INTERNATIONAL **INSOLVENCY** AND **RESTRUCTURING** REVIEW

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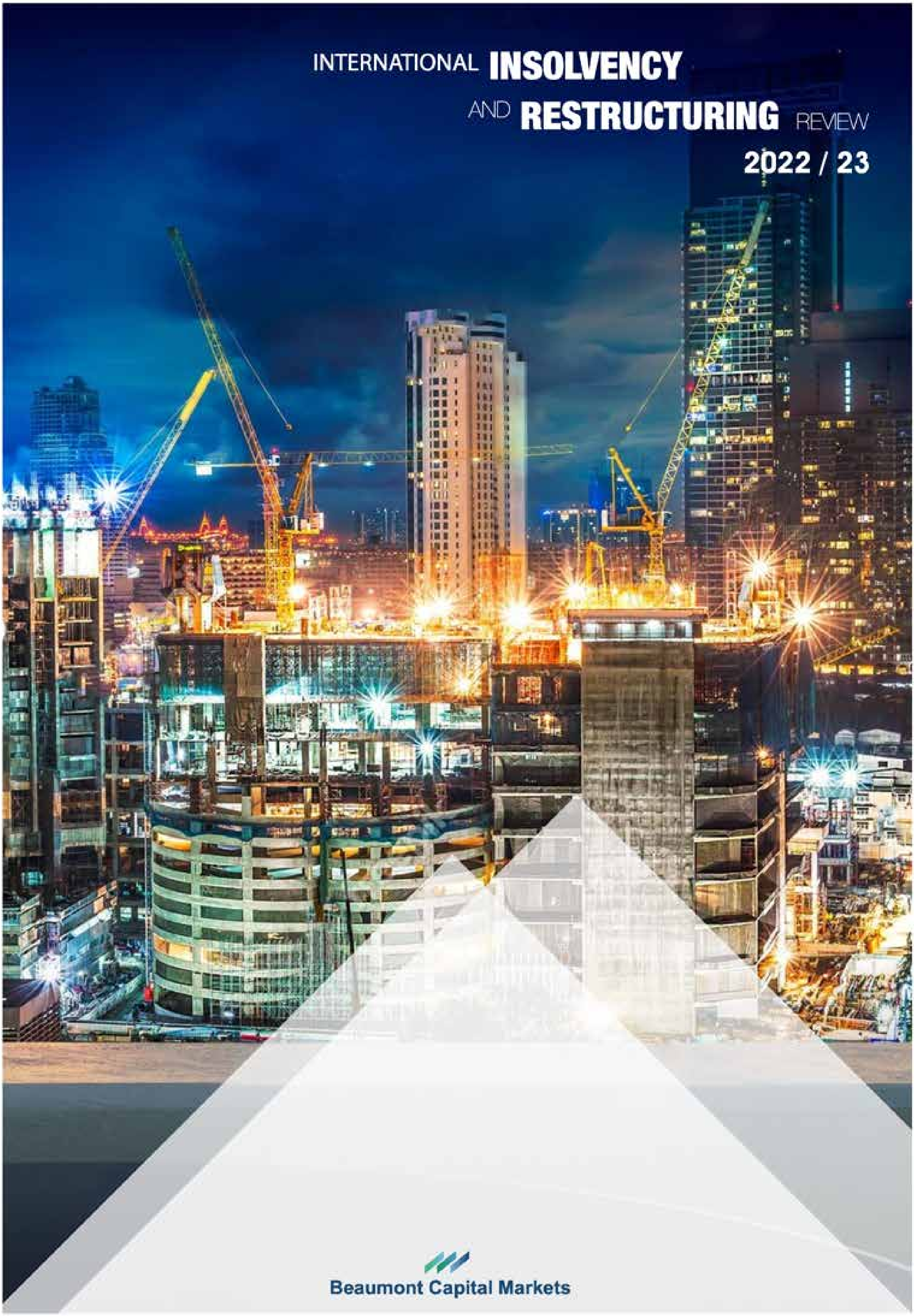

Beaumont Capital Markets

The International Insolvency & Restructuring Review 2022/23

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FOREWORD

Insolvency and Financial Sector Stability: Emerging from the pandemic

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Mahesh joined the WBG's Legal Vice Presidency in 2006 and has since held various positions at both the World Bank and International Finance Corporation. He previously worked at the European Bank for Reconstruction and Development and as an insolvency litigator at a leading Canadian law firm. He has published and taught at the university level and lectured extensively in North America, Europe, Africa and Asia.

Insolvency and Financial Sector Stability: Emerging from the pandemic

The world appears to be exiting the acute phase of the COVID-19 pandemic, but many obstacles to a full economic recovery remain. 2022 began with a welcome milestone: more than half the world has received two doses of a vaccine. However, within this statistic, there is widespread inequality. As of March 2022, more than four fifths of people in low-income countries were yet to receive a single dose[1] and economic recovery appears to be following the trend of vaccine inequality. By 2021, only 21% of low-income countries had recovered to 2019 per capita levels of income, compared to 40% of high income countries.[2]

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In 2020, total global debt reached 263 percent of GDP.

In 2020, total global debt reached 263 percent of GDP, its highest level in half a century.[3] Price increases in key commodities, contributed to by supply chain problems, translate to a substantial additional cost to be borne by businesses and consumers. This will make servicing already elevated debt levels much harder. Some sectors are more vulnerable than others. In industries like tourism and aviation, as projections for a return to pre-COVID levels are being downgraded to 2023 and beyond,[4] so too are the prospects of survival for businesses reliant on a full recovery.

In many countries, the crisis response has included widespread debt relief measures like moratoria and changes to credit reporting requirements. Because many countries have relaxed the rules for non-performing loans during the crisis, it is harder to sort viable from non-viable debtors. As governments wind down these support measures, lenders should expect to see increases in nonperforming loans and bankruptcies. This may exacerbate inequality because banks confronting a decline in loan quality typically limit lending, and those reductions typically hit low-income households and small businesses the hardest. If left unaddressed, rising NPLs can set the stage for systemic banking crises, which are associated with severe recessions and consequent effects on poverty and inequality.[5]

The challenge for policymakers in the near to medium term will therefore be to strike a balance between providing enough support to facilitate recovery, while limiting the longer-term financial and macroeconomic risks that could emerge from higher debt levels resulting from the crisis.[6] Insolvency systems play a critical role in navigating periods of elevated debtor distress. In times of elevated corporate debt, there is an increasing likelihood for “zombie” businesses – businesses that can meet their short term debt obligations but lack a long term path to viability – to proliferate. Such firms create a drag on economic recovery by tying up capital and finance in inefficient enterprises. Inefficient insolvency frameworks make it more likely that banks will continue lending to such firms, in turn prolonging economic crises. Improvements in insolvency systems are also associated with greater access to credit, improved creditor recovery, strengthened job preservation, higher productivity, and lower failure rates for small businesses.[7] Insolvency reforms can therefore equip policymakers with the right set of tools to facilitate the emergence of their economy from the pandemic.[8]

1 Our World in Data, ‘Coronavirus (COVID-19) Vaccines’, data as at 15 March 2022. Available at: https://ourworldindata.org/covid-vaccinations?country=OWID_WRL
2 World Development Report, 2022. Available at: https://www.worldbank.org/en/publication/wdr2022
3 World Bank, Global Economic Prospects, January 2022.
4 For example, the Economist Intelligence Unit forecasts that tourism levels in the Cayman Islands will not return to pre-COVID levels until 2024, and Bain & Company projects air travel demand may not recover to pre-COVID levels by the end of 2023.
5 World Development Report, 2022. Available at: https://www.worldbank.org/en/publication/wdr2022
6 Viral Acharya, Simone Lenzu and Olivier Wang, ‘Zombie Lending and Policy Traps’ (National Bureau of Economic Research, 2021), at p 41; Bo Becker and Victoria Ivashina, ‘Corporate Insolvency Rules and Zombie Lending’ (2021). Available at: https://www.ecb.europa.eu/pub/conferences/ecbforum/shared/pdf/2021/Ivashina_paper.en.pdf.
7 World Development Report, 2022. Available at: https://www.worldbank.org/en/publication/wdr2022
8 A revised version of the World Bank’s Principles for Effective Insolvency and Creditor/Debtor Regimes, a blueprint for effective insolvency laws, was published in 2021. They are available at: https://openknowledge.worldbank.org/handle/10986/35506

AUSTRALIA

A joint sitting of international courts – solving the cross-border insolvency of an online financial services provider

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Morgan has over 30 years' experience in advisory, workout and insolvency across a wide range of industries. This experience has involved formal appointments, expert reports and informal advisory roles throughout Australia, New Zealand and throughout Asia in several jurisdictions on domestic and cross border Insolvency and Restructuring engagements.

These engagements include advising corporates, financiers, government agencies and the World Bank / IMF, focused particularly on assisting financially distressed businesses and financial institutions both on an organisation and sector level.

Morgan has a Masters Degree in Commerce and is a member of the Institute of Chartered Accountants in Australia and New Zealand. He is a registered Liquidator in both Australia and New Zealand, and is a Fellow of the Australian Restructuring, Insolvency and Turnaround Association.

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Phil has 18 years of restructuring, turnaround and insolvency experience in Australia and the UK. His experience includes formal appointments, multi jurisdictional restructurings and informal advisory roles in businesses ranging in size from SMEs to multinational organisations.

Phil has extensive experience in Trans-Tasman (Australia/ New Zealand) insolvencies including Halifax Investment Services, Dick Smith Retail and Borders Bookstores.

Phil hold a Masters Degree in Civil Engineering from the University of Bristol (UK). He is a Fellow of the Institute of Chartered Accountants in England & Wales, a member of Chartered Accountants Australia & New Zealand and a member of the Australian Restructuring Insolvency & Turnaround Association. He is also a Registered Liquidator in both Australia and New Zealand.

A joint sitting of international courts – solving the cross-border insolvency of an online financial services provider

Australia has seen various corporate insolvencies of investment management firms over the last ten years, where there has been a deficiency in collateral held on trust for investors.

In such circumstances, by virtue of their appointment as voluntary administrator or liquidator to the company, the insolvency practitioner may become trustee of the trust. A significant challenge arises when there is both a deficiency and commingling of client moneys, such that it is not possible to trace back to an investor's individual entitlement. This challenge only becomes more complex when dealing with cross-border claimants.

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> In November 2018, the HIS entities in Australia and New Zealand went into voluntary administration

This raises a range of issues for an insolvency practitioner that requires judicial advice and directions, including:

- How the deficiency should be treated amongst the investors?
- Whether some or all trust assets should be pooled? In what manner should they be pooled?
- When should close out of investments occur?
- What should be the claim date for the calculation of investor entitlements?

One of the key case developments in Australia has been the liquidation of Halifax Investment Services Pty Limited (in liquidation) (HIS), which has provided further clarity on the approach for seeking judicial advice and directions to deal with a deficient mixed fund in relation to trust assets held across different jurisdictions.

Single deficient mixed fund – commingling of trust assets across different jurisdictions

HIS was a licensed financial services provider that offered various white label trading platforms to over 12,000 predominantly retail investors located in 65 countries.

The group's head office operations were domiciled in Australia, with additional sales offices in New Zealand and China.

Investors contracted with either the Australian or New Zealand entity, and invested in a range of financial products on public exchanges with HIS acting as intermediary. HIS was also the provider of certain over-the-counter (OTC) financial products directly to investors.

Under Client Money Rules, HIS was required to hold investor funds on trust, which would then be used to purchase investments in accordance with the investor's instructions. These investments were held by a custodian in HIS's name on behalf of the investor, with the investor having no direct contractual arrangement with the public exchange or custodian.

In November 2018, the HIS entities in Australia and New Zealand went into voluntary administration under the Australian and New Zealand regimes respectively with the same practitioners appointed in both jurisdictions.

Following appointment, investigations indicated a deficiency of approximately A$20 million in client funds. In addition, following a review of over 10,000 transactions through HIS's bank accounts, it was determined that in over 98 percent of cases it was impossible to trace which investor funds had been used to purchase which investments.

There was extensive commingling of funds between trading platforms and jurisdictions. This in effect created one single deficient mixed fund.

Open investor positions following appointment

The liquidators recognised that they were dealing with trust assets and would require judicial advice or direction from the courts in both jurisdictions before distributing or realising these assets.

Not only was there a deficient mixed fund, there were also certain categories of investors who claimed that their entitlement was traceable and preferred a distribution in specie of their investment rather than a cash distribution. The liquidators formed the view that a liquidation of the portfolio was premature pending the courts hearing the competing arguments from investors and providing direction on how the deficient mixed fund should be treated as amongst the beneficiaries.

All investor accounts were frozen upon appointment which prevented any investor from being able to purchase any additional equities or make any new trades through HIS. Investors could however close any open positions that existed as at the date of appointment, at their own discretion.

This position was maintained until after judicial advice and directions were received.

Key challenge – consistency of outcome

The nature of the commingling presented the unique challenge of requiring judicial advice and directions from courts in both Australia and New Zealand in relation to the same deficient mixed fund. If the applications were run independently, there was a risk of inconsistent or conflicting directions in relation to the same funds, which could create a situation of deadlock. This would prevent a timely resolution which in turn would impact investors.

Access to justice was also an important point of consideration. HIS held approximately 12,000 client accounts, with investors based across 65 jurisdictions (with a significant majority based in Australia and New Zealand). Many investors were individuals, some of whom had invested relatively significant amounts of their savings with HIS.

The holding of any physical hearings in both Australia and New Zealand would provide clients in each jurisdiction with the opportunity to be heard in person, without the need to travel from Australia to New Zealand or vice versa. Such an approach would reduce some of the barriers for investors to participate and be heard in any proceedings, if they wished to do so.

UNCITRAL Model Law on Cross-Border Insolvency – an available mechanism to resolve the jurisdictional issues?

A relevant consideration for the Liquidators was whether simultaneous applications should be made seeking recognition in both jurisdictions to enable a coordinated approach.

The HIS case involved two separate entities (in Australia and New Zealand respectively), and although they were in the same corporate group, the provisions of the Model Law enacted into legislation in the two jurisdictions only provide for assistance in relation to the same entity as opposed to multiple entities within the same group. On one view the UNCITRAL provisions did not increase the chances of consistent rulings, and on another they may not have applied at all.

However, the court rules of both countries included provisions for the courts of each country to provide "assistance" to each other when required and could form the basis of a request a joint sitting.

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Co-operation between courts – "classic candidate" for cross-border collaboration

An application was made to the Federal Court in Australia for judicial advice and directions in respect of HIS's Australian entity, with a parallel application made to the High Court in New Zealand in respect of the New Zealand entity.

The Courts agreed to a joint sitting, setting a precedent for courts in Australia or New Zealand sitting jointly with a court from another country. The joint sitting meant that the judges could confer, but more importantly that they could hear the same evidence at the same time and in doing so would be as informed as each other. Further, any representatives would be able to appear in their own jurisdictions, but evidence would be available to both courts.

Both courts received the same submissions and heard the same evidence but delivered separate judgments with each court reaching its own conclusions and expressing its own reasons for doing so.

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The Federal Court in Australia accepted submissions that HIS was a “classic candidate for cross-border cooperation between courts to facilitate the fair and efficient administration of the winding up”.

The courts had intended to physically sit jointly in both Australia and New Zealand to hear the proceedings. However, due to the impact of COVID restrictions, the hearings were conducted virtually with counsel physically present in each location.

Representative respondents – ensuring the courts heard the views of investors

Given the nature of the application for judicial advice and directions in this case, the liquidators were an impartial party seeking direction from the courts.

In order to ensure the key issues of contention were sufficiently ventilated before the courts, representative respondents were appointed. Some of these issues were significant for the body of investors, especially the date on which claims were to be valued given the fact that a significant proportion of the assets under management on the various platforms operated by HIS remained in market traded assets, and so were moving in value continuously, and the value of many investors’ portfolios had increased above their value as at the date the liquidation commenced.

The representative respondents were separated into categories and argued in favour of certain positions, including:

- On the one hand, that the date at which the claims of investors should be valued for the purposes of calculating a proportionate entitlement to a distribution should be either the date of the insolvency event and, on the other hand, claims should be valued as at the date the portfolio was ultimately liquidated. This was highly relevant to investors whose portfolios had moved in value and their proportionate claim in relation to a distribution could be significantly impacted.

- The manner in which distributions should be affected, whether by a liquidation of the portfolio and distribution of cash, or whether assets should be distributed to investors in specie.

- Treatment of investments that had not been traded by investors since they were transferred in to one of the HIS operated investor platforms, and therefore they were not affected by the deficiency and could be traced.

In total there were five categories of representative respondents who had counsel appointed to represent them and argue their positions before the court.

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Judicial process – ability and willingness of international courts to co-operate

The Federal Court in Australia and High Court in New Zealand sat jointly for a two-week partly in-person and partly virtual hearing, in which they heard substantial evidence from the liquidators as well as the representative respondents. Following a period of deliberation, the courts handed down their separate judgments and made orders on the same day. The orders provided a uniformity of outcome and avoided any inconsistent directions in relation to the same assets.

An appeal was lodged by an investor who claimed that the courts had erred in their assessment of the claim date for calculation of investor entitlements. The appeal was heard by three Australian judges in the Full Federal Court of Australia and three New Zealand judges in the New Zealand Court of Appeal. Both courts dismissed the appeal.

The HIS matter demonstrates the ability and willingness of courts to co-operate in relation to cross border insolvencies to facilitate a fair and efficient winding up.

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BELGIUM

The International Insolvency and Restructuring Review
Key developments and the latest trends in Belgium

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He has a strong experience in insolvency procedures (bankruptcy, liquidation, judicial reorganisation), business restructuring and corporate law. He acts on a regular basis for creditors, banks and companies in distress. He is regularly appointed as trustee and liquidator by the Undertaking Court of Brussels. He is also an experienced litigator in commercial and corporate matters, white collar crimes and directors liability.

He has over 15 years of professional expertise in business restructuring and insolvency law: law on continuity of undertakings, collective negotiations with creditors, debts restructuring and haircuts, distressed acquisitions and transfers under supervision of the Court, bankruptcy and liquidations.

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Stéphanie Nachsem is a member of the Brussels Bar since 2021.

