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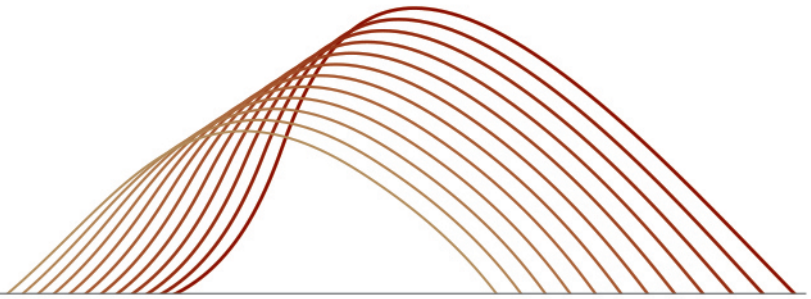

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New EU Regulation on Insolvency Proceedings

By The EU Insolvency and Restructuring Practice

Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast) (the "Regulation") reforms the former European Regulation on Insolvency proceedings (EC) 1346/2000 (the "Original Regulation"). The aim of the Regulation, in particular, is to enhance the effective administration of cross-border insolvency proceedings, establishing a common framework for the benefit of all stakeholders.

The main features of the Regulation are:

- the extension of its application to pre-insolvency proceedings which promote the rescue of economically viable but distressed businesses and give a second chance to entrepreneurs;
- the creation of an EU-wide system of web-based insolvency registers;
- the possibility of avoiding the opening of multiple proceedings and preventing "forum shopping";
- updating the rules on secondary insolvency proceedings to, *inter alia*, extend to "pre-insolvency" or "hybrid" proceedings;
- amending the rules concerning the information for creditors and lodgement of claims; and
- the introduction of new procedures with the aim of facilitating cross-border coordination and cooperation between multiple insolvency proceedings in different Member States relating to members of the same group of companies.

Once adopted, the Regulation will have direct effect in each EU Member State (except for Denmark, as it is not taking part in the adoption of the Regulation and is not bound by it or subject to its application) without the need for separate enactment at a national level. However, some of the provisions will not be effective for another two (2) years after the Regulation comes into force. This is to allow Member States to familiarise themselves with the new provisions. The Original Regulation will continue to apply to proceedings opened before the new Regulation comes into force (*i.e.*, 26 June 2017) (art. 84, paragraph 2).

Once the Regulation is in force it will increase the efficiency of pre-insolvency and insolvency restructuring proceedings, enhance legal certainty, assist in creating a more transparent pan-European distressed debt market, and reduce transaction costs.

I. Extended Scope of the Regulation

The Regulation is applicable to the types of proceedings listed in Annex A of the Regulation, which include public proceedings, interim proceedings (*i.e.*, a temporary stay to allow negotiations with creditors), and pre-insolvency proceedings based on rescue, adjustment of debt, reorganisation, or liquidation, including where the debtor remains in possession, under the control or supervision by a court or the appointed insolvency practitioner. Therefore, the Regulation also applies to proceedings that may be commenced in situations where there is only a likelihood of insolvency and whose purpose is to prevent the debtor's insolvency and/or the cessation of its business activities.

The Regulation shall not apply to confidential procedures or proceedings which refer to (i) insurance undertaking; (ii) credit institutions; (iii) investment firms and other firms, institutions, and undertakings to the extent that they are covered by Directive 2001/24/CE (*i.e.*, any legal person whose main business is the provision of investment services to third parties and/or the performance of investment activities on a professional basis); or (iv) collective investment undertakings (*e.g.*, investment funds).

II. International Jurisdiction

A. Centre of Main Interest ("COMI") and Measures to Avoid "Forum Shopping"

The Regulation better specifies the definition of centre of main interest ("COMI") to be distinguished in the event the relevant debtor is, *inter alia*:

- a company or a legal person—the place of the registered office is presumed to be its COMI in the absence of proof to the contrary. The presumption will only apply if the registered office has not been moved to another Member State within the three (3) month period preceding the filing of the petition for the relevant insolvency proceedings; and

- an individual exercising an independent business or profession—the principal place of business is presumed to be its COMI in the absence of proof to the contrary. The presumption will only apply if the principal place of business has not been moved to another Member State within the three (3) month period preceding the filing of the petition for the relevant insolvency proceedings.

