



Luxembourg newsflash

3 October 2019

Restructuring & Insolvency – Briefing note 2/2

This is the second 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. You can read our first briefing note [here](#).

More information about our Restructuring & Insolvency capabilities can be found on our dedicated webpage [here](#).

Part 2 – Adoption of the EU Restructuring Directive

On 16 July 2019 Directive (EU) 2019/1023 of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase efficiency of restructuring, insolvency and discharge of debt (the “**Restructuring Directive**”) entered into force.

The Restructuring Directive ensures that entrepreneurs and companies in financial difficulties can seek support at an early stage in order to keep their business going. Where there is a likelihood of insolvency, Member States must give debtors the opportunity to access a preventive and flexible restructuring framework that enables them to restructure their business in order to prevent insolvency.

The overall goal of the Restructuring Directive is to reduce the barriers to the free flow of capital in the EU, optimise the rescue mechanism for distressed businesses and promote a culture of second chances for failed entrepreneurs.

Most provisions of the Restructuring Directive will need to be implemented by Member States in their national legal frameworks by 17 July 2021.

1) Scope

The Restructuring Directive applies to entrepreneurs (incorporated or not) and to large, small or micro-enterprises engaged in business, trade or other professional activities, with the exception of financial institutions, insurance companies, undertakings for collective investment¹ and certain regulated entities.

It focuses on preventive procedures (i.e. restructuring proceedings) with a view to rescuing economically viable debtors only and as such leaves the Insolvency Regulation² untouched. Indeed, the Insolvency Regulation rather addresses matters of conflicts of law and jurisdiction in cross-border insolvency proceedings and of recognition of insolvency judgements within the EU.

2) Prevention of financial difficulties

The Restructuring Directive provides for certain measures aiming at an **early identification of financial difficulties**. Member States will in particular have to provide businesses with access to early warning tools in order to detect circumstances that could give rise to a likelihood of insolvency at the earliest possible stage. These early warning instruments may include alert mechanisms in respect of unpaid debts, advisory services provided by public or private organisations to the debtor and incentives for certain service providers of the debtor (e.g. accountants) or tax and social authorities to flag a negative development to the debtor.

3) Second chance principle

Over-indebted entrepreneurs³ will have access to automatic **discharge of their debt** after a maximum period of 3 years. Any **disqualifications** from taking up or pursuing a business linked to the over-indebtedness will also end on the date their debt is discharged. Member States will however be allowed to implement certain safeguards in order to prevent abusive situations.

4) New framework for restructuring proceedings

The Restructuring Directive provides for a general **“debtor in possession” principle** requiring businesses subject to restructuring proceedings to continue to operate during the restructuring process, with the debtor remaining in control of its assets and the day-to-day management of its operations. As a consequence, the appointment of an administrator or court-appointed agent will not be mandatory in all cases.

The Restructuring Directive also grants the debtor the benefit of a limited-duration **stay of enforcement** in order to assist with the negotiation of a restructuring plan with creditors. The stay may be lifted at the request of creditors under limited circumstances only. It can initially be granted for a period of up to 4 months but can under certain conditions be extended for a maximum period of 12 months if there is sufficient progress in the negotiations.

¹ UCIs falling within the scope of Directive 2009/65/EC (UCITS Directive (recast)) or Directive 2011/61/UE (AIFM Directive).

² **Regulation** (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on **insolvency** proceedings.

³ Entrepreneurs being natural persons exercising a trade, business, craft or profession.

The debtor will have a **right to submit a restructuring plan** which only “affected parties” (for example creditors, workers, equity holders in certain cases) will have a right to vote on. Unaffected parties will not be required to support the plan as a condition of its adoption. Member States can also decide to exclude certain persons from having a right to vote (such as shareholders, very low ranked creditors and parties related to the debtor having a conflict of interest under national law). The process for adopting a plan is the following:

