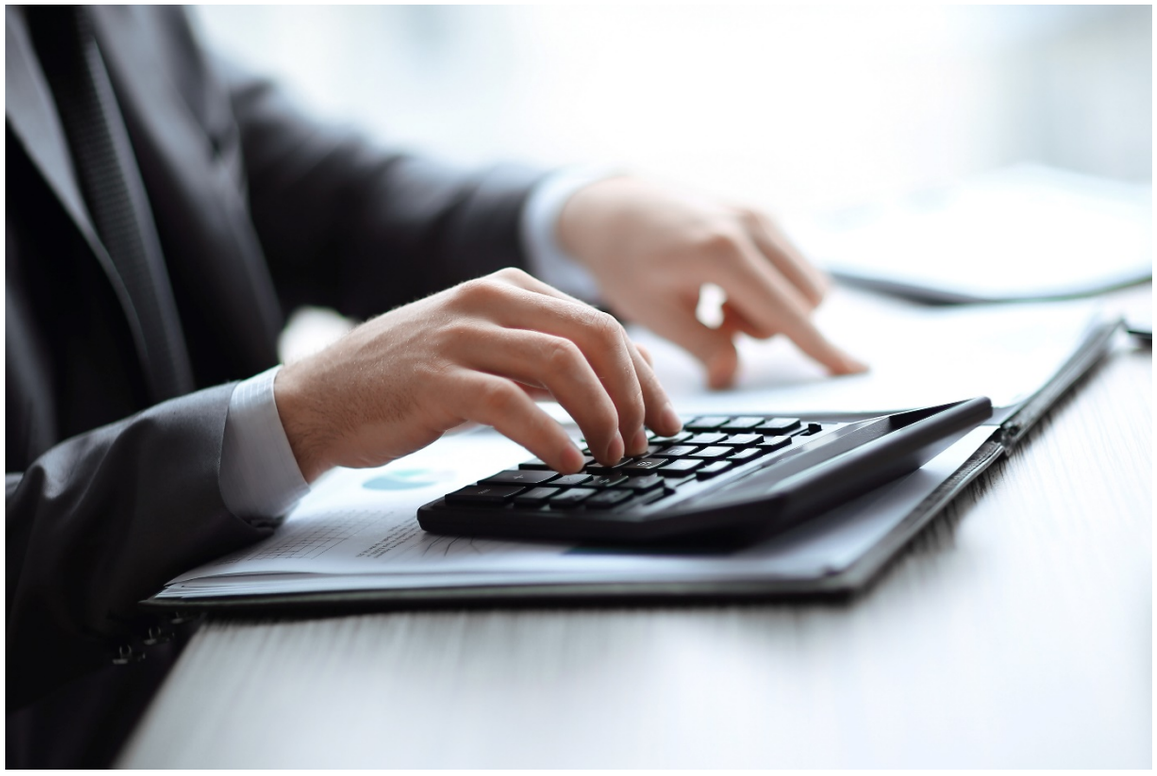
PREVENTIVE RESTRUCTURING FRAMEWORKS, DISCHARGE OF DEBT AND DISQUALIFICATIONS



THE SCOPE OF THE DIRECTIVE

- **EARLY WARNING TOOLS**
- **PREVENTIVE RESTRUCTURING**
- **FRAMEWORKS**
- **DISCHARGE OF DEBT**
- **MEASURES TO INCREASE THE EFFICIENY OF PROCEDURES CONCERNING RESTURCTUING INSOLVENCY AND DISCHARGE OF DEBT**

Directive (EU) 2019/1023 of the european parliament and of the council of 20 june 2019

on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency).

REGULATORY FRAMEWORK

On June 26, 2019, was published in the Official Journal of the European Union, the directive (EU) 2019/1023 of the European Parliament and of the Council, (hereinafter, the "Directive") concerning preventive restructuring frameworks, debts, disqualifications and measures aimed at increasing the efficiency of the restructuring, insolvency and debts procedures and with which the directive (EU) 2017/1132 was amended in terms of restructuring and insolvency.

THE OBJECTIVE OF THE DIRECTIVE

The objective of this Directive is to remove obstacles to the exercise of fundamental freedoms which result from differences between national laws and procedures concerning preventive restructuring, insolvency, discharge of debt and disqualifications.

Differences between Member States in relation to this matter translate into additional costs for investors when assessing the risk of debtors getting into financial difficulties in one or more Member States, or of investing in business in financial difficulties.

The availability of effective preventive restructuring frameworks would ensure that action is taken before enterprises default on their loans, thereby helping to reduce the risk of loans becoming non-performing in cyclical downturns and mitigating, the adverse impact on the financial sector.