The purpose of harmonized arrangements regarding insolvency proceedings is to avoid assets or judicial proceedings being transferred from one EU country to another in order to obtain a more favourable legal position to the detriment of creditors ("*forum shopping*").

As a general rule, any further insolvency proceedings which have been opened subsequent to the opening of a main insolvency proceeding (*i.e.*, in the Member State where the COMI of the relevant debtor is located) shall be secondary insolvency proceedings (please see paragraph IV below).

Abusive COMI relocation is discouraged. Presumptions as to COMI are refutable and the relevant court will carefully assess whether a debtor's COMI is genuinely located in a Member State and shall specify the grounds on which the jurisdiction of the court is based. Where the circumstances give rise to doubts regarding the court's jurisdiction, the court should ask the debtor to supply additional evidence to support his assertions and give creditors an opportunity to present their views.

If the centre of a debtor's main interests is located within the territory of a Member State, the courts of another Member State will only have jurisdiction if the debtor has an establishment

within the territory of that other Member State and such jurisdiction shall only extend to claims in connection with the debtor's assets located within such territory.

B. Applicable Law and Protection of Third Party Rights

The law applicable to the effects of insolvency proceedings is essentially that of the Member State in which such proceedings are opened. This rule applies in particular to the rank and priority of claims. The Regulation provides for a new exception and specific protection of third party purchasers. In the event a debtor disposes (for consideration) of registered assets (*e.g.*, immovable assets, ships, or aircrafts subject to registration, or securities registered in a mandatory register), the validity of such disposal shall be governed by the law of the Member State where the assets are located or under whose authority the register is kept. No amendments have been made to the rules on claw-back actions and the protection of secured creditors.

III. Enforceability of Other Judgments

The Regulation provides for the direct recognition and enforceability in all Member States of any judgment opening insolvency proceedings handed down by a court of a Member State from the moment that it becomes effective in the Member State of the opening of the proceedings with no further formalities.

IV. Secondary Proceedings

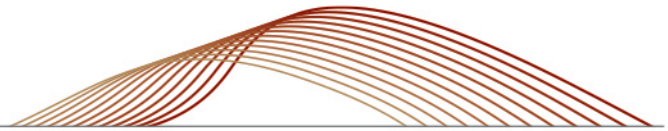
A. Establishment

Secondary proceedings under the Original Regulation can, at present, be opened in a Member State other than the one where the debtor's COMI is located, provided the debtor has an "establishment" in that jurisdiction. As defined under the Original Regulation, an "establishment" is a place of operations where the debtor carries out "a non-transitory economic activity with human means and goods." As alluded to above, the definition of establishment used in the Original Regulation will be amended under the Regulation. In particular, the definition will be altered such that an establishment will only exist if such non-transitory economic activity has been carried out for at least three (3) months prior to the opening of the proceedings.

B. Nature of Proceedings

From a corporate restructuring perspective, the secondary proceedings regime under the Original Regulation often proved unsatisfactory for creditors, particularly in relation to the insolvency of multinational companies with integrated operations. Indeed, historically, the opening of secondary proceedings was often viewed as having a destabilizing effect on main proceedings or other rescue plans, at times hindering the administration of the main proceedings and leading to increased costs with unnecessary duplicative work across borders.

The Regulation seeks to address these concerns by attempting to limit the need to open secondary proceedings through the introduction of so-called "synthetic" or "virtual" secondary proceedings (where an insolvency practitioner in main proceedings provides an undertaking that the distribution and priority rights of local creditors will be the same as if secondary proceedings had been opened). Indeed, under recital 19(a) and Article 29(a) of the Regulation, an insolvency practitioner may request that the court postpone or refuse to open secondary proceedings if they are not necessary to protect the interests of local creditors. This can be demonstrated through the provision of an undertaking. Where such an undertaking is provided and approved by a "qualified majority" (which is to be determined in accordance with the rules that apply to the adoption of restructuring plans under the law of the Member State where secondary insolvency proceedings could have been opened) of "known local creditors," it can be used as a basis to refuse the opening of secondary proceedings.