She practices in commercial law and business restructuring, with particular focus on litigation, insolvency law and judicial reorganisation procedures.

She advises companies in the context of commercial dispute resolution. She also assists within the framework of bankruptcy operations, notably assets recovery and directors' liability.

She holds a Master's degree in Business law from the University of Liège, during which she took part to the 28th Willem C. Vis International Commercial Arbitration Moot (Vis moot). She also did an exchange program at the University of Kobe (Japan) in International Business Law.

Introduction

Faced with the COVID-19 crisis and the wave of bankruptcies predicted by economists, the Belgian authorities reacted quickly to reduce the harmful effects of the pandemic on the economy as much as possible. As a result, innovative solutions appeared in Belgian company law. In particular, a royal decree of 24 April 2020 known as the "bankruptcy moratorium", a law of 20 December 2020 granting another moratorium and a law of 21 March 2021 reforming insolvency law are the result of this prompt and innovative reaction.

> "Several interventions at national level also helped to limit the effects of COVID-19 on the economy.

While the moratorium attempted to reduce the direct impact of COVID-19 on the economy by preventing tax and social security administrations from pursuing companies in default, the law of 21 March 2021 attempts to fill gaps historically present in Belgian insolvency law by widening access to judicial reorganisation procedures and limiting certain adverse effects on the value of the company in the preparatory phase of these procedures.

In this article we will also discuss the most recent developments and the impact of the forthcoming transposition of the European Restructuring Directive.

Impact of the COVID-19 crisis in Belgium from the point of view of insolvency law and measures implemented by the ECB and the Belgian authorities

Measures adopted

The massive financial intervention taken at European level, namely the "Pandemic emergency purchase programme" set up by the ECB in March 2020 was undoubtedly the first support granted to Belgian companies. This programme was implemented to facilitate access to affordable financing for individuals and companies, with a budget that has been successively increased to reach the colossal amount of EUR 1,850 billion.[1]

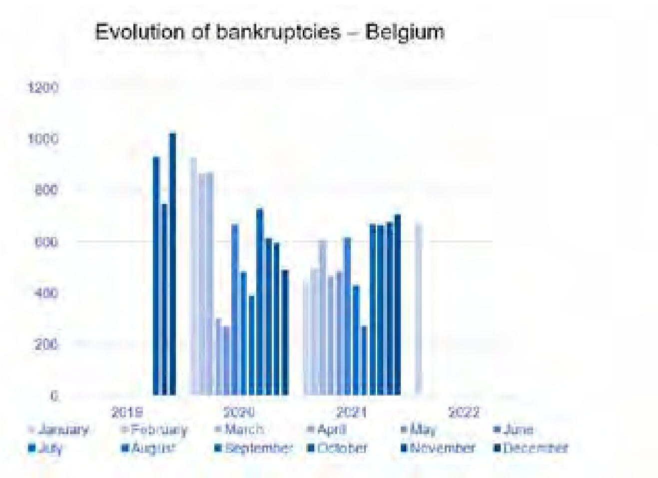
In addition to this financial programme set up at the level of the ECB, several interventions at national level also helped to limit the effects of COVID-19 on the economy. In particular, the Belgian government issued a royal decree granting a temporary reprieve to companies corresponding to a temporary moratorium ("cease-fire") during which any debtor company was protected against enforcement measures and a declaration of bankruptcy (from 24 April 2020 to 17 June 2020). By virtue of the law of 20 December 2020, another moratorium was granted from 20 December 2020 to 31 January 2021. These two successive periods correspond to the first two crisis waves.[2]

However, in between these two moratoria, the Belgian tax administration and the Belgian social security institution, which are at the origin of the majority of bankruptcy summons in Belgium, decided to renounce to introduce such procedures, which had the effect of creating a *de facto* moratorium. This practice remained in force after 31 January 2021 and it was only very recently (November 2021) that the Belgian social security institution announced that it would gradually resume bankruptcy summons.

Evolution of bankruptcies and the M&A market

These moratoria, combined with the massive intervention of the ECB and the bonuses and payment deferrals granted by the Belgian authorities, undeniably had the effect of greatly reducing the number of bankruptcies pronounced in Belgium throughout the crisis. The number of companies in financial difficulty was indeed halved thanks to government and European measures.[3] Paradoxically, given the violence of the crisis, the latest figures for September, October, November, December 2021 and the beginning of 2022 are still well below the pre-crisis figures for the last months of 2019.

1. European Central Bank, Pandemic Emergency Purchase Programme, accessed on 17 February 2022, at https://www.ecb.europa.eu/mopo/implement/pepp/html/index.en.html
2. Royal decree nr. 15 of 24 April 2020 on the temporary suspension for companies of implementing and other measures for the duration of the COVID-19 crisis, M.B., 24 avril 2020; Law of 20 December 2020 on various temporary and structural provisions relating to justice in the context of the fight against the spread of the coronavirus COVID-19, M.B., 24 December 2020.
3. *Graydon, Nombre d'entreprises en difficulté financière réduit de moitié grâce aux mesures gouvernementales*, 9 January 2020, Graydon, accessed on 20 January 2022, at https://graydon.be/fr/nombre-dentreprises-en-difficulte-financiere-reduit-de-moitie-grace-aux-mesures-gouvernementales.

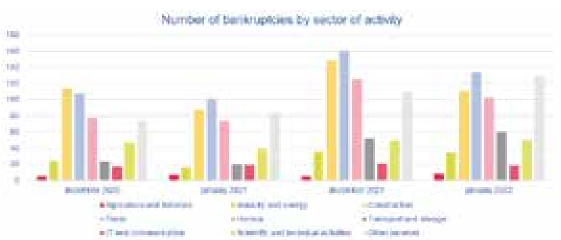


[4]

In 2021, the M&A market rebounded strongly from the sharp decline in 2020, which saw a near-total halt in activity in the early months of the COVID-19 crisis. Nearly EUR 30 billion of deals were completed, half the amount of last year when the market collapsed to EUR 20 billion due to the outbreak of the pandemic.[5] This is due to rapid growth in certain sectors, mainly technology (telecommunications, media) or the pharmaceutical industry, the credibility of institutional recovery plans, and the persistence of low interest rates.

Sectors concerned

As regards the sectors most affected by the crisis, the hotel and catering sector, the commercial sector in general and the construction sector clearly stand out. In contrast, the IT sector and the agriculture and fisheries sectors have only been slightly affected. It is therefore not surprising that the bans and restrictions imposed by the government during the COVID-19 waves are reflected as follows in terms of the number of bankruptcies per sector of activity.



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Strategic options from a distressed perspective – legal perspectives and recent developments

General

Under Belgian law on judicial reorganisation, three safeguard options are provided for companies facing difficulties to avoid bankruptcy. As a reminder, the objective of judicial reorganisation procedures is to allow the debtor in difficulty to avoid bankruptcy and to effectively continue its activities while restructuring them (ie the equivalent of Chapter 11 of the *United States Bankruptcy Code*). The judicial reorganisation procedure will be organised through the granting by the Court of a suspension period during which enforcement measures for debt recovery are frozen. At the end of the suspension period the company in difficulty will have to present a reorganisation plan, or a sufficiently credible disposal project to obtain approval from the Court. This can be achieved by negotiating an agreement with its creditors on its debt, either by negotiating an amicable agreement with some of them (*accord amiable/minnelijk akkoord*) or a collective agreement which will involve all creditors (*accord collectif/collectief akkoord*), or by transferring all or part of its business, under the supervision of the Court (*transfert sous autorité de justice/overdracht onder gerechtelijk gezag*). During the whole process, the debtor remains, in principle, in control of its activities.

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Under Belgian law on judicial reorganisation, three safeguard options are provided for companies facing difficulties to avoid bankruptcy.

4. *Statbel, Faillites mensuelles*, 17 February 2022, STATBEL, accessed on 25 February 2022, at https://statbel.fgov.be/fr/themes/entreprises/faillites/faillites-mensuelles.
5. *S. Souris, M. Sephiha, Millésime 2021 fructueux sur le marché des fusions-acquisitions*, L'Echo, 31 December 2021, accessed on 15 January 2022, at https://www.lecho.be/entreprises/general/millesime-2021-fructueux-sur-le-marche-des-fusions-acquisitions/10356590.html.
6. *Statbel, Faillites mensuelles*, 17 February 2022, STATBEL, accessed on 25 February 2022, at https://statbel.fgov.be/fr/themes/entreprises/faillites/faillites-mensuelles.

First issue – disruption of the initial idea of the procedure of reorganization by transfer

In the context of a judicial reorganisation, the main objective of the transfer of the business (third alternative listed above) is the continuity of the business by a transferee. The current Article XX.89 of the Economic Law Code (ELC) governing the procedure provides that, in the event of comparable offers, priority must be given to the offer that guarantees the permanence of employment. In accordance with Article XX.86, §3 ELC and collective labour agreement no. 102, the candidate-taker is, however, free to decide which employees will be taken over. The advantage of the transfer under judicial authority is that the transferee can decide to take over a company in difficulty without having to take over the entire workforce.

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> With a view to adapting Belgian law to European law following the Plessers judgment, a bill was tabled on 21 October 2020.

This possibility left by Belgian law to the candidate-taker has nevertheless recently been overturned following the Plessers judgment of 16 May 2019 rendered by the Court of Justice of the European Union.[7] The Court decided that the absence of an obligation for the transferee to take over all the employees in the context of a transfer under judicial authority was contrary to European law and more particularly to Directive 2001/23/EC on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses.

Until the law is changed in this respect, the Belgian law in force, although contrary to the Directive, remains applicable to judicial reorganisation transfer.

With a view to adapting Belgian law to European law following the Plessers judgment, a bill was tabled on 21 October 2020. According to the envisaged changes, the transfer under judicial authority would be profoundly revised and would have as its main objective a liquidation of the legal person or the assets of the company, in circumstances that are in the interest of the creditors. Additional safeguards would also be provided to prevent a reorganisation procedure from being used to circumvent the existing rules on social plans. Although the purchaser would be free not to take over all the employees, they would be obliged to give reasons for their choice. These changes resulting from the Plessers ruling will most probably be incorporated into the law transposing the European Directive on restructuring and insolvency.

Second issue – low success rate of judicial reorganisation and legislative change to reduce adverse effects – Law of 21 March 2021

The success rate of judicial reorganisation proceedings currently stands at a low rate of 25%.[8]

These procedures are actually most effective for companies that (i) are profitable or have a prospect of profitability with a good future business plan, but (ii) are faced with too much debt that is crippling them.

Moreover, this rate is also explained by the fact that these procedures impose a significant challenge on the company that decides to resort to them: the immediate loss of value and reputation as a result of the publications imposed by the opening of the judicial procedure. The suspension period is indeed granted to a company if the reorganisation procedure is published in the Belgian Official Gazette (*Moniteur Belge/Belgisch Staatsblad*) and in the Belgian register of companies (*Banque Carrefour des Entreprises/Kruispuntbank van Ondernemingen*). It goes without saying that such a publication inevitably leads to distrust on the part of the various economic players. This results in delivery stoppages or demands for upfront payment, demands for additional guarantees from suppliers and banks, and loss of customers. In many cases, the mere initiation of such proceedings brings the company into serious disrepute.

7. CJUE, judgment Plessers, 16 May 2019, C-509/17, ECLI:EU:C:2019:424.
8. P. Lambrecht, N. Ragheno, « Continuité des entreprises : succès ou faillite de la loi ? », Wymeersch, E. and al. (ed.), het vennootschapsbelang, 1e edition, Brussels, Intersentia, 2017, p. 305.

The COVID-19 crisis has shown the need to remedy these difficulties by making the judicial reorganisation procedure more flexible and improving its effectiveness. The legislator has decided, by a law of 21 March 2021 amending Book XX of the Economic Law Code and the Income Tax Code 1992, to facilitate access to judicial reorganisation procedures and remedy their adverse effects.

The law of 21 March 2021 has made the following changes to Belgian insolvency and restructuring law:

(i) simplification of the admission to the judicial reorganisation and the documents to be produced by the debtor in support of its application;

(ii) creation of a tax exemption for write-downs and provisions on claims on counterparties for which a reorganisation plan has been approved or an amicable agreement has been established during the taxable periods until the plan or the amicable agreement has been fully implemented or the procedure has been closed;

(iii) introduction – and this is the most important innovation – of the possibility of a preparatory agreement and a discrete and accelerated judicial reorganisation procedure to remedy the above-mentioned difficulties related to the publicity measures involved in the introduction of the procedure (referral);

(iv) possibility for the debtor to request itself the appointment of a judicial representative (a person in charge of assisting the debtor in reaching an amicable agreement with the creditors or in drawing up a reorganisation plan), whereas previously only the public prosecutor or any interested person (creditors) was authorised to do so. Furthermore, the court can also appoint a judicial representative when events lead to the ungovernability of the company.

Latest developments in Belgian law and future transposition of the EU Restructuring directive 2019/2013

Last developments in judicial reorganization: prepack option

As introduced below, Article 6 of the law of 21 March 2021 has implemented a confidential judicial reorganisation procedure in Belgian law by means of the new article 39/1 inserted in the ELC.[9]

The main objective of this specific procedure, known as the "prepack" is to preserve as much as possible the value and reputation on the market of the company whose continuity is threatened.

The prepack involves requesting the appointment by the Court of a judicial representative who will be in charge of assisting the debtor in the judicial reorganisation. The judicial representative will facilitate negotiations with one or more creditors with a view to concluding an agreement or a reorganisation plan. This appointment is not published.

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> Since the procedure is confidential, it will not automatically suspend the payment of third-party claims.

Hence, the procedure allows the analysis of the possibility of a judicial reorganisation in a strictly confidential framework, to avoid undermining the credit of the company.

Since the procedure is confidential, it will not automatically suspend the payment of third-party claims. No suspension period will therefore be granted. However, the judicial representative will have the possibility to request from the Court, simultaneously with the confidential procedure, terms for the payment of certain debts, proportionate to the needs of the company in difficulty. The duration of such suspension period may not exceed four months (Art XX.39/1, § 3 ELC). The aim is therefore to save the company by minimising the harmful effects of the publicity of the procedure.

9. Law of 21 March 2021 amending Book XX of the Economic Law Code and the Income Tax Code 1992, article 6, M.B., 26 March 2021.

Once the judicial representative has reached a preparatory agreement with one or more of the creditors, the law allows the binding vote and homologation route to be used to impose measures on opposing creditors (including abatements of claims). The procedure will therefore be accelerated and the judicial representative will only refer the matter to the court when they are of the opinion that there is a favourable vote likely to take place. Publicity will therefore take place in the final stages of the procedure.

Most of the provisions of the law of 21 March 2021, and more specifically Article 6 that inserted the above-mentioned confidential judicial reorganisation, were initially in force until 31 June 2021, but were finally extended until 16 July 2022. This extension is in line with the European Directive 2019/1023 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) of 20 June 2019. Belgium has been granted an additional year to implement the directive. The transposition of the latter is therefore expected by 17 July 2022 at the latest. The confidential judicial reorganisation introduced by the law of 21 March 2021 is therefore not intended to disappear from the Belgian legislative arsenal but will obviously be taken up in the law transposing the directive.

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> A new restructuring and insolvency Belgian law is expected in the coming months to transpose the EU Insolvency Directive 2019/1023.

However, Articles 3, 13 and 14 of the law of 21 March 2021 will only enter into force on 1 January 2023.[10] In particular, Article 13 will allow creditors taking part in a collective agreement to vote electronically (double majority required for approval – in number and in debt), according to the procedures determined by the delegated judge.

New Belgian law on restructuring and insolvency transposing the EU Directive 2019/1023

A new restructuring and insolvency Belgian law is expected in the coming months to transpose the EU Insolvency Directive 2019/1023.[11] In line with the requirements of the directive, the new law will notably focus on a preventive restructuring procedure and strengthening the procedure allowing for debt remission. In addition, the consequences of the CJEU Plessers judgment will be integrated.

Preventive restructuring

Inspired by the French and German existing frameworks, the Directive aims at setting a preventive restructuring framework enabling the debtor to act at an early stage, to avoid liquidation.[12]

Article 4 of the Directive calls on Member States to 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, thereby protecting jobs and maintaining business activity.[13]"

This framework "may consist of one or more procedures, measures or provisions, some of which may take place out of court, without prejudice to any other restructuring frameworks under national law."

10. Y. Brulard, Le preinsolvency à la suite de la loi du 21 mars 2021 réformant le livre XX du Code de Droit économique : une opportunité de mettre en œuvre des techniques de restructuring créatives, R.G.F.C.P., 2021, liv. 6, 5-20.
11. Directive (EU) 2019/1023 of the European Parliament and 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), OJ L 172, 26.6.2019, 18-55.
12. E. Russo, *The EU Directive on Restructuring and Insolvency and the Strengthening of the Creditor's Role in the Course of Restructuring Procedures*, JD Supra, 15 April 2021, accessed on 2 February 2022, at https://www.jdsupra.com/legalnews/the-eu-directive-on-restructuring-and-4168881.
13. Directive, Art 4.

Article 4 therefore requires Belgium to have a pre-insolvency procedure, such as the one temporarily introduced by the Belgian legislator by the law of 21 March 2021. The legislator has already indicated its intention to keep this confidential reorganisation procedure in the context of a brand-new private procedure that will retain the strictly confidential nature of the procedure and the possibility of requesting a suspension period that may not exceed four months.

Class voting

In addition, the Directive introduces the obligation to treat creditors in separate classes for the purposes of adopting a restructuring plan in such a way as to reflect their rights and the seniority of their claims and interests.[14] There currently exists no system of voting in different classes under Belgian insolvency law. All creditors vote together in one single class despite the significant difference in restructuring measures they can be subject to. In accordance with the Directive's requirements, a class voting system will therefore now be introduced into Belgian law to prevent vulnerable creditors from being treated unfairly in business restructurings. The question however still remains how farreaching the new Belgian voting system will be as the Directive allows for several derogations to this principle. For example, there is no requirement to divide creditors into more than two classes (unsecured and secured) and SMEs could be exempted.