The scope of the directive

The Directive consists of three main parts, concerning:

- preventive restructuring framework and early warning tools with a view to preventing insolvency and ensuring their viability for debtors;
- procedures aimed to discharge of debt for entrepreneurs who are insolvent but honest; and
- measures to increase the efficiency of procedures concerning restructuring insolvency and discharge of debt.

General provisions: early warning tools

Member States shall ensure that debtors have access to one or more clear and transparent early warning tools which can detect circumstances that could give rise to a likelihood of insolvency and can signal to them the need to act without delay.

Early warning tools may include:

a) alert mechanisms when the debtor has not made certain types of payments;

b) advisory services provided by public or private organisations;

c) incentives under national law for third parties with relevant information about the debtor.

Member States shall also ensure that information on access to early warning tool is publicly available online and that, in particular for SMEs, it is easily accessible and presented in a user-friendly way. ([1])

Preventive Restructuring Frameworks

Legitimate subjects: preventive restructuring frameworks provided for under this Directive shall be available on application by debtors. Member States may also provide that preventive restructuring frameworks are available at the request of creditors and employees' representatives, subject to the agreement of the debtor ([2]).

Objective assumption: Member States shall ensure that, where there is **a likelihood of insolvency**, debtors have access to a preventive restructuring framework that enables them to restructure, with a view **to preventing insolvency and ensuring their viability, without prejudice to other solutions for avoiding insolvency**.

Subjective assumption: a restructuring framework should be available before a debtor becomes insolvent under national law, namely before the debtor fulfils the conditions under national law for entering collective insolvency proceedings, which normally entail a total divestment of the debtor and the appointment of a liquidator.

(1) Enterprises, and in particular SMEs, which represent 99% of all business in the Union, should benefit from a more coherent approach at Union level. SMEs are more likely to be liquidated than restructured, since they have to bear costs that are disproportionately higher than those faced by larger enterprises. SMEs, especially when facing financial difficulties, often do not have the necessary resources to cope with high restructuring costs and to take advantage of the more efficient restructuring procedures available only in some Member States. In order to help such debtors restructure at low cost, comprehensive check-lists for restructuring plans, adapted to the needs and specificities of SMEs, should be developed at national level and made available online.

(2) It is appropriate to exclude form the scope of this Directive debtors which are insurance and re-insurance undertakings; credit institutions; investment firms and collective investment undertakings; central counterparties; centrale securities depositories and other financial institutions and entities. Member States should be able to exclude other financial entities providing financial services which are subject to comparable arrangement and powers of intervention.

The appointment of the judicial or administrative authority: the appointment by a judicial or administrative authority of a practitioner in the field of restructuring shall be decided on a case-by-case basis. Member States shall provide for the appointment of a practitioner in the field of restructuring, to assist the debtor and creditors in negotiating and drafting the plan, at least in the following cases:

- where **a general stay of individual enforcement actions**, in accordance with Article 6.3, is granted by a judicial or administrative authority, and the judicial or administrative authority decides that such a practitioner is necessary to safeguard the interest of the parties;
- where the restructuring plan needs to be confirmed by a judicial authority by means of a cross-class cram down, in accordance with Article 11; or
- where it is requested by the debtor or by a majority of the creditors, provided that, in the latter case, the cost of the practitioner is borne by the creditors.

Effects:

a. *debtor in possession*: Member States shall ensure that debtors accessing preventive restructuring procedures remain totally, or at least partially, in control of their assets and the day-to-day operation of their business;

b. *stay of individual enforcement actions*: Member States shall ensure that debtors can benefit from a stay of individual enforcement actions to support the negotiations of a restructuring plan in a preventive restructuring framework. A stay of individual enforcement actions could be general, in that it affects all creditors, or it could apply only to some individual creditors or categories of creditors. In order to provide for a fair balance between the rights of the debtor and those of creditors, a stay of individual enforcement actions should apply for a maximum period of up to four months. Complex restructuring may, however require more time. Member States should be able to provide that, in such cases, extensions of the initial period of stay of individual enforcement actions can be granted by the judicial or administrative authority. In the interest of legal certainty, the total period of the stay of individual enforcement actions should be limited to 12 months. Member States should provide that judicial or administrative authorities can lift a stay of individual enforcement actions if it no longer fulfils the objective of supporting negotiations, for example, if it becomes apparent that the required majority of creditors does not support the continuation of the negotiations;