In addition to obtaining approval, the undertaking will be subject to any existing requirements (as to form and approval for distributions) of the Member State where main insolvency proceedings are opened. The form of undertaking must also follow the requirements prescribed in the Regulation (*e.g.*, it must be made in the official language of the relevant Member State where secondary insolvency proceedings could have been opened). Consequentially, it remains to be seen whether "synthetic" or "virtual" proceedings will become commonplace.

Nevertheless, as the Regulation also provides for enhanced and expanded duties of communication and cooperation between the officeholder in main proceedings and any officeholder in secondary proceedings, it does at least seem that the Regulation will provide considerable scope for the increased exploration of restructuring options and the coordination of restructuring plans between various jurisdictions and processes.

C. Types of Proceedings

In addition to the foregoing, it is also notable that Articles 3(3) and 27 of the Regulation abolish the requirement for secondary proceedings to be winding-up proceedings in circumstances where the court is satisfied that a more suitable procedure is available. Indeed, the Regulation seeks to extend the types of secondary proceedings with the recognition of "hybrid" and "pre-insolvency" procedures. The national laws of Member States have long provided for "pre-insolvency" and "hybrid" proceedings which are aimed at encouraging companies to restructure their debts before matters become critical. As a result of the Regulation, such proceedings (including *sauvegarde financière accélérée* in France; *procedimiento de homologación de acuerdos de refinanciación* in Spain; and *accordi di ristrutturazione dei debiti* in Italy) will now be expressly regarded as secondary proceedings. This development significantly extends the existing range of proceedings available on a secondary basis and could help further facilitate corporate rescue across Member States.

V. Information for Creditors and Lodgement of Claims

The Regulation provides a broader definition of creditors than the Original Regulation, including, in particular, public creditors who are subject to the same rules as private creditors. More generally, it provides for two major innovations: (A) the standardized procedure to file and lodge claims and (B) the reinforcement of the publicity of information relating to insolvency proceedings.

A. Standardization of the Procedure for Filing and Lodging Claims

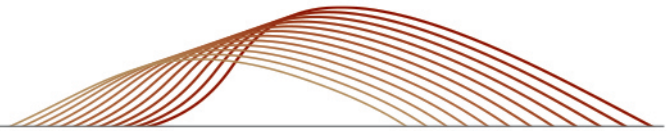
The Regulation creates a European standard claim form to file claims in any Member State.

The procedure to lodge claims provides that "*any foreign creditor may lodge its claim using the standard claims form*." This standard claim form has to be created by the Commission, and will include, in addition to being accompanied by any supporting documents, certain specific information (including, *inter alia*, the debtor's name, contact details, bank details, the amount of the claim, and possible interest claimed) and will specify the interest rate the period of calculation and the capitalized amount of interest.

When a cross-border insolvency procedure is opened under the Regulation, all the creditors have to provide the same essential information to the insolvency practitioner in order to get a clear view of the liabilities of the debtor. It also enables creditors to provide all the information necessary to protect their rights.

B. EU Insolvency Register and Publications

The Regulation introduces a new instrument in order to improve access to information for the relevant creditors and courts and to prevent the opening of parallel insolvency proceedings. In particular, Articles 24 (effective as of 26 June 2018) and 25 (effective as of 26 June 2019) of



the Regulation provide for the creation of a central European database (Article 24), and national electronically searchable databases (Article 25) to be linked together.

