Luxembourg newsflash

16 September 2019

Restructuring & Insolvency – Briefing note 1/2

This is the first of a series of two briefing notes published by the Restructuring & Insolvency practice of Arendt on recent or ongoing legislative changes in matters of insolvency law at Luxembourg and EU levels.

More information about our Restructuring & Insolvency capabilities can be found on our dedicated webpage here_

Part 1 ─ Update on the upcoming reform of Luxembourg insolvency law

An extensive reform of Luxembourg insolvency law has been in the works since the adoption by the Chamber of Deputies of draft bill No. 6539 on business preservation and the modernisation of bankruptcy law on 26 February 2013 (the "**Draft Bill**"). The parliamentary works have been ongoing since then and are expected to enter into their final stage by the end of the year.

This note aims at summarising the expected changes to Luxembourg insolvency law resulting from the Draft Bill.

➔ What is this reform about?

The main objectives of the Draft Bill are the preservation of the activities of companies in financial difficulties and the protection of the various stakeholders involved by favouring reorganisations over liquidations. The Draft Bill provides new reorganisation tools to distressed companies to that end and also aims to improve the general oversight and early identification of distressed companies.

➔ What are the new means available to restructure a Luxembourg company?

The Draft Bill makes a distinction between (i) out-of-court restructurings and (ii) reorganisation proceedings (in the context of a judicial procedure). While both have in common that they are largely voluntary (*i.e.* they are granted upon request of the business being in financial distress), out-of-court proceedings dot not require a formal application to be made to a Luxembourg court and do not result in any form of publicity.

However, the enforcement of creditors' claims is not suspended under out-of-court restructurings, the effects of which may only be imposed on participating creditors. On the contrary, reorganisation proceedings result in a temporary moratorium on the enforcement of creditors' claims and may bind all creditors under certain conditions.

1) Out-of-court restructurings

The first out-of-court procedure which is available under the Draft Bill is the **conciliation procedure** (*mesure de conciliation*), whereby the company which is in financial distress can require from a public body composed of representatives of various ministries and public entities[1] the appointment of a conciliator (*conciliateur d'entreprise*). The scope of the conciliator's mission is defined by the Draft Bill in a flexible manner and largely by interested parties themselves. The conciliator can for instance assist the distressed company in negotiating with its main creditors or support such company in the evaluation of its difficulties and in the determination of appropriate remedies which could be put in place.

The second out-of-court procedure provided by the Draft Bill is the **mutual agreement outside reorganisation proceedings** (*réorganisation extrajudiciaire par accord amiable*), under which the debtor attempts to conclude an agreement with two or more of its creditors, with or without the assistance of a conciliator, with regard to all or some of its assets or activities. The main advantages of such procedure is that it remains unknown to other creditors, which may facilitate the restructuring of the distressed company, and provides creditors who agreed to be bound by a mutual agreement with the assurance that it may not be challenged in case of an opening of an insolvency proceeding to the extent that it was concluded during the applicable "hardening period".

2) Reorganisation proceedings

If the viability of a company's activities is threatened to the extent that measures which can be enforced against third parties are necessary, the debtor may apply for a judicial reorganisation procedure with the competent district court.

The main advantage of this procedure is that it automatically results in the suspension of any individual enforcement of claims vis-a-vis the applicant not only during the period between the filing of the request and the date of the judicial decision approving the opening of the reorganisation proceedings but also during the proceedings (if granted). The objective of such a moratorium is to provide additional time to the debtor without the risk of individual creditors' claims being enforced, in order to achieve one of three potential outcomes, *i.e.*:

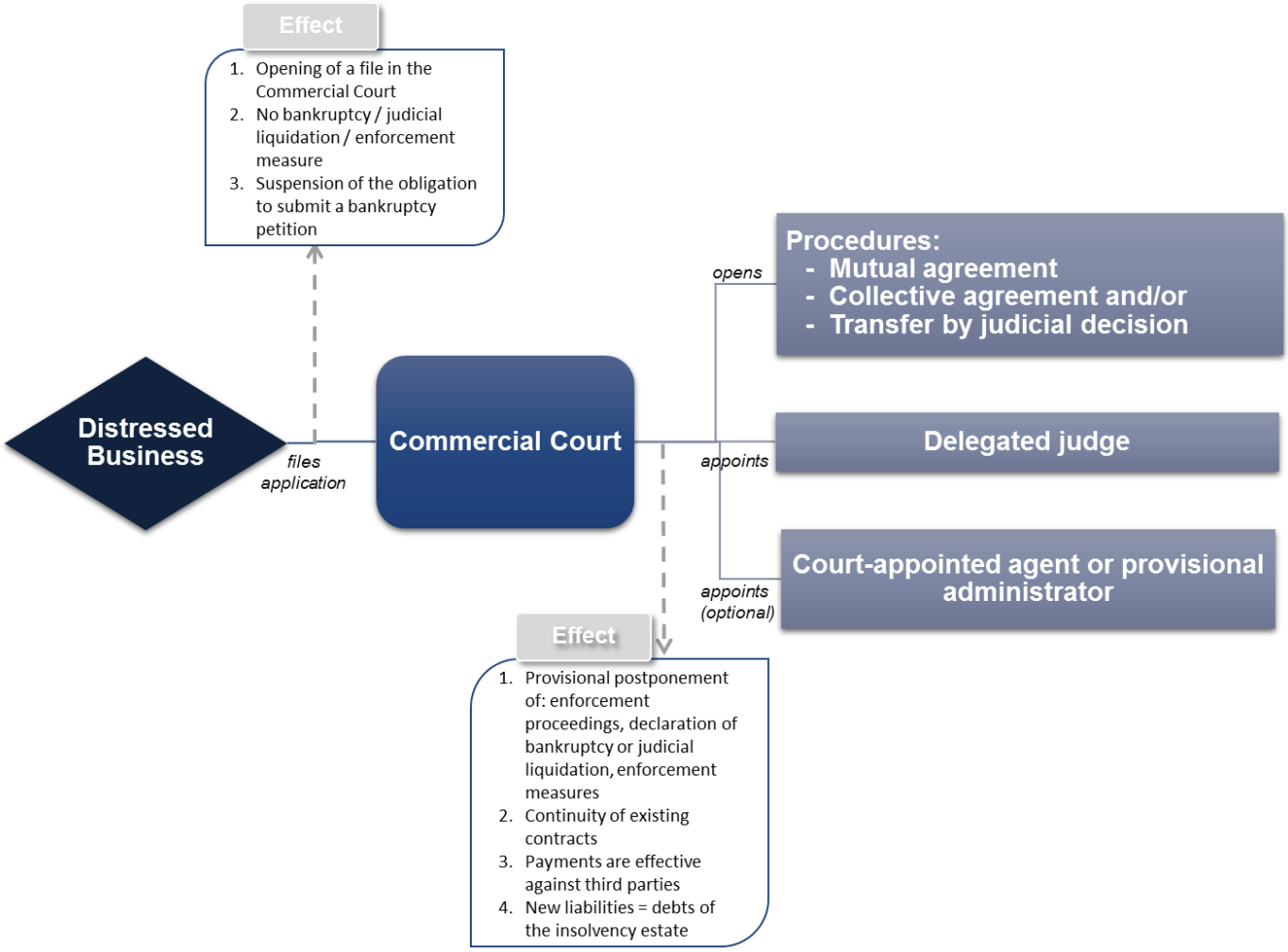
(1) negotiating a **mutual agreement** with one or several of its creditors; or