(see Dengler J., *The impact of the EU Restructuring Directive on the Belgian collective plan: "To class or not to class?" – that's the question for the Belgian legislator*).[15]

Economic signals for the detection of companies in financial difficulties

Furthermore, the aim of the Directive is also to detect early on circumstances that could lead to insolvency and to remedy them through rapid procedures or measures to maintain or restructure the business and to avoid insolvency. Managers should therefore look after the interests of all stakeholders and take all measures to avoid insolvency (Article 19).[16] To this end, the Directive provides for the establishment by Member States of "early warning tools" to detect situations that could give rise to the likelihood of insolvency; for example, through the use of computer technology (Article 3).[17]

The latter has already been introduced in Belgium by the Royal Decree of 13 June 2021[18] that sets up a central register of economic indicators for the detection of companies in financial difficulties. However, it will undeniably be formally implemented by the upcoming law. The objective of this register is to help the Chambers for Enterprises in Difficulty to identify enterprises under its jurisdiction that are experiencing financial difficulties that could jeopardise the continuity of their economic activities. To this end, relevant indicators are collected in the register on the basis of a unique identifier, namely the enterprise number. These relevant indicators relate to the number of debts that must legally be communicated to the Company Court, seizure notices, the financial health indicator calculated by the National Bank of Belgium, the number of employees of the company and regular changes of registered office.

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> There currently exists no system of voting in different classes under Belgian insolvency law.

Debt remission and last developments on hard bankruptcy

With regard to insolvency procedures and impacts, the Directive insists on the possibility for insolvent entrepreneurs to apply for a "procedure which may lead to a total remission of debts" (Article 20).[19]

14. Directive, recital 44.
15. J. Dengler, The impact of the EU Restructuring Directive on the Belgian collective plan: "To class or not to class?" – that's the question for the Belgian legislator, Corporate Finance Lab, 3 December 2021, accessed on 24 February 2022, at https://corporatefinancelab.org/2021/12/03/the-impact-of-the-eu-restructuring-directive-on-the-belgian-collective-plan-to-class-or-not-to-class-thats-the-question-for-the-belgian-legislator/.
16. Directive, Art 19.
17. Directive, Art 3.
18. Royal decree of 13 June 2021 on the central register of economic indicators for the detection of companies in financial difficulties, M.B., 25 June 2021.
19. Directive, Art 20.
20. Belgian Constitutional Court, judgement 151/2021, 21 October 2021, https://www.const-court.be/public/f/2021/2021-151f.pdf

Belgian law already provides for such debt remission at the request of the debtor. However, the Constitutional Court annulled Article XX.173, § 2, of the ELC insofar as it provides that the bankrupt natural person who does not submit a request for debts remission within the foreclosure period of three months after the publication of the bankruptcy judgment irrevocably loses the right to this cancellation. This was considered by the Court to considerably broaden the possibility of having recourse to this measure in time and therefore annulled by the judgment of 21 October 2021.[20]

Finally, the Directive also deals with the time limit for disqualification from engaging in commercial activity, limiting it to the expiry of the period for remission of debts. Under Belgian law, the bankrupt natural person is allowed to engage in a new professional activity from the day after the bankruptcy judgment, unless he has been subject to a professional ban by the Court.

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> We commend the efforts of the legislator, who is trying to provide real answers to the difficulties encountered by the debtor.

Perspectives for the future and conclusion

In the context of the future transposition of the Directive, the Belgian legislator has a relatively wide margin of appreciation and can either follow a minimalist approach, seeking approximations with existing instruments, or opt for a maximalist approach which optimises the procedures for safeguarding companies. The legislator has already indicated its intention to keep the confidential reorganisation procedure and to widen access to the existing procedures. With a view to preserving the rights of creditors, the legislator plans to incorporate into Belgian law the differentiation by classes of creditors within the framework of the vote of a reorganisation plan.

On the one hand, we commend the efforts of the legislator, who is trying to provide real answers to the difficulties encountered by the debtor by mitigating the harmful effects on company’s credit of reorganisation procedures. The use of a confidential procedure, insofar as it aims to remedy a major weakness in our law, could in fact prove to be really effective in safeguarding the value of companies facing difficulties. As a result, the chances of recovery might be higher. On the other hand, we insist on the need to set limits on legislative intervention. The balance of interests between creditor and debtor must always be respected, meaning that the interests of the creditors should never be disregarded.

However, we believe that the upcoming legal changes do not intend to avoid bankruptcy at all costs but to avoid bankruptcy when the prospects of safeguarding the company are real and can be envisaged. In this respect, the use of the private judicial reorganisation procedure has to be strictly regulated to avoid jeopardising the rights of creditors. The role of the insolvency practitioner, and more fundamentally their diligence and probity, will be more important than ever.

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Martin specialises in corporate restructuring and insolvency, as an insolvency practitioner in the Cayman Islands and qualified accountant with over 27 years' experience. He is a director of the firm's liquidation and restructuring companies, R&H Restructuring (Cayman) Ltd. and R&H Restructuring (BVI) Ltd., both of which are affiliates of Rawlinson & Hunter in the Cayman Islands, of which Martin is a partner.

He has broad experience in leading complex administrations, liquidations and receiverships across a number of industry sectors. He has significant cross border experience having worked with corporates in the UK, US, Cayman Islands, British Virgin Islands, Bermuda, the Middle East, Ireland, British Channel Islands, the Far East and continental Europe.

Martin is a fellow member of both the ACCA and the ABRP (R3), a member of American Bankruptcy Institute and a member of RISA, the Cayman chapter of INSOL, acting as chair of the Legal & Regulatory committee. Martin also sits on the Insolvency Rules Committee in the Cayman Islands

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Overview of the restructuring landscape

The Cayman Islands benefit from a robust and mature restructuring and insolvency regime which has its roots in the English legal system but has developed specific processes and procedures for handling the unique attributes of Cayman Islands entities that get into financial distress. The restructuring market is supported by well-trained and experienced practitioners both in the legal and insolvency practitioner communities, and benefits from a stable, effective and efficient court system.

The main pieces of legislation governing insolvency procedures are as follows:

- Companies Act (2022 Revision);
- Companies Winding Up Rules 2018; and
- Insolvency Practitioners' Regulations 2018.

Official liquidation, the main procedure for handling insolvent estates, is a process that is commenced with the filing of a winding up petition in the Grand Court of the Cayman Islands, which subsequently oversees the liquidation process. Post-filing of a petition (or in parallel), an application for the appointment of a provisional liquidator can also be made in circumstances where there is a need to protect assets and/or the status quo, pending the court hearing of the petition.

"The restructuring market is supported by well-trained and experienced practitioners both in the legal and insolvency practitioner communities.

Provisional liquidations and a pivot to the new restructuring officer's regime

Over the past few years, there have been a number of winding up petition filings in the Cayman Islands combined with an application for the appointment of "light-touch" provisional liquidators for restructuring purposes. As a formal tool to restructure a company's affairs, this process is soon to become redundant with the introduction of the restructuring officer regime, discussed in further detail below.

HQP Corporation Limited ("HQP") has been one of the high profile cases to enter into provisional liquidation proceedings in recent times. HQP is a Cayman Islands holding company with subsidiary entities based out of Hong Kong and the PRC. HQP was set up as a financing vehicle for the purpose of raising capital for the operating entity of the group, a company developing a business to business auto parts trading platform in the PRC. This type of group structure is typical for the jurisdiction.

After a fraud committed by HQP's principal, shareholders of the company filed a petition with the Grand Court of the Cayman Islands for the company to be wound up and for provisional liquidators to be appointed. Although malfeasance had occurred, there was still a possibility that the trading entity of the group could be rescued and value preserved. The provisional liquidation allowed for a moratorium on claims against the company, to allow the liquidators to assess the economic viability of the group and to adjudicate on what grounds, and to what extent, the group might continue to trade prior to the Court considering the winding up petition. Historically there have been mixed results using this mechanism for restructuring purposes, with many companies ultimately entering into official liquidation. The restructuring officer regime is being introduced to provide a viable alternative for distressed entities to enter formal restructuring proceedings without the need for a winding up petition to be filed, and to potentially avoid official liquidation.

This has been one of the more interesting developments in the restructuring space in the Cayman Islands in recent times and would allow the directors of an entity to apply to the Grand Court for the appointment of a restructuring officer, typically without shareholder consent. This process formed part of the new Companies (Amendment) Bill 2021 and we await the commencement order which is expected in May 2022, at which point the restructuring officer route will be available to companies seeking to restructure.

The expected introduction of this new regime has been well received by professionals in the industry as Cayman Islands insolvency law is now aligning itself with other jurisdictions that offer a more debtor-friendly alternative. The restructuring officer process is more akin to administration proceedings and Chapter 11 proceedings in the UK and US respectively. While the Cayman Islands may still be viewed as more of a creditor centric jurisdiction, this new regime will present a more balanced approach, leaving debtor companies with better options when in distressed situations.

Recent trends in insolvency and restructuring

As a popular jurisdiction for private fund entities and their associated fund administration (both offshore feeder funds and master funds), the Cayman Islands has seen its fair share of high profile fund collapses in recent years. The liquidation of Penrich Global Macro Fund L.P. was brought under the supervision of the Grand Court in 2020 when it moved from voluntary into official liquidation. The principal of the former fund manager, based out of New Zealand, was criminally indicted and subsequently convicted for fraudulently manipulating the financial statements provided to investors and the liquidators are focused on recovering value for stakeholders via potential civil claims against certain parties. This course of action is typical for a fund against which a fraud has been perpetrated (in this case, alleged overvaluation of assets and fraudulent manipulation of fund financials).

With the cross-border nature of insolvency proceedings seen in the Cayman Islands, stakeholders often need to consider which venue or jurisdiction to file their claim or winding up proceeding, which can lead to confusion and may result in officeholders being appointed in different jurisdictions over the same company. We have seen an emerging trend in Hong Kong where the High Court has made winding up orders in relation to entities incorporated in the Cayman Islands, whose operations, for example, are in the PRC. The rationale for these orders is often that the centre of main interests of the company is in Hong Kong, whereas the law in the Cayman Islands is based on the seat of a company's incorporation. There have been concerns raised recently by the Grand Court around the need for comity and cooperation between the courts of different jurisdictions.

A considerable number of winding up applications in the provisional liquidation space have involved Cayman Islands' entities with operations in the PRC that are listed on the Hong Kong Stock Exchange. The Hong Kong court's recent resistance to recognising the appointment of Cayman Islands provisional liquidators over entities listed in Hong Kong has created difficulties for liquidators in fulfilling their duties in a meaningful way. This has occasionally resulted in parallel proceedings being conducted in two jurisdictions, often by different practitioners over the same entity.

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> The Cayman Islands has seen its fair share of high profile fund collapses in recent years.

When faced with a recent winding up petition, the Grand Court addressed the issue in an order and judgment on Silver Base Group Holdings Limited. The bondholders of the company filed a petition to have the company placed into liquidation in Hong Kong. Shortly thereafter, the company filed a petition in the Cayman Islands for the appointment of "light touch" provisional liquidators on the basis that there was a viable prospect of the company being restructured. The Grand Court presiding judge, Justice Doyle, adjourned the winding up hearing twice, reiterating that further work should be undertaken to update both the creditors of the company and the Hong Kong court on the steps being taken by the company. Justice Doyle subsequently granted the winding up order, however, in his judgment asserted that it was the responsibility of liquidators in the place of the incorporation of the company, not the centre of main interest, to deal with liquidation proceedings. He further stressed that the liquidators should consult with the company's creditors on the support for and viability of the restructuring proposal, as well as reporting to the court.

Similarly, in the winding up of GTI Holdings Limited, Justice Doyle again expressed concerns on comity and cooperation in connection with the Hong Kong court's treatment of a winding up petition filed in Hong Kong against the company.

This is a topic that continues to unfold, the outcome of which will no doubt have an impact on liquidations of this kind. The difficulties involved with comity is a focal point for liquidators practicing in the Cayman Islands, considering how entities have traditionally been structured in the jurisdiction where foreign recognition is usually one of the initial steps a liquidator must address upon appointment.

Another emerging topic is the ability to fund liquidations by engaging with local counsel on a conditional or contingency fee basis. The Private Funding of Legal Services Act 2020 came into force in 2021 and allows for contingency fee agreements, a mechanism previously unavailable for liquidators as a tool for financing the bringing of litigation claims. This will enhance the ability of liquidators to bring claims on behalf of an insolvent entity that would not ordinarily have the economic means to fund a claim using the resources at its disposal. This is a relatively recent legislative change and it remains to be seen how frequently it will be utilised.

> "When a liquidation occurs, it is often the case that cash at bank or other liquid assets have been largely depleted.

Asset realisation and recovery

As one of the leading centres for offshore company structures, investment funds and private wealth trusts, Cayman Islands entities often hold assets in jurisdictions across the world. As a result, in an insolvency context, asset realisation and claims enforcement processes are almost always conducted across multiple international borders.

When a liquidation occurs, it is often the case that cash at bank or other liquid assets have been largely depleted, as often owners/directors will have used this liquidity in an attempt to stave off insolvency or, in a fraud context, to enrich themselves. These liquidations will likely therefore be "cash poor" but potentially "claims rich."

There are many instances where companies act as an investment vehicle for investors to pool their money into a quasi-fund which purports to invest in property and other asset classes. Often these companies form part of a larger group structure with related entities located in other jurisdictions.

In the case of Platinum Partners Value Arbitrage Fund L.P., the complexity from an asset recovery perspective was the investigations being carried out by US authorities and the ensuing indictments and criminal trials of a number of the individuals who are currently the target of the liquidators' civil actions. In these situations, cooperation and dialogue with foreign enforcement authorities is key, notably in explaining the role and responsibilities of a Cayman Islands liquidator and the required oversight of the Grand Court. Recently we have seen a Cayman Islands fund, having previously been accused of fraud, negotiate a settlement with the SEC using the assistance of US counsel, resulting in a settlement of $84 million with their full asset portfolio being frozen. The Grand Court commented on the agreement stating that it presented "a significant and progressive step in the constructive cooperation and dealings of both jurisdictions with each other in the best interests of international creditor investment protection".

Upcoming developments

Global political and economic unrest has been well documented over the past 24 months. The onset of the Covid-19 pandemic has wreaked havoc on a number of industries worldwide with multiple governments introducing economic stimulus packages to prevent widespread bankruptcy and a subsequent global economic recession. Given the recent emergence from the global pandemic, governments have started to withdraw this fiscal stimulus. While we are yet to see any major economic fallout from the easing of these measures, it is likely that there will be a number of companies unable to survive without continued financial assistance.

At the same time, there were some of the largest increases to stock prices in the tech sector throughout 2021, which was a groundbreaking year for many start-up entities. This significant increase has since ground to a halt with the geopolitical disruption which has had an immediate impact on the global stock market and no indication that stock prices are set to rebound in the near future. Global oil prices are also now at an all-time high due to supply chain issues and we expect this to will have a significant impact on a number of industries.

These are unprecedented times both economically and politically, with a number of analysts commenting that there may be a global recession, considering how fragile many sectors were as they began to rebuild following the pandemic.

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> Global oil prices are also now at an all-time high due to supply chain issues and we expect this to will have a significant impact on a number of industries.

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Introduction

The art of achieving sustainable turnaround in uncertain times

There are many reasons why companies struggle with strategic, operational and financial challenges. Although none of these have had such an enormous impact as the global COVID-19 pandemic, external and internal factors have always forced companies to continually improve performance to remain competitive and preserve value. In case performance deteriorates substantially, a rigorous approach to turnaround, or even restructuring, is required.

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> Smooth-running turnaround projects are a decisive success factor for over three-quarters (77%) of respondents.

Examples of external challenges include:

- Increasing world volatility, uncertainty, complexity and ambiguity – “VUCA” – often driven by technological advancement
- Profound changes in customer demand and customer behavior, for example through greater emphasis on sustainability
- Political uncertainty and changes in geopolitical power structures
- Macro shocks such as the global COVID-19 pandemic

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Internal factors can also threaten performance and require business model adjustments, for example:

- Growing complexity through diverse business models within major companies
- A lack of transformation and performance mindset in the company culture and leadership
- The need to act quickly in spite of rigid structures and processes
- Failure to align different and partially overlapping performance improvement projects and initiatives within the company
- A lack of central coordination and transparency from top management
- Insufficient availability of key personnel

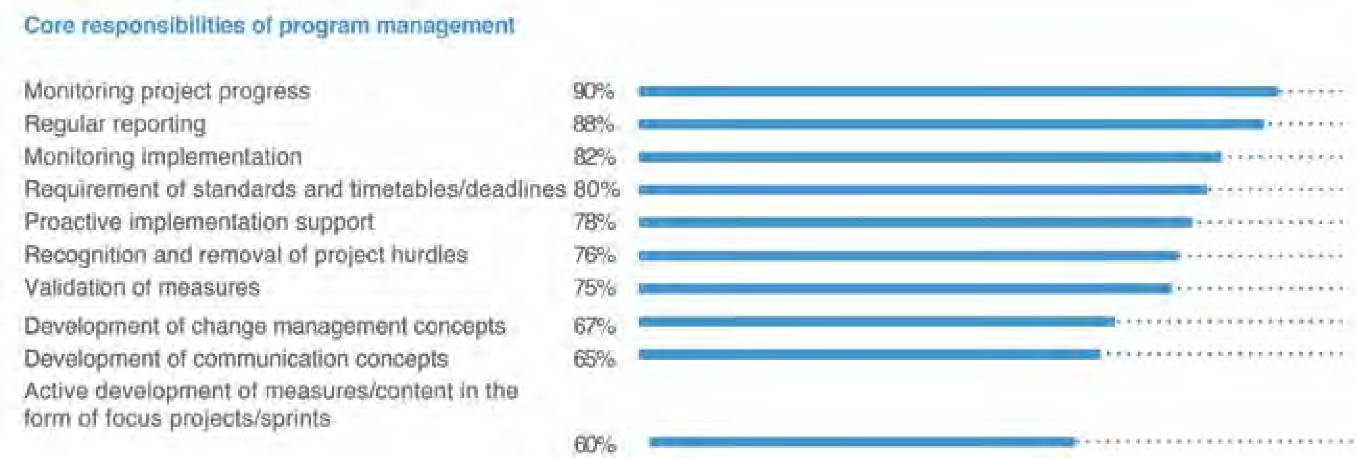
Survey results

Turnaround project management – transforming improvements into reality

We surveyed top managers from a wide range of company sizes and industries about their experiences and expectations in turnaround management.