- **Affected parties** are to be **divided into classes**. The type and nature of interests shall determine the classes (for example, secured creditors, unsecured creditors, etc.). The classes must reflect sufficient commonality of interest based on verifiable criteria, in accordance with national law. As a minimum, creditors of secured and unsecured claims shall be treated in separate classes for the purposes of adopting a restructuring plan. Member States can also determine that workers shall be treated as a distinct class. Finally, the competent national court will examine the classification of affected parties at the latest when the plan is submitted for confirmation.
- A **majority in each class** of affected parties will have to vote in favour of the plan in order for it to be validly adopted. Member States can determine a higher participation and/or majority threshold in each class which shall not go beyond 75% by claim amount or by headcount in each class.
- The plan will need to be **confirmed by a court** if it (i) affects the claims or interests of dissenting affected parties, (ii) provides for new financing, or (iii) involves a loss of more than 25% of the workforce.
- The court is in a position to confirm the plan if (i) creditors with commonality of interest in the same class are **treated equally**, and in a manner proportionate to their claim, (ii) **notification** of the plan has been given in accordance with national law to all affected parties, (iii) where there are dissenting creditors, the plan satisfies a “**best-interest-of-creditors**” test⁴, and (iv) if applicable, any new financing is necessary to implement the plan and does not unfairly prejudice the interests of creditors.
- In the case of **cross-class cram-down** (i.e. when some classes have not approved the plan with the requisite threshold), the plan can still be confirmed by a court if (i) it meets the “best interests of creditors” test, (ii) it has been approved by either (a) a majority of classes of affected parties if at least one of those classes is classified as either secured or senior to unsecured or (b) at least one of the voting classes of affected parties or impaired parties, other than an equity-holder 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 which 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, (iii) the plan ensures that dissenting voting classes of affected creditors are treated at least as favourably as any other class of the same rank and more favourably than any junior class and (iv) no class of affected parties can, under the restructuring plan, receive or keep more than the full amount of its claims or interests.

⁴ This test is deemed satisfied if no dissenting creditor would be worse off under a restructuring plan than such a creditor would be if the normal ranking of liquidation priorities under national law were applied, either in the event of liquidation, whether piecemeal or by sale as a going concern, or in the event of the next-best-alternative scenario if the restructuring plan were not confirmed.

Ultimately, **dissenting minority creditors and shareholders** will not be allowed to obstruct the adoption of restructuring plans of a viable business provided that their legitimate interests are protected. As mentioned further above, the Restructuring Directive sets out the conditions under which a court can confirm a plan that is not supported by all classes of creditors. Plans which are confirmed by a court (whether with the support of all classes of affected parties or not) are binding upon all affected parties.

5) Protection of new-money financings

Member States shall ensure that any new and/or interim financing is not declared void and that the grantors of such financing do not incur civil, administrative or criminal liability because of it being deemed detrimental to the general body of creditors. This protection may, at the option of Member States, be restricted to restructuring plans that have been confirmed by the court. The providers of new or interim financing are also entitled to receive priority payments for their claims in the case of a subsequent insolvency of the debtor which sought the new financing.

6) Equity Holders

According to the Restructuring Directive, Member States shall ensure that equity holders which are excluded from participating in the vote on a restructuring plan are not allowed by other means to unreasonably prevent or create obstacles to the adoption, confirmation and implementation of such a plan.

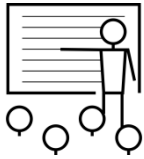
7) Employees

Employees shall, under the terms of the Restructuring Directive, receive full labour law protection in the context of any restructuring. In particular, the existing EU regulations on matters of employment protection shall remain applicable and stays of enforcement should not relate to unpaid salaries. Member States may also decide that employees shall be part of a specific class of affected parties when a restructuring plan is discussed and voted upon. Finally, the existing rights of information of workers shall be maintained in situations where a plan would lead to a material amendment of work organisation or contractual relations between workers and the relevant company.

8) Compliance of draft bill No. 6539 with the Restructuring Directive

It is unknown at this stage whether the government will decide to push through draft bill No. 6539 which was the subject of [our first briefing note](#) in its current form or to revise it in order to adapt it to the terms of the Restructuring Directive. From a preliminary analysis of both instruments, they certainly aim to cover generally similar issues under generally similar objectives (i.e. prevention of insolvency situations, second chance and new and more efficient restructuring processes) although the Restructuring Directive provides for additional requirements as regards preventive measures and procedural constraints to be complied with in restructuring proceedings (e.g. classification of affected parties, cross-class cram-down mechanics, etc.).

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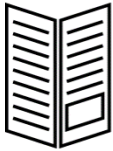
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Further insight will be offered during a breakfast seminar to be held **on 9 October 2019**. **You can register by clicking here**. Webinars will also be organised shortly after the Draft Bill has been voted. Stay tuned!



HELPDESK

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



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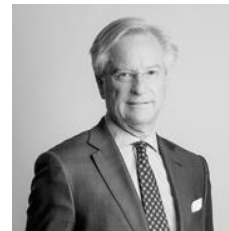
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