Certain essential information must be mandatorily published as soon as possible after the opening of the proceedings (including: (i) the date of the opening of insolvency proceedings; (ii) the relevant court; (iii) the type of insolvency proceedings; (iv) whether the proceedings are main or secondary proceedings; (v) the debtor's name, its registered office and number; (vi) the name and contact details of the insolvency practitioner appointed in the proceedings, if any; and (vii) the time limit for lodging claims, if applicable, or a reference to the criteria for calculating that time limit). Each Member State shall ensure that said mandatory information is available free of charge via the interconnected insolvency registers system.

The interconnected insolvency registers system shall be composed of the insolvency registers of the Member States and the European e-Justice Portal. The system shall provide a search service in all the official languages of the Member States.

The following obligations of the Member States are introduced to ensure access for any interested party to insolvency information:

- an obligation to keep a record relating to cross-border insolvency proceedings open to the public;
- a mandatory level of information which must be contained in the Member States' insolvency registers; and
- an obligation to interconnect the Member States' insolvency registers.

Furthermore, Article 86 of the Regulation imposes an obligation on the Member States to, within the framework of the European Judicial Network in civil and commercial matters, provide a short description of their national legislation and procedures relating to insolvency. Member States are required to regularly update such information and the Commission has to make such information available to the public.

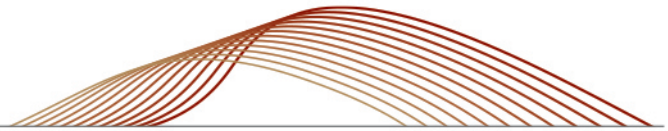
The Regulation provides for an obligation of cooperation and exchange of information between Member States' courts and between the coordinators of the procedures (between primary and secondary procedures and among procedures for different companies in the same group). It is expressly stated that coordination between different Member States' courts may relate to the appointment of coordinators, the exchange of information, the coordination of the management of the assets involved in the proceedings, the hearings, and the approval of protocols.

VI. Insolvency Proceedings of Members of a Group of Companies

As a general consideration, the "one legal entity—one insolvency proceeding" principle remains untouched, *i.e.*, each group member's separate legal personality has to be respected. Consequently, the new provisions regarding group insolvencies are strictly focused on procedural law while the Regulation primarily focuses on cooperation and communication obligations between the different insolvency administrators and insolvency courts involved with the aim to enhance the effectiveness of cross-border group insolvency proceedings.

A. Communication Obligations

Where insolvency proceedings relate to two (2) or more members of a group of companies, certain cooperation and communication obligations are triggered with the stipulated aim of "proper cooperation between the actors" whereas three (3) different communication levels can be distinguished:



- the cooperation and communication between insolvency practitioners;
- the cooperation and communication between courts; and
- the cooperation and communication between insolvency practitioners and courts.

One of the most noteworthy points from a practical restructuring point of view is the strategic objective of the insolvency practitioners to consider the implementation of a coordinated (cross-border) restructuring plan.

B. The Insolvency Practitioner

Insolvency practitioners shall have certain rights, including (i) the right to be heard in any of the other group insolvency proceedings opened, (ii) the right to request a stay of any measure related to the realization of assets in other group insolvency proceedings opened, and (iii) the right to apply for the opening of group coordination proceedings.

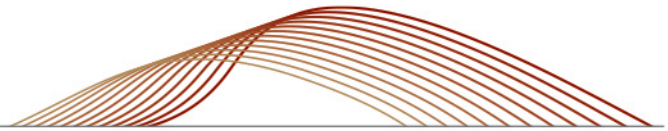
C. Group Coordination Proceedings

To allow for a coordinated (cross-border) restructuring of the group, the Regulation introduces procedural rules on the coordination of the insolvency proceedings of members of a group of companies (the "Group Coordination Proceedings"). This concept forms the largest part of the provisions of group insolvency proceedings since it will likely become the backbone of cross-border insolvency proceedings (irrespective of its voluntary nature).

As a starting point, the Regulation does not introduce a common jurisdiction when dealing with the insolvency for a group of companies in one or more Member States but rather sets out a complex mechanism (based on the principle that each (insolvent) company's legal personality needs to be respected pursuant to the substantive law of its COMI) pursuant to which proceedings may be coordinated with a view to increasing communication and efficiency between processes in different Member States.