Smooth-running turnaround projects are a decisive success factor for over three-quarters (77%) of respondents. With core responsibility for turnaround project management firmly lying with administration and reporting functions (90% and 88%, respectively).

Despite that reliance, the survey findings suggest that only a small proportion of companies are leveraging the full potential of effective turnaround project management, since only roughly half of respondents indicated that desired targets were achieved. While hygiene factors are viewed as very important, success-related functions such as the development of change management or communication concepts, and active development of performance improvement measures appear to carry less weight for the survey respondents.

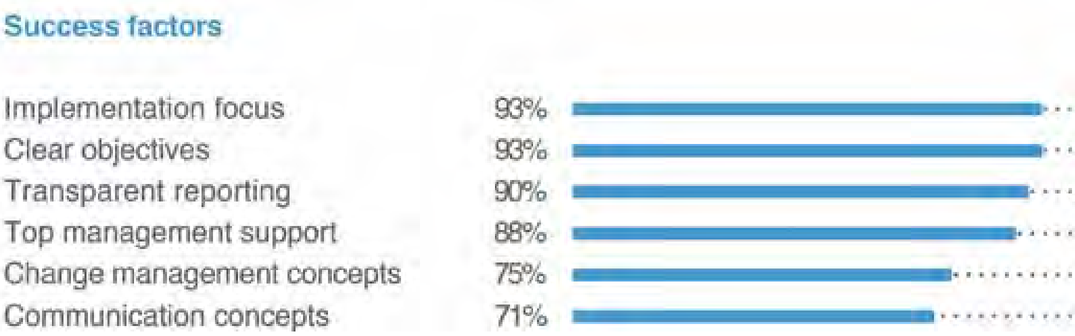


Only 47% of the top managers surveyed achieved the targets.

Only half confirmed measurable added value.

This unused potential indicated by the survey results could be a reason for the increased dissatisfaction with a view to turnaround project management, with only 47% of the top managers indicating that they actually achieved targets and expectations. Furthermore, only half (49%) confirmed that the measures ultimately gave rise to measurable added value.

Why is this percentage so low? It does not reflect a lack of knowledge of the critical success factors as they are clearly specified by the survey respondents:



What is clear is that the factors classified as critical for success differ considerably from the functions viewed as core responsibilities.

While reporting is viewed as significant, the respondents consider the implementation focus even more important, with around three-quarters of the respondents seeing sophisticated change and communication concepts as important for the success of turnaround project management. At the same time, two-thirds of the survey respondents would like to see change initiatives more firmly integrated into project management.

In summary, the survey shows that that decision-makers regard good turnaround project management as a key driver of success even though the high expectations have rarely been met in practice.

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> The professionals in the RTOs are not just advisors but support with relevant industry know-how.

For companies to achieve the desired degree of measurable success in the future, they will undoubtedly have to place a stronger emphasis on the implementation of measures and support for these efforts with suitable change and communication concepts. In our opinion, these are the pillars on which the success of turnaround project management rests – central success factors that also form the foundation of our reshaping results restructuring and turnaround offices.

The reshaping results restructuring and turnaround office (RTO)

Committed to achieving sustainable turnaround

To improve their financial and strategic performance, companies sometimes initiate uncoordinated performance improvement initiatives. Company-wide planning, coordination and implementation as well as a systematic follow-up review are critical to success. Our restructuring and turnaround offices (RTOs) specialise in this.

Wherever initiatives are needed to adjust business models, improve results or increase liquidity, RTOs draw on the experience and know-how gained from numerous successfully implemented turnaround projects.

As the main control centre, the RTO reports to management or the steering committee and acts as the extended arm of top management.

Fortified by this clear mandate, the RTO can coordinate the turnaround process centrally in collaboration with teams from the business and implement it with the necessary emphasis. In doing so, the RTO leadership takes responsibility for the management and coordination of the overall project, while special turnaround teams handle performance projects in the various divisions or project subclusters.

Key to the success of RTOs is their focus on the implementation of the planned measures as well as their holistic approach that considers all aspects relevant to the turnaround process. This enables separate teams to focus on overarching cross-disciplinary issues or personnel implementation.

As good communication are key to successful change, the change management office oversees communications for the turnaround project.

The change management office is responsible for mobilising the staff and the leadership team, strengthening their willingness to accept changes and mitigate any resistance.

From idea to realisation

Finally, an advisor who acts as an entrepreneurial partner

The key to every restructuring and turnaround project is the management of measures, which help to assess and realise the potential for earnings and liquidity improvements.

The professionals in the RTOs are not just advisors but support with relevant industry know-how, functional expertise and implementation orientation.

The targeting

As part of the targeting, we define the total earning and liquidity improvement requirements. The targets are fixed and invariable. They are derived from internal and external benchmarks incorporating stakeholder expectations.

We then divide the improvement requirements among the individual divisions or subproject clusters. For this, we use a variety of methodologies, depending on the situation.

The maturity degrees

The measure management uses a maturity degree logic, with which we can present transparent and detailed progress – and later implementation – for all improvement measures.

The maturity degrees are represented in detail to clearly reflect the measures and implementation progression. Controlling and HR department resources are systematically incorporated in the maturity degree tracking to bundle all necessary perspectives in the measures assessment process.
The management board and the RTO also benefit from the maturity degrees as a central program management element. Tracking these specifications right from the outset of the project provides information on progress with the measures, potential delays and need for action.
We also continuously forecast the maturity degree development in order to present the company with a clear idea of the project's robustness and target attainment.

Integration in the income statement

Measurable values are created during the implementation phase, that are already initiated in the detailing phase.
In RTOs, particular importance is attached to accurately embedding each measure in the income statement; through cost types and cost centres or through appropriate KPIs. Only then can the actual effect of the measures be tracked and presented in the income statement to enable them to be measured and managed effectively.

Prioritising measures

All measures are prioritised and categorised prior to implementation, so that immediate measures and short-term wins can be filtered out quickly to achieve initial savings effects.

Tools and reporting

Comprehensive performance programs in large companies are highly complex. To effectively control them at all times, software-based measures management systems are installed at the beginning of the project.

The software solution has a high level of automation to keep most resources assigned for the actual work.

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> Many executives mistakenly believe that their employees will perceive the planned changes just as they do.

With these sophisticated tools, we guide stakeholders through the measure management process– starting with a step - by - step walk-through of measure detailing, including automated plausibility checks through to the creation of interactive dashboards in real time for the highest level of implementation transparency.

Change management

How sustainable change is achieved

To make a company future-ready, changes must be made. Human nature means that people are generally hesitant and sceptical about changes, all the more when they fear personal or financial disadvantages or when the significance of the change is not clear.

Therefore, engagement via an intensive dialogue with all stakeholders is crucial – whether it is the workforce, middle management or the employer-side – to actively include all persons involved in the process, and thereby change mindsets.

Many executives mistakenly believe that their employees will perceive the planned changes just as they do. However, the reality is usually different: while the reasons and the context for financial decisions are presented logically at the executive level and are based on data, the workforce usually does not have the same insight into or understanding of the background and exact objectives.

We therefore recommend reviewing management decisions, and thus the planned change measures, in terms of their communication impact. Based on our experience, asking "How does it come across?" is at least as important as asking "Which structural changes lead to which savings potentials?" It is therefore important to clearly explain to all persons concerned what the management intends to achieve with the planned changes in order to:

- Win the support of stakeholders; or
- Reduce the resistance of potential opponents.

Shaping change interactively

Change management workshops are an excellent tool to promote the changes on a wide platform. They can be used to define success stories and objectives for change management. Further, it is important to establish an overarching purpose and vision in the workforce, in which the medium - and long-term values of the company are reflected in a strong, authentic and honest story.

Communicating change authentically

For any kind of transformation, it is not just about sharing facts and figures but also about the emotional responses by affected people. The connections required by the change process must be created and the consequences must be considered. It is about the right tone at the right time.

Creating change competence

Existing opposition by stakeholders must be identified, taken seriously and managed. Executives are ambassadors of change; they must therefore be enabled to implement change. Executives need to understand which dialogues on change they should conduct with their teams and colleagues.

Our survey respondents confirmed and prioritised the importance of these change management aspects for turnaround plans:

Conclusion

Central, content-oriented steering is a driver for turnaround

While in-house project management frequently does not yield the desired results, RTOs can ensure that centrally coordinated measures follow a holistic approach.

With professional planning, management, implementation and performance monitoring from a single source, measures can be precisely aligned to objectives, systematically tapping into the business's potential. Its aim is to lead the organisation back to sustainable success together.
When the room to manoeuvre becomes smaller and pressure increases, steady and swift decisive action is called for. RTOs provide decision-makers with the required support to make independent decisions in the context of a turnaround or restructuring improvement framework.
By anchoring the performance paradigm in the company methods and culture, management will create an opportunity to set itself apart from the competition in the medium term and use their new strengths in the long term.

Companies act wisely by implementing turnaround project management proactively and not when the crisis is already there. The best projects are implemented in the company with foresight in a proactive fashion.

In conclusion, there are four key factors that mark a successful RTO:

1. A robust mandate for turnaround project management — clear objectives and top management support
2. Deep functional know-how and flexible handling of changed conditions without deviating from the overall financial objective
3. Objectivity as an essential basis for steering and "leading by numbers" — consistent, accurate and promptly generated by powerful tools
4. Proactive stakeholder management and comprehensive communications, both internally and externally

The views reflected in this article are the views of the author and do not necessarily reflect the views of the global EY organisation or its member firms.

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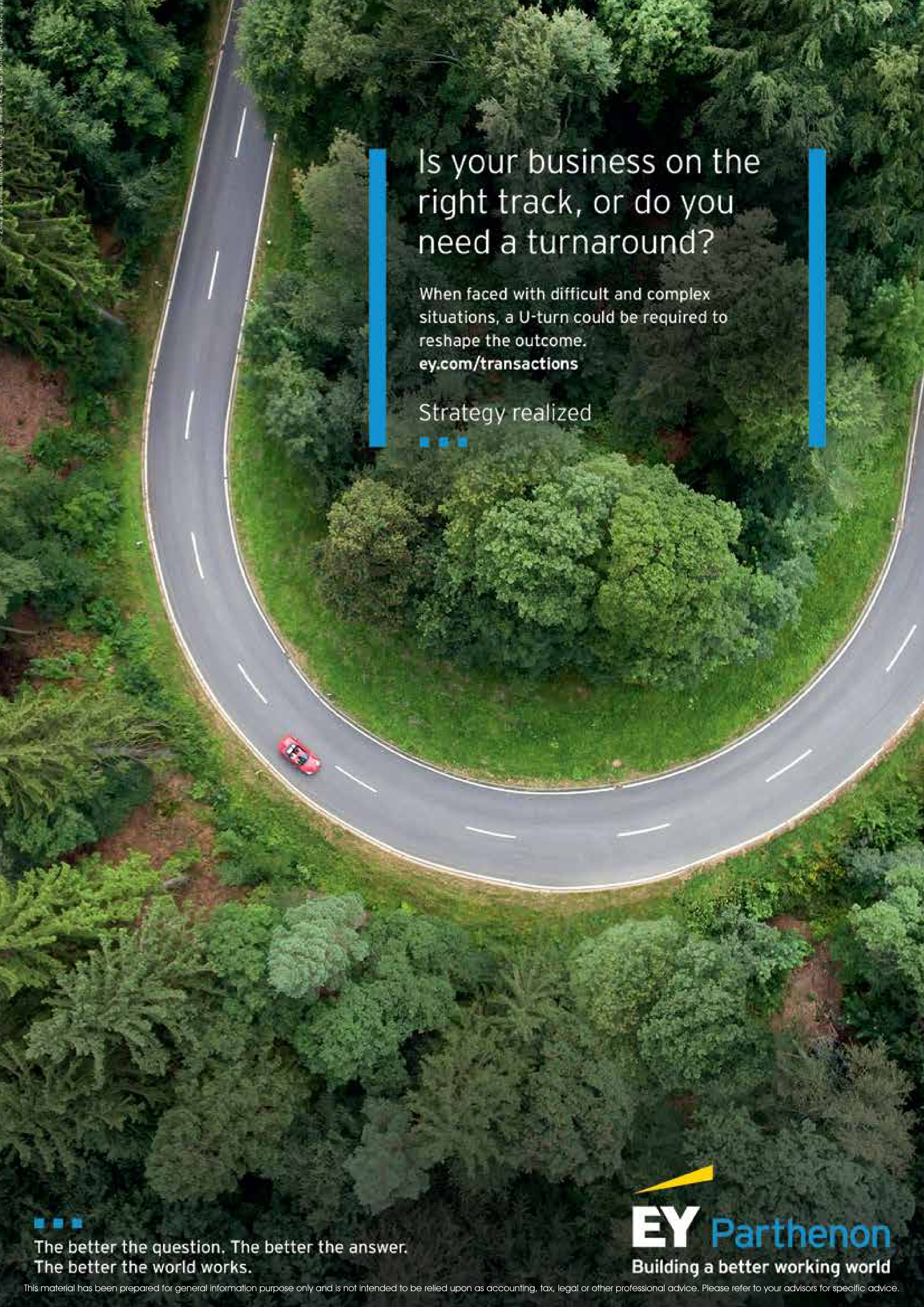
> RTOs provide decision - makers with the required support to make independent decisions in the context of a turnaround or restructuring improvement framework.



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Germany: When in Germany do as the English do?

Andreas Dimmling[1] and Sandra Krepler

Introduction

2021 had started with the most profound innovation for German restructuring law for over two decades. One year later this innovation has not kept its promises but the German restructuring market had not been as uneasy as it had been 2021.

After many German restructuring experts and insolvency practitioners had long campaigned for the introduction of a formal out-ofcourt restructuring, the implementation of the EU Restructuring Directive (Directive (EU) 2019/1023 of 20 June 2019) into German law (so-called SanInsFoG) as of 1 January 2021 finally brought change.[2]

> "Many of the state's measures to avoid a wave of insolvencies due to the COVID pandemic expired in 2021.

The German law now provides for the first time ever for an out-of-court restructuring regime that allows cram down of dissenting creditors.

The German legislator reckoned it necessary to bring in the new restructuring regime as of January 2021 because many of the state's measures to avoid a wave of insolvencies due to the COVID pandemic expired in 2021. However, we still do not see any increase in corporate insolvencies in Germany. And this is not because of the new restructuring law.

So, let's have a closer look at the German insolvency and restructuring market:

I. Is German Economy STILL in crisis?

After GDP fell by 5 per cent in 2020 compared to 2019, marking the first time since the financial crisis in 2008/2009 that the domestic economy has fallen into recession, the German economy recovered well and reached a substantial growth of 2.7 per cent in 2021 compared to the previous year.[3] The labour market also recovered somewhat and the unemployment rate even fell to 5.4 percent.[4]

Consequently, the expected increase in corporate insolvencies did not materialise. From January to October 2021, a decrease of 14 % compared to the previous year was recorded.

Many companies still profit from numerous aid and support measures for the economy in 2020 by German government.

However, the rapidly rising inflation rate has been a cause for concern in recent months. In February 2022, it was 5.1% for Germany compared to the previous year. Raw materials and energy in particular have become 20% or more expensive.

II. Development in Insolvency law

1. One year after the introduction of the new restrukturing act -an interim assessment

German insolvency law lacked a proper and formal out-ofcourt restructuring tool. Cramdown proceedings in out-ofcourt restructurings were not possible under existing law.

On 20 June 2019, the European Parliament and the European Council passed the Directive (EU) 2019/1023[5], which, inter alia, contains the introduction of preventive restructuring measures to avoid insolvencies at an early stage in the process. This forced the German legislator introducing a proper out-of-court restructuring tool. Are there already prominent use cases for the

1 Andreas Dimmling and Sandra Krepler are lawyers in the Munich office of GSK Stockmann; Andreas co-heads the insolvency and restructuring group of GSK Stockmann.

2 See https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32019L1023.

3 See https://www.destatis.de/EN/Press/2022/01/PE22_020_811.html

4 See https://www.arbeitsagentur.de/en/press/en-2022-06-labour-market-in-january-2022

5 The full directive can be accessed via https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019L1023&from=de

Since January 1, 2021 the Directive has been transferred into German Law. The core of the SanInsFoG is the Act on the Stabilisation and Restructuring Framework for Companies (StaRUG). Yes, I agree, the German legislator has never been good in giving its most innovative laws a comprehensive and catchy title.

What is the basic principle?

The basic principle of the StaRUG is that a company offers a restructuring plan to creditors during a status where insolvency has not occurred yet. The company can choose if all creditors shall take part in the plan or only certain groups of creditors. The plan is drawn up by the company and presented to all involved creditors. The creditors shall then vote on the plan divided into different groups. If a sufficient majority of 75% of the debts to be restructured vote in favour of the plan, even dissenting creditors or dissenting groups shall have no power to prevent the plan from becoming effective (crossclass cram down effect).

During the phase of the restructuring plan being drawn up and voted on, the company can seek certain standstill measurements through court order. As a consequence, creditors cannot take legal action against the company during this time for immediate enforcement of debts.

The restructuring plan will in most cases be drawn up under the supervision of a restructuring expert who shall be appointed by the court if the debtor or a minority of at least 25% of creditors ask for. The restructuring expert can be a lawyer experienced in restructuring cases. He may have also monitoring and moderating tasks between the company and creditors.

StaRUG is somewhat similar to the Scheme-of-Arrangements or (since June 2020) Restructuring Plans in England. But is different in two points. First, although the new German restructuring plan requires professional assistance, costs involved should be still considerably lower than reaching out for a Scheme of Arrangement in London. Second, Schemes of Arrangement are not recognised in Germany as insolvency procedures and therefore the stipulations of a Scheme of Arrangement are not easily enforced in Germany. So, Germany had to do it "the German way".

INTERIM BALANCE AFTER ONE YEAR OF StaRUG - Has the restructuring tool starug already been widely adopted?

StaRUG procedures are not published in registers open to the public. Therefore, we lack information on how many StaRUG procedures have taken place since beginning of 2021. However, according to well informed sources it seems likely that not more than 10-15 cases had been completed successfully. In 4 cases, there was a court-confirmed restructuring plan.[6]

Does the StaRUG meet the expectations of the practice?