[1] The *Secrétariat du Comité de conjoncture*.

(2) entering into a **collective agreement upon a reorganisation plan** enforceable against all of its creditors, including those who have opposed such agreement, provided that a majority (in number) of creditors representing at least half of the aggregate amount of the debtor's liabilities have given their consent to such reorganisation plan; or

(3) operating a **transfer by judicial decision**, whereby a court-appointed agent is tasked to organise the transfer in one or more transactions of all or part of the assets or activities of the distressed company with a view to ensuring the continuity of its activities.

The following chart summarises the key aspects of reorganisation proceedings:



➔ How are creditors protected in out-of-court and reorganisation proceedings?

Within the context of an out-of-court procedure, should the distressed company be deemed bankrupt at a later stage, any agreements reached between such company and the creditors may not be challenged solely because they were entered into during the applicable 'hardening period'. This essentially mitigates clawback risks for participating creditors, who may also rely upon and seek the enforcement of the terms of the mutual agreement.

The same benefit is afforded to creditors of a company subject to reorganisation proceedings. Furthermore, a reorganisation plan will only be validly entered into if agreed upon by a majority (in number) of creditors representing at least half the liabilities of the relevant company. A transfer of assets or activities by a decision of a court of justice may be imposed on creditors by the competent district court but the court-appointed agent tasked to sell such assets or activities must do so taking into account the interest of creditors. Finally, certain publicity measures for the benefit of creditors are also provided for in the Draft Bill.

➔ What are other noteworthy changes to the Luxembourg insolvency law?

The Draft Bill provides for the following additional changes to Luxembourg insolvency law:

- **Information gathering:** the preventive measures contained in the Draft Bill are designed to allow for the gathering of certain information from businesses to identify those experiencing financial difficulties at an early stage where they may still benefit from efficient reorganisation procedures. A series of economic indicators (e.g. social plans, debt owed to public authorities, etc.) shall be collected by certain public entities, which will among others analyse whether a bankruptcy petition is appropriate.

- **Second chance:** an entrepreneur exercising his/her activity as a natural person (*i.e.*, without the benefit of a limitation of liability) and whose business has failed may under the Draft Bill be given a "second chance" if he or she is deemed to have acted in good faith (and he/she will not be held personally liable for the outstanding debts of the failed business).

- **Employment law:** under the Draft Bill, as a matter of principle, all the rights and obligations resulting from employment contracts are transferred to the purchaser of the assets of the relevant distressed company; however, contrary to the current regime, the Draft Bill also allows the purchaser to choose the employees that it wants to take over, as long as its choice is dictated by technical, economic and organisational reasons.

- **Sanctions:** certain provisions of the Draft Bill are designed to prevent entrepreneurs acting in bad faith from abandoning their business and starting a new one, thereby escaping any sanctions. To that effect, certain offences will now become easier to prosecute. The scope of liability of directors in a bankrupt entity will also be slightly increased. Finally, The Draft Bill also introduces an administrative dissolution procedure without liquidation inspired by Swiss law and aimed at eliminating "empty shells" in a timely and cost-efficient manner by avoiding formal bankruptcy proceedings.

Related news and content

EVENT
Further insight will be offered during a breakfast seminar to be held on 9 October 2019. **You can register by clicking here**. Webinars will also be organised shortly after the Draft Bill has been voted. Stay tuned!

HELPDESK
In the meantime, should you have any questions please reach out to the Arendt Restructuring & Insolvency team: RIDesk@arendt.com

BROCHURE
Furthermore, should you be interested in learning more about our extensive range of services, **please click here to download our brochure**.

For more information, please contact:

Sébastien Binard
Partner
Commercial & Insolvency

Clara Mara-Marhuenda
Partner
Commercial & Insolvency

Grégory Minne
Partner
Commercial & Insolvency

Paul Mousel
Partner
Commercial & Insolvency

Philippe Wery
CEO
Arendt Business Advisory

Stéphane Joly-Meunier
Counsel
Private Equity & Real Estate