c. *effects on the netting arrangements*: Member States may provide that a stay of individual enforcement actions does not apply to netting arrangements, including close-out netting arrangements, on financial markets, energy markets and commodity markets, even in circumstances where Article 31.1 does not apply, if such arrangements are enforceable under national insolvency law. The stay shall, however, apply to the enforcement by a creditor of a claim against a debtor arising as a result of the operation of a netting arrangement;

d. *effects on current agreements*: Member States shall provide for rules preventing creditors to which the stay of individual enforcement actions applies from withholding performance or terminating, accelerating or, in any other way, modifying essential executory contracts to the detriment of the debtor, for debts that came into existence prior to the stay of individual enforcement acions, solely by virtue of the fact that they were not paid by the debtor;

e. *effects on the eventual opening of an insolvency procedure*: Member States shall ensure that the expiry of a stay of individual enforcement actions without the adoption of a restructuring plan does not, of itself, allow the opening of an insolvency procedure with could end in the liquidation of the debtor, unless the other conditions for such opening laid down by national law are fulfilled.

Content of restructuring plans: Article 8 of the Directive regulates the minimum content of the preventive restructuring plan. More specifically, it will have to indicate, *inter alia*:

- the identity of the debtor;
- the debtor's assets and liabilities at the time of the submission of the restructuring plan;
- the creditors, whether named individually or described by categories of debt in accordance with national law;
- where applicable, the classes into which the creditors have been grouped, for the purpose of adopting the restructuring plan, and the respective values of claims and interests in each class;
- where applicable, the identity of the practitioner in the field of restructuring;
- the terms of the restructuring plan.

The right to vote of the creditors and the formation of classes: Member States shall ensure that creditors have a right to vote on the adoption of a restructuring plan. Member States may exclude from the right to vote the following: (a) equity holders; (ii) creditors whose claims rank below the claims of ordinary unsecured creditors in the normal ranking of liquidation priorities; or (iii) any related party of the debtor or the debtor's business, with a conflict of interest under national law.

Member States shall ensure that creditors are treated in separate classes which reflect sufficient commonality of interest based on verifiable criteria, in accordance with national law. The judicial or administrative authority should examine class formation, including the selection of creditors affected by the plan, when a restructuring plan is submitted for confirmation.

Confirmation of restructuring plans: Member States shall ensure that certain restructuring plans are binding on the parties only if a judicial or administrative authority confirms them.

Confirmation of a restructuring plan by a judicial or administrative authority is necessary to ensure that the reduction of the rights of creditors or interests of equity holders is proportionate to the benefits of the restructuring and that they have access to an effective remedy. For this reason, the restructuring plan will have to be notified to all known creditors on which it could have an unfair effect on their interests.

More specifically, pursuant to art. 10.2 of the Directive, the confirmation is necessary where the restructuring plan:

- affects the claims or interests of dissenting creditors;
- contains provisions concerning new financing;
- involves the loss of more than 25 % of the workforce, if such loss is permitted under national law ([3]).

Finally, Member States should be able to provide that confirmation by a judicial or administrative authority is necessary also in other cases. Member States should ensure that a judicial or administrative authority is able to reject a plan in the event that the latter does not have reasonable prospects to prevent the debtor's insolvency and to guarantee the economic sustainability of the company.

Cross-class cram-down: Member States shall ensure that a restructuring plan which is not approved by all classes of creditors, in every voting class, may be confirmed by a juridical or administrative authority upon the proposal of a debtor or with the debtor's agreement, and become biding upon dissenting voting classes where the restructuring plan fulfils at least the following conditions:

- is complies with article 10(2) and (3);
- it has been approved by:
  a) a majority of the voting classes of creditors provided that at least one of those classes is a secured creditors class or is senior to the ordinary unsecured creditors class; or, failing that;
  b) at least one of the voting classes of creditors or where so provided under national law, impaired parties, other than an equity-holders class or any other class which , upon a valuation of the debtor as a going concern, would not receive any payment or keep any interest, or, where so provided under national law, which

([3]) In this case, the confirmation of restructuring plans should only be necessary where national law allows for preventive restructuring frameworks to provide for measures having direct effects on employment contracts.

could be reasonably presumed not to receive any payment or keep any interest, if the normal ranking of liquidation priorities were applied under national law;

- it ensures that dissenting voting classes of affected creditors are treated at least as favorably as any other class of the same rank and more favorably that any junior class; and
- no class of creditors can, under the restructuring plan, receive or keep more than the full amount of its claims or interests.

Effects of restructuring plans: Member States shall ensure that restructuring plans that are confirmed by a judicial or administrative authority are binding upon all creditors ([4]).