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> The restructuring plan will in most cases be drawn up under the supervision of a restructuring expert.

The small number of StaRUG cases leads to the interim conclusion that the regime falls short of its high expectations. Some therefore refer to the StaRUG as a "toothless tiger".[7] The reasons for this are still not clear. One important point is that under a StaRUG procedure the debtor cannot adjust the contractual terms of current contracts (such as lease agreements) against the will of the contracting party.

Additionally, some creditors and insolvency courts are quite reluctant to test the new regime and tend to prefer traditional insolvency procedures.

Those cases where the StaRUG procedure went well were characterized by a complex debt structure that prevented the operational restructuring.

6 See https://rsw.beck.de/aktuell/daily/meldung/detail/studie-wenige-firmen-nutzen-bislang-neues-sanierungsverfahren.

7 See https://www.lto.de/recht/kanzleien-unternehmen/k/starug-unternehmensstabilisierung-restrukturierung-gesetz-insolvenz-zwischenbilanz-eu-2019-1023-saninsfog/.

Are there already prominent use cases for the application of the StaRUG?

The best-known case connected with the StaRUG procedure is the clothing company Eterna Mode Holding GmbH, based in Passau. On September 10, 2021, its creditors approved a restructuring plan to implement a reorganisation under the StaRUG. This provided for a debt cut to bondholders and payment of a settlement rate of 12.5% on their claims and outstanding interest. The necessary financial resources were provided by the existing shareholders of Eterna. The responsible restructuring court confirmed the restructuring plan in October 2021.

2 Extension of deadlines for imminent insolvency and overindebted-ness test

> The 2021 Insolvency Act reform also introduced new regulations on the legal obligation to file for insolvency.

The 2021 Insolvency Act reform also introduced new regulations on the legal obligation to file for insolvency.

Whereas under the former law, the deadline for filing for insolvency had to be no later than three weeks after the reason for opening insolvency proceedings occurred, the new version doubles this deadline to six weeks in the event of over-indebtedness. Thus, the debtor has more time trying to restructure avoiding insolvency. In case of illiquidity, the maximum deadline remains at three weeks after illiquidity occurred.

III. What are the most interesting insolvency cases in Germany at the moment?

Even though the number of corporate insolvencies in 2021 was lower than forecast, there were important insolvency proceedings. Two are of particular interest to the international readership.

1. Eyemaxx real estate AG – can we already speak of insolvency tourism to Austria?

Eyemaxx Real Estate AG is a real estate project developer registered in Germany. Unlike many other similar companies, Eyemaxx had issued numerous bonds over the years for financing expansion and real estate projects.

When Eyemaxx suddenly filed for insolvency in November 2021, many investors and real estate observers were surprised. On the one hand, the question suddenly arose whether the real estate industry is not as crisis-proof as thought? On the other hand, experts were surprised that Eyemaxx filed for in insolvency in Austria and not in Germany. The Austrian insolvency court that already was responsible for the Air Niki case in 2017, quickly accepted the filing and appointed the same insolvency administrator as it had appointed in 2017 for the Air-Berlin subsidiary. The argument as to why the Austrian court considered itself competent is also the same as in the Air-Niki case in 2017: although the debtor is registered in the commercial register in Germany, the COMI is located in Austria. It is sufficient that the main decisions are taken and the management is based in Austria.

This move provoked turmoil among bond holders of Eyemaxx because the insolvency regime is less favourable for bond holders in Austria than in Germany. The Eyemaxx manoeuvre was described as a new insolvency tourism from Germany to Austria.

However, following several creditor filings for insolvency of Eyemaxx in Germany, the German insolvency court of Aschaffenburg opened secondary insolvency proceedings in Germany. This step is also similar to the Air Niki case in 2017. The secondary proceedings limit the main insolvency proceedings, by removing the domestic assets from the seizure effect of the main proceedings. Accordingly, the assets of Eyemaxx located in Germany – that seem to form the majority of assets - will be realised in Germany and bondholders can protect their position in the German proceedings now.

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2. Wirecard AG – it just becomes more and more obscure

The inglorious winner of Germany's biggest insolvency scandal is still Wirecard AG. Wirecard was valued more than 21 billion euros at the end of 2018 and now lost all its glamour and value. Wirecard's bookkeeping was manipulated by its management, approximately 1.9 billion euros failed to exist, Wirecard's former managing directors are held on remand by German prosecutors or are on the run.

Meanwhile, Wirecard's insolvency administrator sued the former members of the Management Board and two former members of the Supervisory Board for a total of 140 million euros in damages for possible breach of duty in granting loans worth millions. The aim of the lawsuit is to obtain the directors' and officers' liability (D&O) insurance of the board members. In addition, there have also been increasing indications recently that Wirecard's auditors of the past could also be liable. Investors had initially failed with lawsuits against the auditors. But a court information in the next higher instance could be the prelude to an unprecedented settlement between investors, the insolvency administrator and the Big 4 auditing firm.

IV. German restructuring Market – Quo Vadis?

German restructuring experts continue to expect that the number of substantial restructuring and insolvency cases should rise strongly soon. If the COVID pandemic and the new StaRUG procedure could not trigger this wave, current crises seem to have the potential to get many German companies into trouble. Even before the Russian attack on Ukraine, inflation was climbing inexorably, making production and refinancing increasingly expensive for companies. The war in Ukraine, the sanctions against Russia and the looming shock to the global economy could now be the prelude to sharply rising restructuring cases. In this situation, the StaRUG procedure could still develop into a powerful instrument because it can so quickly and silently overcome the company's financial crisis. These advantages could fit well with the current demand for quick help in a crisis without much publicity.

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> German restructuring experts continue to expect that the number of substantial restructuring and insolvency cases should rise strongly soon.

Restructuring & Insolvency

Time pressures, uncertainty and loss of trust define entrepreneurial crises – the fear of personal liability or loss of funds often goes hand in hand with this. We will assist you, for example, in avoiding liability risks as managing director or shareholder, or in securing and enforcing your claims in a crisis with a customer.

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- Providing representation in court to assert or provide defence for crisis-related claims such as executive liability or contesting insolvency
- Advising liquidators on complex legal aspects of insolvency proceedings, e.g. corporate law, state aid law and bank law
- Liquidation and alternative methods for winding down companies
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"The restructuring team at GSK impressed us with their precise analyses and the dynamism of their content. What particularly impressed me, however, was their respectful approach that paved the way for constructive solutions without having to surrender one's own position. If I ever have to assert complex claims again, I shall definitely rely on the expertise of GSK."

Frank Gebert, former CEO of Alno AG

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HONG KONG

Key developments and the latest trends in Hong Kong – from a legal perspective

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Justin's practice covers complex commercial litigation (in jurisdictions such as Hong Kong, Singapore, PRC and the UK), cross-border regulatory and internal investigations, and international commercial arbitration, with a particular focus on China-related disputes and investigations.
He has particular expertise in advising on shareholder and joint venture disputes, insolvency proceedings, disputes with activist or minority shareholders, professional negligence and asset tracing and recovery actions.

His experience included advising a Chinese state-owned bank on all aspects of the domestic and international recovery and enforcement of a nearly USD 2.3 billion overdue debt owed to it and on the recovery from the affiliate of the borrower who jeopardised such debt (including debt declaration and participation in the winding-up procedures).

Justin is also ranked by Chambers & Partners in 2020 as a rising star in Dispute Resolution (International Firms).

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1. Background

The Hong Kong Special Administrative Region ("**Hong Kong**") has long been an international financial centre and investment gateway for Mainland China. In the past decade, we have seen a significant increase in the number of Mainland enterprises[1] listed on the Hong Kong Stock Exchange and their growing share of the total market capitalisation. As at 31 December 2021, there were a total of 1,368 Mainland enterprises listed, representing 53% of the total number of listed companies in Hong Kong, and 79% of the total market capitalisation of the Hong Kong equity market.[2]

> "Many insolvency cases in Hong Kong concern the restructuring or liquidation of offshore-incorporated, Hong Kong-listed Mainland enterprises.

Common features of these Mainland enterprises are:

- first, they are often incorporated in an offshore jurisdiction, and the popular choices are the Cayman Islands, the British Virgin Islands and Bermuda;
- secondly, their business operations strongly gravitate towards Mainland China. Their operations and assets are based in the PRC, held by onshore or offshore incorporated intermediaries, and ultimately controlled by Mainland individuals or organisations; and
- thirdly, they have little connection with Hong Kong, and often the only connection with Hong Kong is their listing status at the Hong Kong Stock Exchange.

For this reason, many insolvency cases in Hong Kong concern the restructuring or liquidation of offshore-incorporated, Hong Kong-listed Mainland enterprises. However, there are currently no statutory provisions in relation to cross-border insolvency and restructuring in Hong Kong. Hong Kong has yet to adopt the UNCITRAL Model Law on Cross-Border Insolvency, which would have provided a foreign insolvency practitioner with means to obtain recognition of the foreign insolvency proceeding and seek judicial assistance from the Hong Kong court in aid of such proceeding.

Due to this gap in the insolvency regime, the Hong Kong courts have developed and applied various common law principles to address the corporate failures of Hong Kong-listed, offshore-incorporated entities with assets predominately in Mainland China. Much of the case law in this area has been developed by the Honourable Mr Justice Harris ("**Harris J**"), who was the Companies Judge of the High Court of Hong Kong.[3]

2. Winding-up of foreign incorporated companies in Hong Kong

It is now well-established under Hong Kong case law[4] that a foreign incorporated company can be wound up in Hong Kong if three core requirements are satisfied:

- First core requirement: The company has a sufficient connection with Hong Kong;
- Second core requirement: There is a real possibility that a winding-up order would benefit the petitioner; and
- Third core requirement: The court is able to exercise jurisdiction over one or more persons in the distribution of the company's assets.

The first and third core requirements are usually satisfied if a company is listed in Hong Kong. Previously, the Hong Kong court found[5] that the second core requirement was also satisfied by the company being listed in Hong Kong. However, more recently, in *Re China Huiyuan Juice Group Ltd*,[6] a case that concerns an application to wind-up a Cayman incorporated, Hong Kong listed company where all of the company's operating assets were in the Mainland, Harris J concluded that a Hong Kong winding-up order would not benefit the petitioner for three reasons:

- First, the company has no assets in Hong Kong.
- Secondly, Harris J observed that the value of listings in Hong Kong had dropped significantly and the petitioner did not produce evidence showing that there was real prospect that the value of the company's listing status could be realized by liquidators for any meaningful amount.
- Thirdly, Hong Kong liquidators would not be able to take control of the company's operating subsidiaries

[1] Comprising H-share companies (enterprises that are incorporated in the Mainland and either controlled by Mainland Government entities or individuals), red chip companies (enterprises that are incorporated outside of the Mainland and are controlled by Mainland government entities) and Non-H share Mainland private enterprises (companies that are incorporated outside of the Mainland and are controlled by Mainland individuals).
[2] According to the annual market statistics published by the Hong Kong Stock Exchange.
[3] Harris J has recently taken up a new role as the president of the Competition Tribunal in Hong Kong.

[4] In the landmark decision of the Court of Final Appeal in *Kam Leung Sui Kwan v Kam Kwan Lai & Ors* FACV 4/2015 (on appeal from CACV 266/2012, HCCW 154/2010).
[5] In the case of *Shandong Chenming Paper Holdings Limited v Arjowiggins HKK2 Limited* [2018] HKCFI 93 and [2020] HKCA 670.
[6] [2020] HKCFI 2940.

in the Mainland which were held via intermediate holding companies incorporated in the BVI. Hong Kong liquidators of a Cayman incorporated company would not be able to change control of the BVI subsidiaries. Therefore, if the benefit that was sought by winding up the Company was to recover assets in the Mainland, it was not a benefit that could be obtained through a winding up of the company in Hong Kong.

Harris J reinforced this approach in *Re Grand Peace Group Holdings Limited*[7] which concerns an application to wind-up a Bermuda-incorporated, Hong Kong listed company. He said that it was "*futile*" for the Hong Kong court to appoint liquidators over a Bermuda-incorporated company in order to take control of its BVI subsidiaries with the aim of taking control of their Mainland subsidiaries, as the BVI courts would not recognise the liquidators. In the circumstances, the second core requirement was not satisfied because the petitioner was unable to "*point to a discernible and real benefits to creditors*". The correct approach would be to seek a winding up order of the holding company in its place of incorporation.

It appears that the clear preference of the Hong Kong courts is for petitioners to commence winding up proceedings in the debtor's place of incorporation. To succeed in an application to wind up a foreign incorporated company in Hong Kong, the petitioner must satisfy the second core requirement by demonstrating with evidence that the winding-up sought will provide a real, not hypothetical, prospect of a material financial benefit.

3. Lack of statutory corporate rescue procedures in Hong Kong

Another well-noted gap in the Hong Kong insolvency regime is the lack of a formal corporate rescue procedure to allow a company in financial distress certain protection from creditor claims in the form of a moratorium or stay of proceedings.[8] For offshore incorporated Hong Kong listed companies in financial distress, one possibility would be to commence "*soft-touch*" provisional liquidation in its offshore jurisdiction of incorporation. This would allow a company to remain under the control of directors and at the same time creditors would be protected by the provisional liquidation process, allowing the company some time to attempt to restructure its debts.

Soft-touch provisional liquidators appointed offshore may also seek recognition and assistance in Hong Kong, including a stay of any existing local winding-up proceedings.[9] The standard form recognition order previously included the following:

"For as long as the Company remains in provisional liquidation in [the relevant jurisdiction], no action or proceedings shall be proceeded with or commenced against the Company or its assets or affairs, or their property within the jurisdiction of this Honourable Court, except with the leave of this Honourable Court and subject to such terms as this Honourable Court may impose."

The effect of such stay would in essence be to block Hong Kong winding-up proceedings and allow the soft-touch provisional liquidation in the offshore jurisdiction to proceed.

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> Another well-noted gap in the Hong Kong insolvency regime is the lack of a formal corporate rescue procedure.

In *Re FDG Electric Vehicles Ltd*,[10] the Hong Kong court clarified that soft-touch provisional liquidation is not necessarily for all purposes a "*collective insolvency process*" given its restructuring objective and therefore no blanket stay of proceedings in Hong Kong is to be given automatically. Instead, the provisional liquidators seeking a stay order should apply to the court for directions, and the court will consider the propriety of any stay on a case-by-case basis.

7. [2021] HKCFI 2361.
8. Moratorium or stay of proceedings are often available under the insolvency laws of other jurisdictions, such as the Singapore Insolvency, Restructuring and Dissolution Act and the UK Corporate and Insolvency and Governance Act 2020.
9. See for example *Re Z-Obee Holdings Ltd* [2018] 1 HKLRD 165, *The Joint Provisional Liquidators of Moody Technology Holdings Ltd* [2020] HKCFI 416, *The Joint and Several Provisional Liquidators of China Oil Gangran Energy Group Holdings Limited* [2020] HKCFI 825.
10. [2020] HKCFI 2931.

In *Re Lamtex Holdings Limited*,[11] the court went further and ordered the winding-up of a Bermudian-incorporated Hong Kong-listed company that had been placed into "*soft-touch*" provisional liquidation in Bermuda. The court focused on the centre of main interest ("**COMI**") of the company, which was clearly Hong Kong and the Mainland, with most of its creditors in the Mainland being in favour of a winding up order. At the same time, the restructuring plan submitted by the provisional liquidators was "*scanty in the extreme*".[12] The court took the view that the provisional liquidators were appointed merely in an attempt to engineer a de facto moratorium and block previously filed winding-up proceedings in Hong Kong. In granting the winding-up order in *Re Lamtex*, Harris J commented:

A "*soft-touch*" provisional liquidation commenced to avoid immediate liquidation with no apparent consideration given to the interests of creditors will not be assisted by the Hong Kong court.

"I anticipate that unless the agreement of a petitioner and supporting creditors have been obtained in advance the court will not deal with recognition and assistance applications made by soft-touch provisional liquidators after a winding up petition has been presented in Hong Kong on the papers."

The Hong Kong court will continue to scrutinise the use of soft touch provisional liquidation, as reaffirmed in *China Bozza Development Holdings Limited*,[13] by Harris J, who expressed concern that the recognition and assistance granted to soft touch provisional liquidation was "*being abused to obtain a de facto moratorium of enforcement action by creditors in Hong Kong*". Harris J reminded practitioners that when it appears likely that a company is insolvent, the company's directors' paramount duty is to consider the interests of the company's creditors. A "*soft-touch*" provisional liquidation commenced to avoid immediate liquidation with no apparent consideration given to the interests of creditors will not be assisted by the Hong Kong court.

These decisions demonstrated the Hong Kong court's approach to the recognition of soft-touch provisional liquidators appointed in the company's jurisdiction of incorporation. While the Hong Kong court recognised that the rationale underlying the common law power of assistance is modified universalism, which had traditionally given primacy to the company's place of incorporation, where there are competing foreign and local insolvency proceedings, it is unlikely to tolerate the use of "*soft-touch*" liquidation to frustrate the proper exercise of a creditor's right to wind-up a company unable to pay its debts.

4. Recognition of insolvency proceedings between Hong Kong and the Mainland

14 May 2021 marked a milestone for mutual recognition of and assistance to cross-border insolvency proceedings between Hong Kong and Mainland, as the Supreme's People's Court and the Government of Hong Kong signed the Record of Meeting on Mutual Recognition of and Assistance to Bankruptcy (Insolvency) Proceedings between the Courts of the Mainland and Hong Kong.

From the perspective of Hong Kong insolvency practitioners, the key features of the framework are:

- Shanghai, Xiamen and Shenzhen are designated as pilot areas and relevant Intermediate Courts in the pilot areas are the designated Mainland courts for the recognition of and assistance to Hong Kong insolvency proceedings.
- A liquidator or provisional liquidator in Hong Kong insolvency proceedings may apply to a designated Mainland court for recognition and assistance. "Hong Kong insolvency proceedings" refer to collective insolvency proceedings commenced in accordance with the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32) and the Companies Ordinance (Cap 622), and include compulsory winding up, creditor's voluntary winding-up and scheme of arrangement sanctioned by a court in Hong Kong.