The procedural rules for the Group Coordination Proceedings can be summarized as follows:

- specification of the essential elements of the coordination, in particular, an outline of the coordination plan (the "Coordination Plan"), a proposal as to whom should be appointed as group coordinator (the "Coordinator"), and an outline of the estimated costs of the coordination;
- the court seized of a request shall immediately inform the other insolvency practitioners about the request and the proposed Coordinator if, among other things, the court takes the view that the opening of Group Coordination Proceedings is appropriate to facilitate the effective administration of the group insolvency proceedings;
- each insolvency practitioner can either accept the proposal or alternatively object to (i) their participation in the proceedings (in which case the objecting insolvency proceeding does not take part in the Group Coordination Proceedings with a subsequent opt-in right), or (ii) the Coordinator (in which case the court may refrain from appointing the proposed person and invite the objecting insolvency practitioner to submit a new request); and
- in case of a positive decision of the court, with respect to the opening of Group Coordination Proceedings, it shall, among other things, appoint the Coordinator and decide on the outline of the coordination.



The Coordination Plan does not have a binding effect on the other insolvency practitioners and they shall not be obliged to follow, in whole or in part, the Coordinator's recommendations or the Coordination Plan.

D. The Coordinator

According to the Regulation, the Coordinator shall, among other things, propose a comprehensive group coordination plan that identifies, describes, and recommends a comprehensive set of measures appropriate to an integrated approach ("Group Coordination Plan"). In particular, the Group Coordination Plan may contain proposals for the re-establishment of economic performance and the financial soundness of the group or any part of it (however, solely on a stand-alone basis of each entity), the settlement of intra-group disputes as regards to intra-group transactions and avoidance actions and agreements between the insolvency practitioners of the insolvent group members.

The Coordinator has a participation right in each group insolvency proceeding and may mediate any disputes and present the Group Coordination Plan. Further, the Coordinator can request (i) information from any insolvency practitioner in respect of any member of the group, and (ii) a stay for a period of up to six (6) months of the proceedings opened in respect of any member of the group, provided that such a stay is necessary in order to ensure the proper implementation of the Group Coordination Plan and would be to the benefit of the creditors in the proceedings for which the stay is requested, or request the lifting of any existing Restructuring Plan Stay ("Coordinator Stay").

The court shall revoke the appointment of the Coordinator if such appointment is (i) to the detriment of the creditors of a participating group member, or (ii) the Coordinator fails to comply with their obligations.

VII. Conclusions

The Regulation certainly represents a significant step forward in the development of the EU insolvency legislation in order to effect a wider harmonization of insolvency proceedings across the various Member States for the benefit of all stakeholders and possible investors irrespective of their location. In fact, the progress in establishing efficient insolvency rules throughout the EU Member States should undoubtedly help in the development of the high yield market, other forms of lending, and the restructuring of European businesses.

In that context, the centralized EU insolvency register linked with all Member States' local registers providing all necessary information relating to pending insolvency proceedings will create a safer and easy-to-access legal and economic environment that should ensure maximum transparency and fair processes.

Although the Regulation has not significantly innovated the definition and the criteria of COMI, it has introduced specific provisions aimed at preventing abusive forum shopping practices. Moreover, the Regulation has sought to expand the scope of the existing secondary insolvency proceeding regime, as well as the ability for cross-border claims to be dealt with in a more centralized manner, in an effort to produce the same result for creditors without the additional complexity of parallel proceedings.

Last but not least, it must be noted that the coordination and cooperation rules introduced by the Regulation for insolvency of groups of companies seem to provide an efficient framework for cross-border restructurings that was previously missing.

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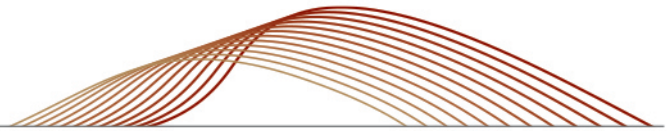

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