Discharge of debt

In order to counter the consequents negative deriving from insolvency, such as, *inter alia*, the disqualifying entrepreneurs from taking up and pursuing entrepreneurial activity and the continual inability to pay off debts, the Directive aims to facilitate the continuation of the existing company in order to guarantee a second chance to the entrepreneur who has undergone an insolvency procedure (event if a partial sacrifice for creditors results).

Member States aim to reduce the negative effects of over-indebtedness or insolvency on entrepreneurs in particular:

I. by allowing for a full discharge of debts within three years from the opening of the procedure (or from the date on which the execution of the restructuring plan begins) without the need for an instance to a juridical or administrative authority;

II. by limiting the length of disqualification orders issued in connection with a debtor's over-indebtedness or insolvency.

Member States shall ensure that, where an insolvent entrepreneur obtains a discharge of debt in accordance with this Directive, any disqualifications from taking up or pursuing a trade, business, craft or profession on the sole ground that the entrepreneur is insolvent, shall cease to have effect, at the latest, at the end of the discharge, without the need to apply to a judicial or administrative authority to open another procedure ([5]).

Measures to increase the efficieny of procedures concerning resturctuing insolvency and discharge of debt.

With reference to common measures aimed at increasing the efficiency of preventive restructuring procedures, insolvency and discharge of debt, Member States should ensure that members of the judicial ([6]) and administrative authorities ([7]) dealing with procedures concerning preventive restructuring, insolvency and discharge of debt are suitably trained and have the necessary expertise for their responsibilities. Member States shall ensure that, in procedures concerning restructuring, insolvency and discharge of debt, the parties to the procedure, the practitioner and the judicial or administrative authority are able to perform the main operations by use of electronic means of communication.

a comparable data on the performance of procedures concerning restructuring, insolvency and discharge of debt in order to monitor the implementation and application of this Directive over time.

([4])Member States should be able to determine what it means for a creditor to be involved, including in the case of unknown creditors or creditors of future claims. For example, Member States should be able to decide how to deal with creditors that have been notified correctly but that did not participate in the procedures.

([5]) Member States may maintain or introduce provisions denying or restricting access to discharge of debt, revoking the benefit of discharge or providing for longer periods for obtaining a full discharge of debt or longer disqualification periods in certain well-defined circumstances and where such derogations are duly justified (such as abuses, frauds, repeated failures to debit, etc.) Member States may exclude specific categories of debt from discharge of debt, or restrict access to discharge of debt or lay down a longer discharge period where such exclusions, restrictions or longer periods are duly justified.

([6]) Such training and expertise should enable decisions with a potentially significant economic and social impact to be taken in an efficient manner. The creation of specialized courts or chambers, or the appointment of specialized judges in accordance with national law, as well as concentrating jurisdiction in a limited number of judicial or administrative authorities would be efficient ways of achieving the objectives of legal certainty and effectiveness of procedures.
([7]) Member States should also ensure that practitioners in the field of restructuring, insolvency, and discharge of debt that are appointed by judicial or administrative authorities ('practitioners') are: suitably trained; appointed in a transparent manner with due regard to the need to ensure efficient procedures; supervised when carrying out their tasks; and perform their tasks with integrity.

Findings

Comparison with the reform of the Crisis and Insolvency Code.

It is important note the comparison between the Directive and our Crisis and Insolvency Code provided for in Legislative Decree 14/2019 (the "**Crisis Code**").

In fact, despite most of the provisions contained in the Directive are already incorporated in the Crisis Code (especially with reference to the alert procedures), some aspects are still many distant from the objectives pursued by the Directive. In particular:

- that relating to the creditor's incentive to have a conduct aimed at supporting the company in financial distress;
- the downsizing of the effects of pre-emption. In fact, while in our legal system, the lower creditor can be satisfied only after the complete satisfaction of the one occupying the higher grade, the Directive suggests that this principle does not operate in absolute terms, thus favoring a better distribution of the usefulness arising from the company reconstruction;
- the obligatory classification of creditors. The Crisis Code, while taking a step forward, has provided for the classification of creditors only for tax debts in the event of incomplete satisfaction and to creditors holding guarantees given by third parties.

The relationship between the Directive and Regulation (EU) 2015/848.

Finally, a further analysis profile is dedicated to the relationship between the Directive and Regulation (EU) 2015/848. The latter, while regulating the competence, recognition, execution, applicable law and cooperation in cross-border insolvency proceedings and the interconnection of bankruptcy registers, does not address with the disparities existing between the national rules that regulate the procedures of prevention. The Directive therefore operates on a different level, having no impact on the scope of application of the Regulation, and aims at full compatibility with it, obliging Member States to put in place prior restructuring procedures that respect certain minimum principles of effectiveness.

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