11. [2021] HKCFI 622.
12. In contrast, in *Re Ping An Securities Group (Holdings) Limited* [2021] HKCFI 651 where the company and the provisional liquidators presented a credible restructuring plan, the Hong Kong court allowed a two month adjournment to the Hong Kong winding-up proceedings.
13. [2021] HKCFI 1235.

• For recognition and assistance to be granted in the Mainland, the COMI of the debtor must have been Hong Kong for at least six months. COMI generally means the place of incorporation of the debtor, but other factors such as the place of its principal office, its principal place of business, the place of its principal assets etc. may also be taken into account. In addition, the debtor's principal assets in the Mainland must be in a pilot area, or it must have a place of business or a representative office in a pilot area.

Shortly thereafter,[14] Harris J applied the framework and issued a letter of request to the Bankruptcy Court of the Shenzhen Intermediate People's Court, seeking its assistance in aid of the liquidation and the liquidators of Samson Paper Company Limited ("**Samson Paper**"), a Hong Kong incorporated company that was part of the corporate group headed by Samson Paper Holdings Limited, a Bermuda incorporated Hong Kong listed company.

Further, Harris J explained[15] that regardless of a company's place of incorporation, as long as the COMI of the relevant company has been in Hong Kong for six months, the Mainland court may recognise and grant assistance to Hong Kong appointed liquidators.[16] That would have been enough to satisfy the requisite second core requirement (there is a real possibility of the winding-up order benefiting the petitioner) for the Hong Kong court to exercise jurisdiction to wind-up a foreign incorporated company. This could potentially resolve some of the difficulties the second core requirement poses to the winding-up of offshore incorporated Hong Kong listed Mainland enterprises in Hong Kong as outlined in section 2 above.

On 15 December 2021, the Shenzhen Intermediate People's Court recognised the Hong Kong appointed liquidators of Samson Paper. Hopefully Hong Kong liquidators, with assistance from the Mainland courts, will be able to undertake a more effective and efficient insolvency process for the benefit of all creditors, overcoming barriers often seen in trying to secure control of companies and assets in the Mainland.

Reciprocally, pursuant to a letter of request issued by the Hainan Province Higher People's Court ("**Hainan Court**"), Harris J granted an order recognising the administrators of HNA Group Co, Limited appointed by the Hainan Court. Recognition was granted on the basis that the Mainland proceedings constituted a collective insolvency process and the company was incorporated in the Mainland.[17]

This is a much-awaited framework for co-operation between the courts of Hong Kong and the Mainland in cross-border insolvency matters, which is a welcome development given the close economic ties between the two jurisdictions. It is very much hoped that the pilot scheme will expand beyond the three pilot areas into other common cities of choice for investments from Hong Kong and overseas.

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> The Bill will introduce a statutory corporate rescue procedure and insolvency trading provisions in Hong Kong.

5. New Corporate Rescue Bill

In November 2020, the Hong Kong government announced that it intends to hold a new round of consultation to finalise the Companies (Corporate Rescue) Bill (the "**Bill**") to be presented to the Hong Kong Legislative Council in the 2020/2021 legislative session. The Bill will introduce a statutory corporate rescue procedure and insolvency trading provisions in Hong Kong.

The proposed corporate rescue procedure will begin with the appointment of a provisional supervisor who will be an independent professional third party and must be a certified public accountant or a person qualified to practice as a solicitor.

14. In *Re Samson Paper Company Limited* [2021] HKCFI 2151.
15. In *Re China All Access (Holdings) Limited* [2021] HKCFI 1842.

16. It should be noted however that if the company is incorporated in Hong Kong, there is a rebuttable presumption that the company's COMI is in Hong Kong: see *Re Zhaoheng Hydropower (Hong Kong) Limited* (In Liquidation) [2022] HKCFI 248, the second case where the Hong Kong court issued a letter of request pursuant to the framework.
17. Prior to the signing of the arrangement on mutual recognition of and assistance to cross-border insolvency proceedings between Hong Kong and Mainland, Harris J had made the first order recognising a Mainland administrator in *Re CEFC Shanghai International Group Limited (in liquidation in Mainland China)* [2020] HKCFI 167 on the basis that Mainland corporate bankruptcy proceedings are collective insolvency proceedings and the subject company is incorporated in Mainland China. The Hong Kong court has subsequently granted a number of recognition orders providing assistance to administrators appointed in Mainland bankruptcy proceedings.

During the provisional supervision period,[18] there will be a moratorium on all civil proceedings and actions against the company. The provisional supervisor will gain control of the company's business as its agent, consider proposals for restructuring the debts of the company and, where appropriate, devise a rescue proposal for approval by the company's creditors at a creditors' meeting. Once approved, the company may enter into a voluntary arrangement under the supervision of a supervisor.

> "During the provisional supervision period, there will be a moratorium on all civil proceedings and actions against the company.

The Bill also seeks to introduce insolvency trading provisions whereby, subject to certain statutory defences, a director will be held responsible for insolvent trading and liable to make a contribution to the company's assets if he or she knew or ought to have known that the company was insolvent when the debt was incurred, or would become insolvent by incurring the debt. Proposed statutory defences include, for example, where the director has taken all reasonable steps to prevent the company from incurring the debt.

However, there have been no further announcements on the progress of the enactment of the Bill. At the time of writing, the precise legislative timetable remains unclear. It remains to be seen when these much-needed legislative reforms, which will bring the Hong Kong corporate rescue regime in line with those in the UK and Singapore, will be implemented.

18. The initial period of provisional supervision is 45 business days, which may be extended to 6 months with creditors' consent and beyond 6 months with leave of the court.

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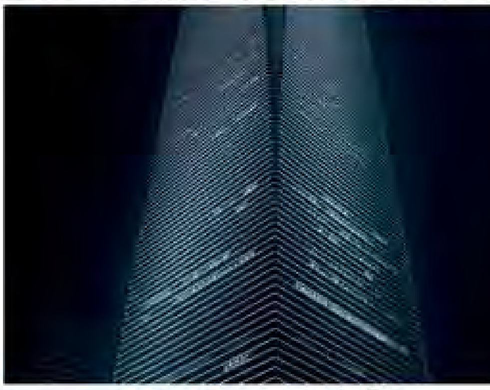


JAPAN
Key Developments and Latest Trends in Japan

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In recent years, out-of-court workouts, particularly turnaround ADR (*Jigyo Saisei ADR*) under the Industrial Competitiveness Enhancement Act (the "**Act**") ("**Turnaround ADR**"), have increased in popularity in Japan compared to judicial insolvency proceedings, such as civil rehabilitation (*Minji Saisei*) or corporate reorganization (*Kaisha Kosei*) proceedings.

The Act has recently been amended to enhance the chances of success of out-of-court workouts under Turnaround ADR. This is anticipated to have a significant impact on insolvencies in Japan.

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Turnaround ADR procedures are supervised by three mediators (typically comprising two attorneys and a certified public accountant).

This article outlines the key features of Turnaround ADR and the recent amendments to the Act.

1. Overview of Turnaround ADR

Large and medium-sized companies in Japan are increasingly turning to Turnaround ADR as compared to judicial insolvency proceedings. This trend is particularly notable for listed companies as in-court insolvency procedures would trigger a de-listing, while informal workouts would not.

Turnaround ADR commences with a debtor filing an application with the Japanese Association of Turnaround Professionals ("**JATP**")[1] and sending a "standstill" notice[2] in the joint names of the debtor and the JATP to financial creditors. A debtor is expected to negotiate with its financial creditors during the standstill period[3].

The followings are main characteristics of Turnaround ADR:

(1). Only financial creditors are subject to the proceedings

Turnaround ADR focuses primarily on the workout of debts owed to financial creditors. In principle, trade creditors are not subject to Turnaround ADR. This enables trade debtor companies to avoid deterioration in the value of their businesses.

As Turnaround ADR does not exclude overseas financial creditors, it is theoretically possible for a debtor to include its overseas financial creditors in its business rehabilitation through Turnaround ADR even if such creditors have no business presence in Japan. However, overseas financial creditors, especially those without any business presence in Japan, would not usually be subject to Turnaround ADR procedures as their claims usually account only for a small portion of the target claims and because communications with such creditors would involve additional time and costs.

(2). Proceedings are presided over by the fair and neutral mediators

Turnaround ADR procedures are supervised by three mediators (typically comprising two attorneys and a certified public accountant) specialising in company turnarounds, selected by the JATP, and settlements among debtors and financial creditors are facilitated by the mediators. This keeps the process fair among creditors.

(3). Unanimous consent of all creditors is required

Under Turnaround ADR, the unanimous consent of all participating creditors is required for a rehabilitation plan to be approved. This means a single "hold-out" creditor, even one with a small amount of claim ("**Small-Claim Creditor**") would be able to block a rehabilitation plan and cause the Turnaround ADR to fail.

2. Measures to enable smooth restructuring of business under Turnaround ADR

(1) Concerns about treatment of financing claims and trade claims in judicial insolvency proceedings following failure of Turnaround ADR

1. JATP is a non-profit organization that is (i) licensed by the Ministry of Justice to engage in dispute resolution work and (ii) further authorized by the Ministry of Economy, Trade and Industry to engage in activities to guide interested parties to consensual arrangements in an effort to help financially ailing companies.
2. A "standstill" notice typically requests the participating creditors not to collect debts, take individual enforcement actions (including a petition for commencement of bankruptcy, civil rehabilitation or corporate reorganisation proceedings).
3. A "standstill" period expires at the time of the first creditors meeting, but is usually extended until the third creditors meeting with the unanimous consent of all participating creditors.[4.] Journal of Laws of 2019, item 55 as amended.

Debtors undergoing Turnaround ADR may fail to obtain the unanimous consent of all participating creditors. In such cases, it is not uncommon for the debtors to file civil rehabilitation or corporate reorganisation proceedings. These judicial insolvency proceedings, however, give rise to two primary concerns, namely:

(a) whether claims in respect of debtor-in-possession ("**DIP**") financing that are provided during the Turnaround ADR (i.e., prior to commencement of judicial insolvency proceedings) ("**Pre-DIP Financing Claims**") would be given priority over other pre-filing claims in the judicial insolvency proceedings; and

(b) whether the claims of trade creditors would enjoy the same level of protection in the judicial insolvency proceedings as they would in the Turnaround ADR.

In judicial insolvency proceedings, unsecured pre-commencement claims (i.e., unsecured claims that arise prior to the commencement of judicial insolvency proceedings) should in principle be given equal treatment. Thus, without special treatment, Pre-DIP Financing Claims would be treated as unsecured pre-commencement claims with no priority over other pre-commencement claims should the debtor subsequently undergo judicial insolvency proceedings. This would make it difficult for a debtor to obtain the DIP financing it needs to restructure its business in the Turnaround ADR.

Similarly, trade creditors, whose claims are generally paid in full in the Turnaround ADR, are not guaranteed the same level of protection in judicial insolvency proceedings. Aware of this risk, trade creditors will sometimes cease their business dealings with a debtor in the course of the Turnaround ADR, if it seems to them likely that the debtor will eventually undergo judicial insolvency proceedings. Such risk mitigation by trade creditors has sometimes made it difficult for debtors to restructure their businesses.

(2) Giving priority to DIP-Financing Claims

To overcome the aforementioned difficulties associated with Pre-DIP Financing Claims, the Act requires a court to take the JATP's "Confirmation"[4] into account when determining whether a rehabilitation or reorganisation plan would impair the requirement that claims are treated equally, in situations where a rehabilitation or reorganisation plan submitted to the court or approved by creditors contains amendments to the terms of the Pre-DIP Financing Claims, and such amendments are different from these pertaining to other pre-commencement claims.

(3) Giving priority to trade creditor claims

The Act also provides a scheme to render similar protection to trade creditors in judicial insolvency proceedings to address the difficulties in respect of trade creditor claims. More specifically, under the Act:

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> Debtors undergoing Turnaround ADR may fail to obtain the unanimous consent of all participating creditors.

(a) if the JATP provides confirmation that (i) the claim of a trade creditor involves a small amount and (ii) the settlement of such claims is necessary to avoid significant impairment to the debtor's business ("Confirmed Claims"); and

(b) if civil rehabilitation or corporate reorganisation proceedings are filed or commenced against the debtor following the failure of Turnaround ADR, and the court takes the JATP's Confirmation into account:[5]

(x) to determine whether settlement of the Confirmed Claim is prohibited by a temporary restraining order (in situations where, following a petition for commencement of civil rehabilitation or corporate reorganisation proceedings, the court wishes to issue a temporary restraining order prohibiting payment of pre-injunction debts and disposition of the debtor's assets);

4. The JATP's "Confirmation" refers to the JATP's confirmation that (i) the corresponding DIP financing is indispensable to the continuation of the relevant debtor's business and (ii) all the financial creditors participating in the Turnaround ADR have agreed to give priority to the Pre-DIP Financing Claims over the other claims of such creditors

5. The Act contains almost identical stipulations for situations where a debtor undergoes corporate reorganisation proceedings following failure of Turnaround ADR.

(y) to determine whether such settlement is necessary to avoid significant impairment to the debtor's business (in situations where, following the commencement of civil rehabilitation or corporate reorganisation proceedings, the debtor has filed a petition for the court approval for settlement of a Confirmed Claim on grounds that it involves a small-amount, and that such settlement is necessary to avoid significant impairment to the debtor's business); or

(z) to determine whether such difference would impair the requirement that the claims be treated equally (in situations where, following the commencement of civil rehabilitation or corporate reorganisation proceedings, a rehabilitation or reorganisation plan submitted to the court or approved by the creditors contains amendments to the terms of a Confirmed Claim, and such amendments are different from those pertaining to other pre-commencement claims).

> "When Turnaround ADR fails, it is not uncommon for a debtor to file for judicial insolvency proceedings.

3 Recent amendments to the Act in 2021

(1) Background – Remaining concerns with judicial insolvency proceedings following the failure of the Turnaround ADR

As noted above, the unanimous consent of all participating creditors is required for a rehabilitation plan to be approved under Turnaround ADR. Accordingly, even a Small-Claim Creditor will be able to block the plan.

When Turnaround ADR fails, it is not uncommon for a debtor to file for judicial insolvency proceedings, which would lead to a significant deterioration in the creditworthiness of the debtor. Moreover, if the judicial insolvency proceedings following the failure of Turnaround ADR takes time to process, the value of the debtor's business would be considerably damaged.

(2) Amendments to the Act – Transition to Simplified Rehabilitation Proceedings (Kan-i Saisei)

To mitigate the concerns above, the Act was amended on June 16, 2021.

The Act now adopts a scheme that makes it easier for debtors to apply for simplified rehabilitation proceedings (*Kan-i Saisei*). *Kan-i Saisei* essentially involves short-term civil rehabilitation proceedings that obviates the need for investigation and determination of claims required for ordinary rehabilitation proceedings. This scheme is similar to the ones described in paragraphs 2(2) and 2(3) above. Under this scheme:

(a) the debtor may, if it has obtained the consent of creditors with three-fifths (3/5) or more of total claims (by value) in a resolution on a proposed rehabilitation plan under the Turnaround ADR, request the JATP provide confirmation that the reduction of claims under the rehabilitation plan is indispensable for the rehabilitation of the debtor's business; and

(b) if a petittion is filed for the commencement of simplified rehabilitation proceedings (*Kan-i Saisei*), the court will be required to take the JATP's confirmation (if any) into account in determining whether the rehabilitation plan is detrimental to the common interests of creditors and, in turn, whether simplified rehabilitation proceedings (*Kan-i Saisei*) should be commenced[6].

Under this scheme, the rehabilitation plan that has been rejected in a Turnaround ADR due to the opposition of Small-Claim Creditors may immediately be proposed to creditors in simplified rehabilitation proceedings (*Kan-i Saisei*).

[6] Under the Civil Rehabilitation Act, if a rehabilitation plan would be detrimental to the common interests of creditors, the court may not issue an order for commencement of simplified rehabilitation proceedings (*Kan-i Saisei*).

Accordingly, this scheme is expected to have the effect of discouraging Small-Claim Creditors from rejecting rehabilitation plans under Turnaround ADR, since the proposed rehabilitation plan under the Turnaround ADR would be been approved by creditors with three-fifths (3/5) or more of total claims (by value), and the same plan would likely be approved under simplified rehabilitation proceedings (*Kan-i Saisei*). In such circumstances, creditors would not be expected to block the rehabilitation plan proposed under the Turnaround ADR, as this would simply damage the value of the debtor's business during the transition period between the Turnaround ADR and the simplified rehabilitation proceedings (*Kan-i Saisei*).

4. Conclusion

With the aforementioned amendments to the Act, Turnaround ADR has now become a much more effective restructuring tool for debtors in financial difficulty.
This is anticipated to have a significant impact on insolvencies and further facilitate out-of-court restructuring schemes in Japan.

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> Turnaround ADR has now become a much more effective restructuring tool for debtors in financial difficulty.

LUXEMBOURG

Implementation of Directive (EU) 2019/1023 in Luxembourg: Struggles and Pitfalls

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Implementation of Directive (EU) 2019/1023 in Luxembourg: Struggles and Pitfalls

In Luxembourg, the dreaded scenario of a wave of bankruptcies in connection with the Covid-19 crisis did not materialise. Indeed, only 1,199 bankruptcies were registered in 2020 and 2021, fewer than in 2019 (1,263 bankruptcies).[1] However, the current situation, in particular the war in Ukraine, will have consequences for distressed businesses. It is expected that when the moratorium on voluntary bankruptcy filings is lifted and various state subsidies come to an end, many businesses will face liquidity issues[2] or at least will have to reorganise their assets or activities (if they have not yet done so).

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> When the moratorium on voluntary bankruptcy filings is lifted and various state subsidies come to an end, many businesses will face liquidity issues

The current Luxembourg legislative framework lacks sufficient tools to allow them to do so. Officially, there are three restructuring procedures, in addition to bankruptcy, available in Luxembourg (excluding the court-ordered liquidation of companies that have seriously breached the law). In practice, however, restructuring through controlled management is too rarely used to be considered relevant.

The usual (pre-Brexit) strategy for Luxembourg-based companies that wished to restructure their assets and activities was either to enforce or threaten to enforce a security interest in order to bring about a consensual arrangement or to shift their centre of main interests to the United Kingdom, where they could (allegedly) benefit from more creditor-friendly and flexible procedures such as a scheme of arrangement or a pre-pack administration process.[3] Since Brexit, however, these procedures have become less predictable in terms of their recognition in EU jurisdictions where relevant assets may be located and, therefore, less attractive. The Luxembourg legislature is aware, however, of the shortcomings of the current Luxembourg legislative framework for corporate restructuring and insolvency and thus tabled Bill No 6539 to address these issues and create a modern toolbox to allow distressed debtors to reorganise their assets and/or activities in Luxembourg.

During review of the bill, Directive (EU) 2019/1023 (the "**Directive**") on preventive restructuring frameworks was adopted. The deadline for implementation of the directive into national law by the Member States was 17 January 2021, with the possibility to request a one-year extension. While the Directive and Bill No 6539 have similar objectives, there are a number of noteworthy differences, such as the requirement to allocate creditors to various classes and the introduction of a cross-class cram-down, similar to Chapter 11 proceedings in the US. It was therefore decided to align the reform of the Luxembourg restructuring and insolvency framework with the implementation of the Directive, in order to kill two birds with one stone.

This article does not cover all conditions to open restructuring or bankruptcy proceedings in Luxembourg and does not explore ancillary topics such as directors' duties and liability in the area of insolvency. Nor does it detail all proposed provisions of Bill No 6539 and the Directive. Rather the aim is to provide an objective assessment of the shortcomings in the current Luxembourg restructuring and insolvency framework and the major expected changes further to the reform.

The current Luxembourg restructuring and insolvency toolbox

A number of restructuring and insolvency tools are available in Luxembourg, which for the most part are obsolete and have fallen into disuse over the last few decades due to the risk assumed by creditors, their complexity and length, which can be value disruptive for the underlying business, and the stringent adjudication criteria, which usually only allow for restructuring of the business at a late stage (i.e. when it is on the verge of bankruptcy), limiting in practice their success as preventive and curative measures. None of the existing procedures permit the group's liabilities, as opposed to those of the Luxembourg entity, to be taken into account or allow credit bidding, which explains why there is very little appetite by lenders to use Luxembourg as a restructuring venue.

1. Available at https://paperjam.lu/article/autant-faillites-qu-en-2020
2. Available at https://www.wort.lu/fr/economie/la-vague-de-faillites-pas-encore-en-vue-61e6895cde135b92361d377f#:~:text=Le%20secteur%20des%20services%20rest-e,cr%C3%A9ances%20et%20en%20informations%20%C3%A9conomiques%20
3. Available at https://www.loyensloeff.com/en/en/news/news-articles/comi-luxem-bourg-technical-analysis-case-law-critique-n22581/

Below we provide a brief overview of the Luxembourg legislative options available to debtors facing insolvency and more generally financial distress. The aim of this article is not to describe all of the conditions for these procedures but rather to detail their main limitations as restructuring tools and the reasons for their inefficiency:

- A scheme of arrangement or composition with creditors (*concordat*), introduced by the Act of 14 April 1886, as amended, and codified in Articles 508 to 527 of the Commercial Code, will be adjudicated if the debtor (i) is unable to pay its debts as they fall due (*cessation de paiements*) and unable to obtain credit (*ébranlement du credit*) and (ii) is not responsible for its financial situation and is acting in good faith. Once the arrangement has been approved and ratified by the court, the court-appointed judge will examine it every three months. It will come to an end if the debtor's situation improves, in which case the debtor must satisfy all its creditors. The composition or arrangement may also be revoked by the court in specific cases (e.g., if the debtor fails to comply with the applicable conditions or if the conditions for bankruptcy are met). From a secured creditor's perspective, this is not an attractive option, as such creditors will only be able to vote on the composition plan drawn up by the debtor if they waive their security interests (mortgage, lien or pledge), and for this reason they will have no incentive to take part in the negotiations or approve the plan. An approved and ratified composition plan will therefore have no effect on the rights of secured creditors to enforce their claims and security interests against the debtor, which may lead to its bankruptcy, thus being counterproductive. Moreover, considering the high threshold to be met in order to be adjudicated and the risk of the approved plan not being ratified by the court, a scheme of arrangement generally degenerates into a winding-up scenario. This explains why this procedure has fallen into disuse, with no scheme of arrangement adjudicated recently.[4]

- A reprieve from payments (*sursis de paiement*), introduced by the Act of 2 July 1870 and codified in Articles 593 to 614 of the Commercial Code, will be adjudicated if the debtor is temporarily unable to pay its debts due to an extraordinary and unexpected event. Historically, this procedure has rarely been used in Luxembourg. The few proceedings typically involve professionals of the financial sector. During the 2008 global financial crisis, the Luxembourg subsidiaries of three Icelandic banks (Glitnir, Kaupthing and Landsbanki) in financial distress applied for a reprieve from payments. This was the last time a reprieve from payments was granted in Luxembourg.

- Controlled management (*gestion contrôlée*), introduced by a grand ducal decree of 24 May 1935, is the closest procedure in Luxembourg to Chapter 11 and hence the only procedure still used in Luxembourg that could qualify as a restructuring process. Controlled management is aimed at reorganising the debtor's business or, if this is not possible, optimising the realisation of its assets. However, it is rarely used in practice for a number of reasons, as outlined below.

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> Controlled management is, however, generally an inadequate means of restructuring the business of a debtor on the brink of insolvency

In the context of controlled management, the competent court appoints one or more commissioners to manage the debtor with a view to restructuring its business or realising its assets. In order to qualify for this procedure, (i) there must be a chance of resolving the company's financial difficulties, despite the fact that it is temporarily unable to meet its obligations, and (ii) it must be demonstrated that controlled management would improve the likelihood of the company's assets being realised in the interest of its creditors.
Controlled management is, however, generally an inadequate means of restructuring the business of a debtor on the brink of insolvency for the following reasons:

4. AS. Bellamine and S. Attoumani, "Le concordat préventif de faillite : une alternative méconnue à la faillite", JN Sociétés, 2012/7, 195-198.

(i) while this is the only restructuring procedure still used in Luxembourg, aside from bankruptcy, the number of debtors for which controlled management is actually granted is too low (0 to 3 per year over the past decade) for it to be considered relevant;[5]

(ii) the debtor should have lost creditworthiness in order to successfully apply for controlled management, but this condition is hard to prove and will only become manifest when the debtor is effectively unable to pay its debts as they fall due out of its own cash flows, i.e. the debtor is in a state of *cessation de paiements*, in which case it will meet the criteria for bankruptcy. This is a potentially high risk and the debtor may have little to no control over it;

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Bankruptcy is the most widely used insolvency procedure in Luxembourg

(iii) if controlled management is granted, the court can nonetheless declare the company bankrupt if it meets the criteria for bankruptcy at any time during the course of the controlled management proceedings, according to settled Luxembourg case law;[6]

(iv) the Luxembourg courts have rejected applications for controlled management on the ground that the proposed reorganisation plan would not improve realisation of the applicant's assets, as some of its subsidiaries were experiencing serious financing difficulties, in particular due to a lack of financial support from their parent company and a general difficulty for group companies to obtain external financial assistance due to a crisis facing the group, which could adversely affect the expected revenue under the plan, consisting largely of dividends and debt repayments (the applicant being only a holding company and having no commercial activity of its own); this is a scenario which is particularly relevant in Luxembourg where holding companies (*sociétés de participation financière*) with no independent source of income are prevalent and widely used in the context of international deal structuring; and

(v) from a strategic perspective, controlled management is not an obvious restructuring choice, as it is a court-led procedure in which the debtor does not remain in possession, as the appointed commissioner(s) are responsible for managing the debtor's assets and drawing up the reorganisation plan; considering that controlled management is rarely used in Luxembourg and the debtor has no control over the appointment of the commissioner(s), there will be uncertainty as to the latter's level of expertise and willingness to properly manage the debtor's assets and engage in potentially lengthy and contentious negotiations to achieve an optimal result for the business and/or creditors.

In view of the foregoing, it is clear that debtors generally lack control over the outcome of controlled management proceedings, which may result in a winding-up scenario.

- Bankruptcy (*faillite/banqueroute*), governed by Articles 437 to 592 of the Commercial Code, will be adjudicated if the company is (i) unable to pay its debts as they fall due (*cessation de paiements*) and (ii) unable to obtain additional credit (*ébranlement du credit*). In this context, a bankruptcy trustee (*curateur*) will be appointed by the court to realise the debtor's assets, in view of settling all or part of the claims against the bankruptcy estate and which may have been accepted in the bankruptcy. Bankruptcy is the most widely used insolvency procedure in Luxembourg.

[5] See https://gouvernement.lu/en/publications/rapport-activite/minist-justice/mjust/2020-rapport-activite-mjust.html.
[6] Court of Appeal, 29 April 1998, no 21924.

Considering the financial situation of the debtor when bankruptcy is adjudicated, it will generally result in the winding-up of the company, although this is not always the case. On rare occasions, the debtor may emerge from bankruptcy and be allowed to continue its activities as a going concern if its creditors receive satisfaction for their claims accepted by the Luxembourg court in accordance with the distribution plan and assets remain after the settlement of all claims (i.e. the debtor has sufficient assets remaining following the close of liquidation), without any further steps on the part of the company being required

Hence, bankruptcy may be considered a viable restructuring option if it appears that the debtor meets the applicable criteria based solely on liquidity concerns (e.g., it has illiquid assets far in excess of its due and payable liabilities) and will be able to settle its claims using the proceeds from the realisation of its assets. In some cases, a Luxembourg debtor acting as a guarantor for affiliated group companies may be able to use bankruptcy to restructure. However, this will entail significant cooperation between the court-appointed bankruptcy trustee, the shareholders of the debtor and management of the affiliated companies in order to reach a compromise on guaranteed claims at the local level or to find alternative guarantees in order to reduce the liabilities of the Luxembourg debtor and achieve a distribution plan that works for all admitted creditors and allows the Luxembourg debtor to emerge from bankruptcy. Needless to say, this scenario is quite rare in practice and, in general, bankruptcy cannot be considered a viable option in Luxembourg for the reorganisation of assets or activities.

In view of the foregoing, it is clear that Luxembourg lacks effective and well-tested statutory tools to facilitate judicial or extrajudicial restructuring. As a result, the chances of a Luxembourg company achieving judicial recovery or restructuring are extremely limited. Out-of-court restructuring is also limited in practice due to factors such as a lack of experience and inadequate legal tools, which push lenders and debtors to pursue extrajudicial restructuring in foreign jurisdictions.

The need for reform of the restructuring and insolvency legislative framework and the introduction of Bill No 6539

The urgent need to reform Luxembourg's restructuring and insolvency legislation has been debated for over a decade. For example, the Luxembourg House of Representatives acknowledged on 8 February 2011 that, in the context of a crisis, an efficient regime for distressed businesses is a national priority. This was further highlighted by the steady increase in the number of bankruptcies adjudicated in Luxembourg, which has nearly doubled in the past 20 years (approximately 600 in 2000 compared to 1,199 in 2021). Considering as well the upcoming end to the moratorium on the statutory obligation for the managers of bankrupt businesses to declare bankruptcy and the wave of bankruptcies expected to follow, the reform of Luxembourg's restructuring and insolvency legislation is a more pressing matter than ever.

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> The preventive aspect of the draft bill aims to prevent the systematic use of bankruptcy as a means of resolving financial difficulties

Bill No 6539 on the preservation of businesses and the modernisation of bankruptcy law was introduced on 1 February 2013[7] with a view to addressing these concerns. The bill has four main aspects, namely preventive, curative, punitive and social. This article focuses on the first aspect, i.e. prevention, and the related proposals.

The preventive aspect of the draft bill aims to prevent the systematic use of bankruptcy as a means of resolving financial difficulties. The core provisions relating to this aspect centre on the creation of an early warning mechanism, in order to identify companies facing financial difficulties and ask them to take action in order to preserve their activity, and the possibility for debtors to benefit from a stay of proceedings while preserving the rights of

[7] See https://chd.lu/wps/portal/public/Accueil/TravailALaChambre/Recherche/RoleDesAffaires?action=doDocpaDetails&backto=/wps/portal/public/Accueil/Actualite&id=6539.

creditors.

Prevention is of the utmost importance and will have significant consequences for Luxembourg restructuring and insolvency law, as it aims in particular to replace obsolete and unused (or very rarely used) procedures, such as the scheme of arrangement/composition with creditors, reprieve from payments and controlled management, with judicial and extrajudicial restructuring procedures that are easier and less expensive for debtors to implement.

With respect to the early warning mechanism, the bill proposes that various statistical, legal, and financial data relating to Luxembourg businesses be collected and compiled by the Secrétariat du Comité de conjuncture, in order to build a file for those companies deemed, based on objective criteria, to be facing financial difficulties. The Secrétariat may request companies facing financial difficulties to provide information about their envisaged restructuring actions.

A business in jeopardy may then request the appointment of a conciliation officer (conciliateur d'entreprise) with a view to facilitating the reorganisation of all or part of its assets and business. In this regard, it should be noted that the debtor may propose a conciliation officer. The conciliation officer shall, in the context of judicial or extrajudicial proceedings, prepare and facilitate the conclusion of an out-of-court agreement with creditors on the reorganisation of all or part of the debtor's assets or activities, the adoption by the creditors of a reorganisation plan, or the sale, by way of a judicial decision, of all or some of the distressed debtor's assets or activities to one or more third parties.

The possibility to conclude an out-of-court agreement is a welcome addition to the Luxembourg legislative landscape, as it will substantially reduce the cost and duration of the procedure to reorganise the assets and activities of distressed debtors. Moreover, the bill provides protection for creditors for acts carried out further to the out-of-court agreement, which cannot be voided under the clawback provisions if the debtor subsequently declares bankruptcy. Furthermore, creditors that are parties to the agreement cannot be held liable on the ground that the agreement did not ultimately succeed in preserving the continuity of the distressed debtor's business, thus effectively protecting the creditors against a potential subsequent bankruptcy of the debtor. This is generally beneficial to both creditors and debtors, as creditors will have an incentive to reach an agreement with debtors at an early stage in the restructuring process, thereby increasing the chances of financial recovery.

Under the bill, judicial reorganisation proceedings may be initiated at the request of the distressed debtor. This procedure aims to preserve, under judicial supervision, the continuity of all or some of the debtor's assets or activities. Following a decision by the court to open judicial reorganisation proceedings, the following principles will apply:

- debtor in possession: debtors relying on judicial reorganisation remain in control of their assets, in whole or in part, and the day-to-day operation of their business;

- stay of individual enforcement actions: all payment obligations (with the exception of voluntary payments required for continuity of the business), enforcement procedures and attachments will be suspended for a maximum period of six months, which may be extended to 12 months;

- the debtor has the right to submit a restructuring plan to the affected parties for approval;

- initially, the bill provided that the reorganisation plan had to be approved by a majority of creditors representing at least half the outstanding claims, with such approval being binding on all creditors; however, the provisions on adoption of the reorganisation plan have been heavily amended over the years (see below).

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> creditors will have an incentive to reach an agreement with debtors at an early stage in the restructuring process, thereby increasing the changes of financial recovery

Due to the numerous implications of the reform, the bill has not yet been finalised. However, two recent developments resulted in acceleration of the review of the bill with a view to expediting its adoption:

- on 22 July 2021, the bill was divided into two different bills, namely Bill No 6539A, which is mainly concerned with the preventive and curative aspects of the reform, and Bill No 6539B, which falls outside the scope of this article and aims to create a new procedure for judicial dissolution winding-up without liquidation of certain businesses without assets, activities or employees;[8]

- additional changes were made to Bill No 6539A in order to adapt it to the purpose of transposing Directive (EU) 2019/1023 on preventive restructuring frameworks.

Directive (EU) 2019/1023 on preventive restructuring frameworks

The Directive (EU) 2019/1023[9] aims to ensure the availability of minimum restructuring measures across Member States to enable debtors in financial distress to address their financial difficulties at an early stage and avoid, insofar as possible, formal insolvency proceedings. Albeit there are certain differences between Bill No 6539A and the Directive, which required adaptation of the bill, it should be noted that both pursue very similar objectives, i.e. the promotion of access to early warning tools to encourage the restructuring of distressed debtors at an early stage, the provision of a stay of individual enforcement actions for a maximum period of 12 months, subject to extension and renewal in order to protect restructuring negotiations, and the introduction of a preventive restructuring framework.

The Directive introduces a number of constraints and concepts intended to protect the rights of the creditors, namely:

- the concept of affected parties, namely creditors, including, where applicable under national law, workers, classes of creditors, and equity holders, whose claims and interests are directly affected by the restructuring plan;

- the requirement to assign creditors to classes based on objective and assessable criteria (national law shall provide for the allocation of creditors amongst at least two classes, namely secured and unsecured creditors);

- rules on adoption of the restructuring plan, which must be approved by at least the affected parties, in terms of a majority in the amount of their claims or interests in each class; Member States have the option to provide for an additional majority condition (i.e. the reorganisation plan should also be approved by a majority of the number of affected parties in each class); these majority thresholds may be increased to up to 75% of the amount of claims or interests in each class, respectively the number of affected parties in each class;

- in view of confirmation of the adopted reorganisation plan, several aspects shall be reviewed and tests applied by the court, including the best interest of creditors test, if certain creditors or classes of creditors voted against adoption of the restructuring plan, and which will be satisfied if no dissenting creditor would be worse off under the restructuring plan compared to its situation if the normal ranking under national law in the event of liquidation, a piecemeal scenario, sale as a going concern or the next-best alternative if the

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[8] See https://chd.lu/wps/PA_RoleDesAffaires/FTSByteServingServletImpl?path=18996133744B43A4CDED1398BDC7BD70981DDE37167A7941FEE63808EF8C7B86B42FEBF853EAABF0F83A235D-05B704A6$B161FB79FE2200C31E0F0ACECC3DE9A5

[9] See https://eur-lex.europa.eu/legal-content/en/ALL/?uri=CELEX:32019L1023

restructuring plan were not confirmed;

- the introduction of a cross-class cram-down, allowing for ratification of the restructuring plan by the court at the debtor's request or with the debtor's consent, even when it has not been approved by all classes of creditors, but only if dissenting classes of affected creditors will not be unfairly prejudiced by the proposed plan. For a cross-class cram-down to be confirmed, a majority of affected (voting) creditors must have approved the reorganisation plan, including at least one class of secured or senior creditors or, in the absence thereof or where so provided by national law, impaired parties in the money (i.e. a class that would be entitled to receive a payment or keep an interest upon valuation of the debtor as a going concern). However, in accordance with Recital 54 to the Directive, this rule is adapted where there are only two classes of creditors, in which case the consent of at least one class should be deemed sufficient if the other conditions for the cross-class cram-down are met. Other conditions to confirm a cross-class cram-down are verification that dissenting 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 (the so-called "relative priority rule") and that no class of affected parties may receive or keep more than the full value of its claims or interests under the restructuring plan. In addition, the best interest of creditors test must be applied. As an alternative to the relative priority rule, Member States may choose to apply the absolute priority rule, whereby a dissenting class of affected creditors is protected by ensuring that it is paid in full if a more junior class receives any distribution or keeps any interest under the restructuring plan. In practice, according to this rule, creditors will only be able to receive a distribution if more senior creditors have been paid in full.

The above tools do not currently exist in Luxembourg and will give Luxembourg a competitive edge where Luxembourg financing structures typically contain different layers of debt and creditors. Indeed, such a modern toolbox will strengthen Luxembourg's position as an attractive and creditor-friendly venue for the structuring of international financing transactions, both at the start and throughout the term of financing arrangements, especially in the event of default, if a reorganisation proves necessary to preserve going-concern value or if new money is needed.

Modification of Bill No 6539A in order to transpose Directive (EU) 2019/1023/EU

The Luxembourg committee in charge of examining Bill No 6539A and proposing amendments thereto reviewed the Directive in order to determine the necessary amendments to the bill and which options should be selected in Luxembourg in order to transpose the Directive.

The Luxembourg legislature has confirmed certain approaches for the determination of affected creditors and their allocation into classes.

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> removing equity holders from the equation will facilitate adoption of a reorganisation plan that provides for a debt-to-equity swap

In this regard, the committee confirmed that it is not intended for equity holders of a distressed debtor to be able to vote on the reorganisation plan in Luxembourg. This is a particularly convenient choice, as removing equity holders from the equation will facilitate adoption of a reorganisation plan that provides for a debt-to-equity swap (a potential restructuring option pursuant to Article 44 of Bill No 6539A). However, the impact of this choice will be limited as the agreement of equity holders will still be required for Luxembourg corporate law purposes, such as the adoption of a shareholder resolution for the acceptance of third parties as new shareholders when the distressed debtor is a Luxembourg private limited-liability company (société à responsabilité limitée), the most popular corporate form in Luxembourg, and pursuant to the provisions of Article 710-12 of the Act of 10 August 1915 on commercial companies, as amended. Therefore, in some cases, the implementation of a debt-to-equity swap under the reorganisation plan will still require the consent of equity holders, which will limit in practice the impact of this otherwise welcome addition to the Luxembourg insolvency and restructuring framework.

In addition, Bill No 6539A provides for the creation of only two classes of creditors, namely extraordinary deferred creditors (*créanciers sursitaires extraordinaires*) and ordinary deferred creditors (*créanciers sursitaires ordinaires*). The first class includes all creditors benefitting from a special lien or a mortgage, proprietary (secured) creditors (*créanciers propriétaires*), and the tax and social security authorities while the second class includes all other creditors. This approach raises some criticism. The Luxembourg legislature justifies the creation of two classes of creditors on the ground that including additional categories would be too complex. While having only two classes of creditors, defined in an objective manner, has the benefit of simplicity, such simplicity may be inconvenient if not irrelevant considering the position of Luxembourg as a central hub for international group and acquisition structuring, usually involving significant financing activities with complex waterfall structures and many categories of lenders and levels of debt (e.g. super senior, senior, mezzanine, second-lien, junior lender, etc.). These various categories of lenders will typically be allocated to the class of extraordinary creditors, despite the fact that their objectives may differ widely in practice (as a natural outcome of their relative positions and rights). In our opinion, it would be advisable to have additional classes of creditors if so justified by the debt structure of the distressed debtor and to opt for strict application of the absolute priority rule. This would also be a creditor-friendly solution, allowing, in the event of a cross-class cram-down, secured creditors to force the adoption of a reorganisation plan, thereby protecting the interests of creditors that initially negotiated better lending and security terms with the distressed debtor.

With regard to the adoption of the reorganisation plan, the Luxembourg legislature opted for a double majority approach, i.e. the plan must be adopted by a majority of creditors in each class and those representing a majority of the value of the claims in each class. If the plan is not adopted further to the initial vote, a cross-class cram down may be confirmed by the court, at the request or with the approval of the debtor, but only to the extent the reorganisation was approved by the class of ordinary creditors and dissenting extraordinary creditors are treated more favourably than ordinary creditors. This approach is however faulty as it does not envisage approval of the reorganisation plan by the extraordinary creditors only, in which case the best interest of creditors test must be conducted to protect the rights of ordinary creditors.

Conclusion

It is expected that Bill No 6539A will be adopted before the end of this year. This would put an end to a decade-long national debate and largely benefit the Luxembourg restructuring and insolvency landscape as well as the Luxembourg market as a whole, as restructuring and insolvency tools are a matter of concern for all lenders that wish to structure their activities through Luxembourg. Moreover, the adoption of Bill No 6539A will allow Luxembourg to offer viable alternatives to procedures available in the United Kingdom, such as company administration, which is loosely similar to the restructuring procedure provided for by the Directive as both aim at allowing a debtor to reorganise or realise its assets while benefitting from a stay of individual enforcement actions, effectively suspending the opening of insolvency proceedings at the request of creditor(s) which would otherwise result in the debtor's liquidation. Therefore, Luxembourg through a comprehensive legislation will be able to position itself as a one-stop shop with respect to debtor's lifecycle.

[10] See https://www.dammann-avocat.com/wp-content/uploads/2020/08/Dalloz-Classes-de-creanciers-oct.-2019.pdf for a comprehensive study on classes of creditors.
[11] See https://paperjam.lu/article/loi-sur-faillite-pourrait-etre?utm_medium=email&utm_campaign=01032022-soir&utm_content=01032022-soir+CID_c61e57930f7b76ef6765c2e-7b4359aa6&utm_source=Newsletter&utm_term=La%20loi%20sur%20les%20faillites%20pourrait%20enfin%20aboutir%20cette%20anne
[12] See https://uk.practicallaw.thomsonreuters.com/7-385-3012

POLAND
Recent developments in insolvency and restructuring in Poland

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A prestigious legal ranking, *Chambers and Partners*, ranks Magdalena in the in the field of restructuring and insolvency in its 2020 edition.
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1. Introduction

Polish insolvency and restructuring law has been regulated by two separate legal acts. The bankruptcy procedure is provided for in the Act of 28 February 2003 - Bankruptcy Law[1]. Issues related to the restructuring of debtors are governed by the Act of 15 May 2015 - Restructuring Law.[2]

There have been recent changes to the Restructuring Law implemented by:

- the Act of 28 May 2021 amending the Act on the National Register of Debtors and certain other acts[3] (entered into force on 1 December 2021); and
- the Act of 6 December 2018 on the National Register of Debtors[4] (entered into force on 1 December 2021).

> The Restructuring Law provides for the possibility of a global restructuring of secured receivables.

Furthermore, there have been changes to the Bankruptcy Law implemented by:

- the Act of 28 May 2021 amending the Act on the National Register of Debtors and certain other acts (entered into force on 1 December 2021); and
- the Act of 30 August 2019 amending the Bankruptcy Law and certain other acts[5] (entered into force on 24 March 2020).

2. Restructuring claims secured on debtors' asset

Lawmakers introduced amendments to the existing rule, according to which the arrangement does not cover security placed on the debtor's property by means of a mortgage, pledge, registered pledge, Treasury pledge or ship's mortgage without the consent of the creditor. According to the amendments, such receivable debts are covered by an arrangement by virtue of law if one of two conditions is fulfilled, in which case the consent of the creditor is not required (Art. 151, para. 2a of the Restructuring Law).

Firstly, the debtor presented to the creditor arrangement proposals providing for full satisfaction, within the time limit specified in the arrangement, of his receivable debt along with collateral receivables which were provided for in the contract that was the basis for establishing the security, even if said contract was effectively terminated or it expired.

Secondly, the debtor presented to the creditor arrangement proposals providing for satisfaction of the creditor to a degree not lower than that which he can expect in case of seeking the recovery of a receivable debt along with collateral receivables from the object of security.

The above-mentioned rules apply accordingly to receivable debts secured by a transfer to a creditor of the ownership of a thing, a receivable debt or another right (Art. 151, para. 3 of the Restructuring Law). Moreover, the regulation provided for in Art. 151, para. 2a and 3 of the Restructuring Law refers to all types of restructuring proceedings. Thus, the Restructuring Law provides for the possibility of a global restructuring of secured receivables. It means the alteration of the status of secured creditors in the whole restructuring system. The position of parties negotiating the arrangement is modified. The creditors and the debtor are no longer held hostage by creditors secured by the debtor's assets.

3. Stay of individual enforcement actions and contractual protection

The procedure for approval of an arrangement is one of four restructuring procedures known in Polish law. In comparison with others, it is the least formal procedure. It also gives the least scope of protection for a debtor. The recent amendments seem to change this. The initiation of a procedure for approval of the arrangement takes place out of court and is associated with the granting of immediate anti-enforcement and contractual protection

1. Journal of Laws 2020, item 1228 as amended, known hereinafter as the Bankruptcy Law.
2. Journal of Laws 2021, item 1588 as amended, known hereinafter as the Restructuring Law.
3. Journal of Laws of 2021, item 1080.
4. Journal of Laws of 2019, item 55 as amended.
5. Journal of Laws of 2019, item 1802.

for the debtor.
To initiate proceedings for approval of the arrangement, the debtor needs to enter a contract concerning the exercising of supervision over the course of the proceedings with a person who will act as the arrangement supervisor (Art. 210, para. 1 of the Restructuring Law). The second step is to make an announcement of fixing the arrangement day by the arrangement supervisor. This is possible after the preparation of the inventory of receivable debts, the inventory of disputed receivable debts, and a preliminary restructuring plan (Art. 226a, para. 1 of the Restructuring Law).

The debtor benefits from contractual protection and a stay of execution in the period between the day of making the announcement of fixing the arrangement day and the day of the valid discontinuance of the proceedings for approval of the arrangement or the completion of the proceedings for approval of the arrangement (Art. 226e of the Restructuring Law in connection with Art. 256 of the Restructuring Law and Art. 312 of the Restructuring Law).

Contractual protection means that it is not permitted for the lessor or the tenancy grantor to terminate the contract of lease or tenancy of premises or immovable property where the debtor's enterprise is run (Art. 226e of the Restructuring Law in connection with Art. 256, para. 1 of the Restructuring Law). The same treatment applies to contracts of credit, to the extent that funds are put at the disposal of the borrower before the day the proceedings are opened, as well as to lease contracts, property insurance contracts, bank account contracts, suretyship contracts, contracts covering licenses granted to the debtor, and guarantees or letters of credit issued before the day of making the announcement of fixing the arrangement day, as well as other contracts of fundamental importance for running the debtor's enterprise. The list of contracts of fundamental importance for running the debtor's enterprise is prepared by the court supervisor (Art. 226e of the Restructuring Law in connection with Art. 256, para. 2 of the Restructuring Law).

The rules for a stay of execution are as follows. Execution proceedings directed at the debtor's assets initiated prior to the day of making the announcement of fixing the arrangement day are suspended by operation of law on the day of the opening of the proceedings (Art. 226e of the Restructuring Law in connection with Art. 312, para. 1 of the Restructuring Law). After the day of making the announcement of fixing the arrangement day, it is inadmissible to direct execution at the debtor's assets or execute a ruling on securing a claim or order that a claim be secured on these assets (Art. 226e of the Restructuring Law in connection with Art. 312, para. 4 of the Restructuring Law).

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> The debtor benefits from contractual protection and a stay of execution.

Such broad protection afforded to a creditor requires a balance between the interests of the debtor and the interests of the creditors. An example of such mechanism is that the decision to make an announcement of fixing the arrangement day rests with the supervisor of the arrangement. An additional way of protecting creditors is that making an announcement of fixing the arrangement day is inadmissible if, within the last ten years, the debtor conducted proceedings for approval of the arrangement in which the announcement of the fixing of the arrangement day had been made, or if within the last ten years, restructuring proceedings regarding the debtor have been discontinued. An exception is situations when restructuring proceedings have been discontinued in consultation with the committee of creditors (Art. 226a, para. 2 and para. 3 of the Restructuring Law). Moreover, the effects of making an announcement of fixing the arrangement day can be repealed by a court upon a motion of the creditor, debtor, or the arrangement supervisor. This is the case when such effects are detrimental to creditors or if the circumstances of inadmissibility of making the announcement of fixing the arrangement day are disclosed (Art. 226f of the Restructuring Law).

Granting the debtor immediate protection at the opening of restructuring proceedings is an aid measure for a troubled debtor. The purpose of this solution is to enable the debtor to carry out restructuring. The recent changes in the procedure for approval of the arrangement seem to correspond with the approach chosen by EU legislators to insolvency and saving businesses. Granting the debtor a stay of execution and contractual protection is one of the key elements of the preventive restructuring mechanism provided for in the Second Chance Directive.[6]

4. Prepared liquidation (pre-pack)

> "Pre-pack makes the process of liquidation of the bankruptcy estate faster and less expensive.

Some changes set out in an amendment to the Bankruptcy Law have been introduced regarding prepared liquidation (pre-pack, Art. 56a et seq. of the Bankruptcy Law). Pre-pack concerns the sale of the debtor's enterprise or of an organised part thereof or of property assets forming a substantial part of the enterprise to the acquirer. It makes the process of liquidation of the bankruptcy estate faster and less expensive. The changes introduced regarding prepared liquidation can be divided into four groups.

Firstly, the amendment clarifies the regulations related to pre-pack. Doubts were resolved that the sale of the debtor's enterprise or of an organised part thereof or of property assets forming a substantial part of the enterprise could be to more than one acquirer. Moreover, it was specified that an application for approval of the terms of sale may be submitted by a participant in bankruptcy proceedings, i.e. the person who filed for bankruptcy, and by the debtor at every stage of the proceedings in the matter of declaration of bankruptcy (Art. 56a, para. 1 of the Bankruptcy Law and Art. 26, para.1 of the Bankruptcy Law).

Secondly, the new solutions aim at ensuring the transparency of proceedings and preserving the rights of creditors. The transparency element accompanies the initiation of a pre-pack procedure. There is an obligation to announce the submission of an application for approval of the terms of sale (Art. 56ab of the Bankruptcy Law).
When an application for approval of the terms of sale has been filed, the court appoints a temporary court supervisor or a compulsory receiver (Art. 56aa, para. 1 of the Bankruptcy Law). The task of the temporary court supervisor or the compulsory receiver includes submitting, within a specified time limit, a report covering information on the debtor's financial standing and on the type and value of the debtor's assets, as well as other information which is important for examination of the application for approval of the terms of sale (Art. 56aa, para. 2 of the Bankruptcy Law).

The transparency of the procedure in the event that at least two applications for approval of the terms of sale have been filed is ensured by conducting an auction among potential acquirers. In this way, the most favourable terms of sale are selected (Art. 56ca, para. 1 of the Bankruptcy Law).

Thirdly, some of the new provisions are intended to discourage applications for approval of the terms of sale to delay the pre-pack procedure. The introduction of a deposit in the amount of one-tenth of the offered price serves this purpose. The deposit may be provided in the form of money, bank suretyships or suretyships of a cooperative savings and credit fund, bank guarantees or insurance guarantees (Art. 56a, para. 2a-2aa of the Bankruptcy Law). If the contract of sale is not concluded due to reasons attributable to the acquirer, the trustee keeps the deposit provided in the form of money. If the deposit has been provided in a form other than money, the trustee seeks satisfaction from the object of security (Art. 56e, para. 2a of the Bankruptcy Law).

[6] 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), Official Journal of the European Union, L 172/18, as amended, known hereinafter as the Second Chance Directive. See Art. 6-7 of the Second Chance Directive.

Fourthly, the amendments refer to the conclusion of a sale agreement and regulate the terms on which the application for approval of the terms of sale is approved. The court grants the application for approval of the terms of sale where the price is higher than an amount obtainable in bankruptcy proceedings in the case of liquidation according to general principles, reduced by costs of proceedings and other liabilities of the bankruptcy estate to be incurred in connection with liquidation under that procedure (Art. 56c, para. 1 of the Bankruptcy Law). The court may grant the application for approval of the terms of sale where the price approximates the amount obtainable in bankruptcy proceedings in the case of liquidation according to general principles, reduced by costs of proceedings and other liabilities of the bankruptcy estate to be incurred in connection with liquidation under such procedure, if this is warranted by an important public interest or if the debtor's enterprise could be thus maintained (Art. 56c, para. 2 of the Bankruptcy Law).

The amendments also introduced solutions regarding the deadline for examining the application for approval of the terms of sale. Such examination can be performed by a court not earlier than 30 days from the date of submission of the application. Moreover, this can be performed not earlier than 14 days from the date of delivery to the creditors secured by the assets to which the application relates of copies of the application together with attachments and a document setting out an obligation to take a position within a specified time limit (Art. 56c, para. 3 of the Bankruptcy Law). The latter term is related to the protection of secured creditors. There is the obligation to attach to the application for approval of the terms of sale a list of the securities known to the applicant, established by the creditors on the assets to which the application relates. The court sends a copy of this application, together with appendices, to the creditors secured by the assets to which the application relates (Art. 56a, para. 2b of the Bankruptcy Law). Secured creditors can take a position on the proposals provided for in the application for approval of the terms of sale. Hence the relation between the delivery of the copies of this application and the hearing on the application by the court.

Lawmakers referred to a situation where, if following the issuance of a ruling approving the terms of sale, circumstances with a significant influence on the value of the property asset subject to sale have changed or have been revealed. In such case, the trustee or the acquirer can file with the court an application for setting aside or amending the ruling. It can be done within the time limit fixed for entering a contract of sale (Art. 56h of the Bankruptcy Law).

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> There is a possibility to amend the terms of sale if the circumstances that have an impact on the assets subject to the pre-pack have changed or new circumstances have been identified.


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